INDIAN CAPITAL MARKET: CHALLENGES TO INVESTOR PROTECTION REGIME

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DECLARATION

I declare that the dissertation entitled **"Indian Capital Market: Challenges to Investor Protection Regime"** is the outcome of my own work conducted under the supervision of Asst. Prof. Mr. Sujith P. Surendran, at College of Legal Studies, University of Petroleum and Energy Studies, Dehradun.

I declare that the dissertation comprises only of my original work and due acknowledgement has been made in the text to all other material used.

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B.A., LL.B. (Hons.) (10th Semester) (2011-2016)
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CERTIFICATE

This is to certify that the research work entitled **"Indian Capital Market: Challenges to Investor Protection Regime"** is the work done by **Siddharth Badkul** under my guidance and supervision for the partial fulfilment of the requirement of **B.A., LL.B. (Hons.) with specialisation in Energy Laws** degree at College of Legal Studies, University of Petroleum and Energy Studies, Dehradun.

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ABSTRACT

The Indian market is one of the main and promising emerging security markets in the world. The capital market in its entirety can be sub-divided into Primary market and Secondary market. In the entire structure of Capital market, investor is the primary stakeholder. In India financial regulators, such as the Securities and Exchange Board of India (SEBI)/Reserve Bank of India (RBI) keep an eye on the activities of the capital markets in their designated jurisdictions to ensure that investors are protected against frauds, unfair trade practices and ensuring healthy functioning of the market, among other duties.

An investor should require protection through an external regulatory body, like the SEBI only when the market mechanism collapses due to fraudulent act of some ingenious market players: an unprecedented act, which could not have been reasonably perceived at the time of framing the regulation. The need of protection is also based on the experience that financial investors are usually structurally inferior to providers of financial services and products due to lack of professional knowledge, information or experience. Market manipulation, insider trading and fraudulent practices are, therefore, generally identified as the primary areas of concern in protecting the interests of investors in securities. In order to afford adequate protection to the investors, provisions have been incorporated in different legislations supplemented by many guidelines, circulars and press notes issued by the Ministry of Finance, Ministry of Law, Justice and Company Affairs and SEBI from time to time. The legislations as well as rules and regulations notified there under list out the disclosure requirements to be complied by the companies and also punishments and remedies for failure of compliance.

In light of the aforesaid, the dissertation report centres around the protection of interest of investors in Indian capital market and the role of Securities Exchange Board of India and other regulatory bodies. The report also emphasis on the legal framework and the measures adopted therein; pertaining to the issue and challenges associated therewith. The dissertation report is inspired by the fact that despite of having a history of over 125 years, Indian Capital Market it has the reputation for

being a snake pit, lacking in fairness and integrity, prone to speculative excess and showing scant regard for the interests of small investors.

Keywords: Capital Market, Primary Market, Secondary market, Investor Protection, Securities.

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Siddharth Badkul
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INDIAN CAPITAL MARKET: CHALLENGES TO INVESTOR PROTECTION REIME IN INDIA

INTRODUCTION

The case of ***Inland Revenue Commissioners v. Rolls Royce Ltd*** [1] defined investor protection in generic sense as:

> "The word 'investment', though it primarily means the act of investing, is in common use as meaning that which is thereby acquired; and the meaning of the verb `to invest' is to lay out money in the acquisition of some species of property". [2]

An investor is an individual or institution who invests in the growth of economy and acknowledges the risk associated with his investment as a portion of his savings. The investment is made in those areas that has high probability of growth or in other words the areas that grow in tandem with country's economy or maybe faster.[3]

Investors, if provided with adequate information about the venture in an understandable manner by virtue of an effective regulatory regime; shall be able to take care of his interest. The argument is justified not only in Indian context but also of various other jurisdictions. The USA Securities Act, 1933 and UK Financial Services and Markets Act, 2000 are also enacted with similar intentions.

Therefore, in a capital market, utmost attention should be given to investor protection regime. To warrant investor understands about financial system, they must be empowered and educated about various rights, which will be discussed in the forthcoming chapters. To identify few areas, investors should be accorded protection deceit, misrepresentations, and other frauds.

Certain rights are available with investor by virtue of their investment and the same are contractually protected. These includes disclosure and accounting rules to furnish accurate and appropriated information about the issue, voting rights, etc.

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[1] [1944] 2 All E.R. 340.
[2] JONATHAN FISHER, THE LAW OF INVESTOR PROTECTION3, 3-4 (2nd ed. Sweet & Maxwell 2003).
[3] Vijay Kumar Gaba, *Investor Protection* [2004] 51 SCL 100 (MAG.)

In light of the aforesaid, the dissertation report centres on the protection of interest of investors in Indian capital market and the role of Securities Exchange Board of India and other regulatory bodies. The report also emphasis on the legal framework and the measures adopted therein; pertaining to the issue and challenges associated therewith. The dissertation report is inspired by the fact that despite of having a history of over 125 years, Indian Capital Market lacks integrity and fairness and is prone to scams.

The report is segmented into five chapters. First chapter introduces the capital market in India. It discusses the conceptual and functional aspects of primary and secondary market in India. Second chapter discusses the legal and regulatory framework vis-à-vis investor protection regime in India. It discusses statues, rules and regulations pertaining to same. Third chapter deals with various fronts where investor's interest is protected. It deals with the regulatory measure adopted by the SEBI under various statutes and regulations for protection of interest of investor. Fourth chapter deal with important cases/instances where investor's interest was at stake. The chapter intents to highlight the lacuna under various investor protection practices that eventually gave rise to few serious scams in capital market of India. Chapter 5 discusses various challenges associated with investor protection regime.

RESEARCH METHODOLOGY

STATEMENT OF PROBLEM

This dissertation pertains to the analysis of existing legal framework of investor protection in Indian Capital Market (both primary and secondary market) and investor protection regime in India, the challenges and limitations associated therein. It expresses the concern on the following points:

- Legal framework for addressing the issue of investor protection in India under the following heads and the measures adopted thereunder:
    - The Securities and Exchange Board of India Act, 1992 and policies/regulations/guidelines framed thereunder
    - Securities Contracts (Regulation) Act, 1956
    - Companies Act, 2013
    - Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.
    - Other legislations

- Role of SEBI as sector regulator vis-à-vis investor protection regime, and the limitations and challenges faced by it with regard to protection of Investor's interest in India.
- Practical challenges to investor protection and the lacunas in the existing framework of law and policy with regard to investor protection in India.
- Role and necessity of market reforms in investor protection endeavours.
- Mechanism for redressesing disputes by SEBI related to investment.
- Effect of globalisation of securities market in the investor protection regime.

OBJECTIVE OF STUDY

The objective of report is to analyse the existing legal framework pertaining to investor protection in Indian Capital Market (both primary and secondary market) and to analyse the challenges faced by the investors in primary and secondary capital market for securing their interest and the limitations of law, therein.

SCOPE AND SIGNIFICANCE OF STUDY

- Legal framework for addressing the issue of investor protection in India under the following heads and the measures adopted thereunder:
    - The Securities and Exchange Board of India Act, 1992 and policies/regulations/guidelines framed thereunder
    - Securities Contracts (Regulation) Act, 1956
    - Companies Act, 2013
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    - Other legislations
- Role of SEBI as sector regulator vis-à-vis investor protection regime, and the limitations and challenges faced by it with regard to protection of Investor's interest in India.
- Practical challenges to investor protection and the lacunas in the existing framework of law and policy with regard to investor protection in India.
- Role and necessity of market reforms in investor protection endeavours.
- Mechanism for redressesing disputes by SEBI related to investment
- Effect of globalisation of securities market in the investor protection regime.

RESEARCH QUESTIONS

The research question of the dissertation report is, whether the existing legal framework dealing with investor protection in India is effective while dealing with issues emerging?

While dealing with the aforesaid research question, the following sub issues will be deliberated:

- What is the legal framework for addressing the issue of investor protection in India particularly in the Capital Market?
- What is the role of SEBI as a sector regulator vis-à-vis investor protection regime, and the limitations and challenges faced by it with regard to protection of Investor's interest in India?
- What are the challenges to investor protection and the lacunas in the exiting framework of law and policy with regard to investor protection in India?
- What is the mechanism for redressing disputes by SEBI related to investment?

HYPOTHESIS

The hypothesis of the dissertation report is:

"The current legal framework for investor protection in India is unable to effectively deal with the emerging issues".

METHODOLOGY

In prolongation of the aforesaid objective, the nature of research is purely doctrinal which involve analysis of existing statutory provisions and cases laws as well as analytical methodology is opted to carry out study relying mainly on secondary data which includes journals, articles, commentaries, textbooks, reference books, internet sources, e-books, committee and law commission reports. Citation method used is Bluebook 19th Edition.

The said methodology is preferred, as there are already voluminous literatures and research works available on the particular topic that could come handy in bringing reforms in capital market vis-à-vis investor protection regime. Further, the objective of this dissertation is to analyse the existing legal framework pertaining to investor

protection in Indian Capital Market (both primary and secondary market) and to analyse the challenges faced by the investor protection regime therein.

For the mentioned purpose, the Researcher will analyse the existing legislative provisions, decided judgment, scholarly articles and comments on various areas connected with the issue. Researcher has collected materials from various sources i.e. primary as well as secondary sources available at the UPES Library and UPES online e-resources database.

LITERATURE REVIEW

1. **A.C. Fernando, *Business Environment* (Pearson Edu. 2011).**

Chapter 8 of the book, which is titled as "Corporate Ethics: Investor rights, privileges, problems and protection" emphasize and provide an in-depth study in-depth coverage of all conceivable topics on the subject. It discusses the role and limitations of SEBI as a market regulator in relation to investor protection. It also discusses the problems, which attributes to the poor performance of SEBI in this regard.

2. **Vijay Kumar Gaba, *Investor Protection* [2004] 51 SCL 100 (MAG.)**

The article signifies that present regulatory framework does not distinguish an investor from a speculator, trader, dealer and jobber in securities. The same regulations apply to all these persons. This anomaly has created circumstances where the regulations aimed at protecting the interest of investors are, in fact, affecting them most.

3. **Monica Verma, *Corporate Governance in India: Problems and Prospects,* [2009] 14 CAT 483.**

This article deals with the concept, current practices, effectiveness, core problems and future prospects of corporate governance in India vis-à-vis investor protection. It also suggests ways to ensure to improve the standards of corporate governance in India.

4. **Kiran Mukadam, *Investor Protection: Present Scenario,* 30 TAXMANN ONLINE 285 (2013).**

The article discusses the current scenario of investor protection regime and deals with the steps towards achieving the investor's confidence in the present Indian economy.

It provides a practical description of steps taken under various laws by SEBI to ensure investor's protection in securities market.

5. **Shewta Prashant, *Subhkam Ventures (India) Private Limited V. SEBI: Heralding Good Times for Pipe Deals,* 55 SCL (MAG) 102 (2010).**

This article discusses the ruling by the Securities Appellate Tribunal on the issue : Whether certain capital protection and governance rights sought by private equity investors in a shareholders agreement will tantamount to controlling a listed company in India as well as the impact of the Securities Appellate Tribunal s ruling on the foreign investor community and the Indian legal fraternity?

6. **Shelley Thompson, *The Globalization of Securities Markets: Effects on Investor Protection,* [41(4)] THE INT'L LAWYER 1121, 1121-1144 (2007).**

This article argues that internationally merging markets result in an increased need for investor protection. The current trend, however, is to maintain the sovereign schemes that regulate each market prior to international mergers rather than to combine schemes of investor protection. Globalisation of securities markets will result in more investors, increased likelihood of securities fraud, and a more internationally interdependent market place, all of which lead to an increased need for investor protection.

7. **Dr. K.V.S.N. Jawahar Babu & S. Damodar Naidu, *Investor Protection Measure by SEBI,* [1(8)]ARTH PRABANDH: J. OF ECON. & MGMT. 72, 72-80 (2012).**

It deals with the measures adopted by SEBI under section 11(2) of the SEBI Act and argues that Indian investors have been steadily fleeing the market, despite the apparent spread of 'equity cult', which calls for immediate attention of the apex body to frame and effectively implement the measures to protect the interests of small investors, and restore their confidence in the stock market.

8. **Pranshu Paul, *Conflicts of Jurisdiction Between SEBI and Other Regulators,* [7(2)] I. L. J. (2007).**

The article deals with the conflicts that arise between the Security Exchange Board of India (SEBI) and various other Indian regulators and opines on how these conflicts

may be tackled. It suggests that a single regulatory body may not be the best approach to be considered in India due to the structure that has become so entrenced, in which the best possible solution that can be adopted is one of concurrent jurisdiction or mandatory consultation. This would ensure no jurisdictional clashes occur between the different regulatory agencies and SEBI in the future. However, the same have to be implemented with much caution to ensure that the objective and purpose of stating such jurisdictions by the legislature is not lost.

9. **Ashamol V, Renjith TA & George Joseph,** ***Legal Framework of Initial Public Offering (IPO) Grading in Protection of Investors*** **, [3(9)] J. OF INT'L ACAD. RES. FOR MULTIDISCIPLINARY 225, 225-233 (2015).**

The paper discusses development in the IPO's market in India that took place in 2007 when SEBI introduced the concept of grading of IPO's and made it mandatory from May 1, 2007. SEBI initiated the concept of grading equity issues in order to safeguard the investors' interest. It correlates Securities and Exchange Board of India (Disclosure and investor protection) Guidelines 2000 to the said context.

10. **G Sabarinathan,** ***SEBI's Regulation of the Indian Securities Market: A Critical Review of the Major Developments,*** **[35(4'0] VIKALP 13, 13-26 (2010).**

The article identifies some of the major interventions of SEBI relating to regulatory and other institutional developments of the market and critically examines the economic consequences of the same. Such a stock-taking will enable a well-rounded and objective review of SEBI's performance.

11. **Vidya Sunderam,** ***More Power to SEBI to Tackle Scams - Amendment to Securities Laws in India,*** **53 TAXMANN ONLINE 506 (2015).**

The article discusses the Securities Laws (Amendment) Act, 2014 ("SLAA") as notified by the Government on August 22, 2014 granting more powers to the capital market regulator by amending the Securities and Exchange Board of India Act, 1992, the Securities Contracts (Regulation) Act, 1956 and the Depositories Act, 1996. It article summarises the major changes brought in by the SLAA while analysing their implications.

CHAPTER 1

1. INDIAN CAPITAL MARKET: AN OVERVIEW

1.1.INTORDUCTION

The capital market is an essential part of economy of any nation. This is for the fact that it provides capitalistic support to the enterprises of the country. A number of reforms in the financial sector have significantly affected the working and administration of the capital market in India. The Indian capital market is additionally experiencing auxiliary transition since liberalization. The intent of such reforms is to enhance market effectiveness, make securities exchange exchanges more transparent, control unfair practices and to harmonize the Indian capital market with international standards.[4]

An all-round and well-regulated capital market is required to perform disciplinary allocative function on one hand and equally on the other hand, it must aim to protect the interest of investors viably and proficiently. This will prompt successful in-flow of both foreign and domestic investment opportunities. In India throughout the most recent decade and half, in consonance with the rebuilding of global models of business sector, major authoritative changes have occurred like, liberalization of the economy, integrated capital markets, the expanding predominance of institutional investors, etc.[5]Capacity of undertakings i.e. companies, to mobilize capital at cheap cost is a deciding factor of their competitive as opposed to their rivals; keeping in mind the end goal to perform well in an competitive environment.[6]

Capital market is related to securities market and long-term loan market. It plays an essential role in supplying the much needed long term and mid-term funds to industries while dealing with shares, bonds, stocks and debentures. It is essentially a market mechanism dealing with those who have the funds to invest and those who

[4] Ashish C. Makwana, Role of Foreign Institutional Investors Foreign Institutional Investors in Indian Stock Market (2013) (unpublished Ph.D. thesis, Saurashtra University, Rajkot) (on file with INFLIBNET Centre).

[5]Md. Noor Alam, FII's role in the promotion of Indian capital market (2011) unpublished Ph.D. thesis, Department Of Commerce Aligarh Muslim University Aligarh (India) 2011(on file with INFLIBNET Centre).

[6]A. C. FERNANDO, BUSINESS ETHICS AND CORPORATE GOVERNANCE (2nd ed. Pearson Educ. India 2012).

need reserves i.e. capital for beneficial speculations. The capital market helps financial development by mobilizing the reserve funds i.e. savings to channels of beneficial employments. Corporate entities, therefore, turns to investors for raising funds, adequate to finance for the infrastructural and corporate activities.[7]

Simultaneously, it is wellspring of income for investors. At the point when financial assets of the company multiplies manifold; the investors get wealthier and they tend to regularly spend some of this extra riches to support deals and advancing financial development. The same is also well reflected by the Government policies, as the stock value is responsive to policies adopted by the Government. If the policy embraces arrangements that speculators accept will hurt the economy and organizational benefits, the investment is impacted negatively and vice-versa.[8]

Post-reform, India remains as an economy that is quickly – modernizing, globalizing and developing. Hence, India is a balanced and a quickly developing business sector economy despite the present turmoil and cynicism. The versatility appeared by India originates from the concrete macroeconomic principles. The same has led India to deal with the late financial services crisis appropriately. This has also been the driving factor for encouraging the investment in Capital market, which has eventually enhanced profitability. Additionally, the Government has focused on reforming the fiscal regime and likewise there has been a sharp ascent in net capital inflow in the market. The solid institutional and macroeconomic arrangement system in India is further supplemented by the integration of market globally.[9]

Throughout post-reform years, the capital market has encountered several transitions and therefore, it is now comparable with the capital markets of developed nations. This is regarded as vital, in view of the fact that despite of slow opening of the economy there was a need to develop investment conducive environment. There has been an up-gradation in the legislative and regulatory framework in this regard with a large portion of the force for managing the capital market has been vested with the SEBI as a sector regulator.[10] However, there also exist several other bodies, which play a vital role in regulation of capital market in India and virtually exist as parallel

[7] Ashish, *supra* note 4.
[8] *Id.*
[9] *Id.*
[10] *Id.*

sector regulator. The problem associated with the same shall be discussed in the forthcoming chapters.

Aforementioned reforms and globalization have introduced major changes in the economy of the country. Since the origin changes in the mid 1990's, the execution of different measures, which includes various basic and institutional changes in the distinctive fragments of the financial market, has gotten an emotional change the working of the economy. By and large, the entire paradigm shift has contextually became possible owing to globalisation, amendment in procedures and introduction of new techniques, etc. has brought significant changes in the mode of interaction between investors, corporates and stock markets.[11]

This chapter deal with the overview of capital market vis-à-vis deals with definition, nature, functions, types of markets, etc.

1.2.DEFINITION

Indian capital market, as discussed above, alludes to such organisation that pertains to stock market, investment corporations/institutions, etc., which deals with long term investing or financing and relocate the money thus collected to those who need capital for business. This is essentially the role of Stock market in capital market, which is associated with in paper long-term financing; and over a genuinely long period stretches it and gives it to those who need it. The papers, mentioned herein, are shares and stocks or debentures or bonds. They are additionally known by the term securities, which might be issued by government or public. Public securities are issued by public companies and the Government issues government securities are.[12]

As depicted by S. Mohan, *"Capital market is an organised mechanism for effective and efficient transfer of money capital from the investing class to the entrepreneur class in private or public sector of the economy"*.[13]

Some expert defines capital market as follows:

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[11] *Id.*
[12] S. MOHAN, FINANCIAL SERVICES 93 (Deep & Deep Publications 2008).
[13] *Id.*

H.T.Parikh described Capital market[14] as "By Capital market I mean the market for all the financial instruments, short term and long term as also commercial, industrial and government paper."[15]

Gold Smith defines[16] *"the capital market of a modern economy has two basic functions; first the allocation of savings among users and investments; second the facilitation of the transfer of the existing assets, tangible and intangible among individual economic units."*[17]

Grant defines Capital market[18] in a broad sense as *"a series of channels through which the savings of the community are made available for industrial and commercial enterprises and for public authorities. It embraces not only the system by which the public takes up long term securities directly or through intermediary but also the elaborate network of institutions responsible for short term and medium term lending".*[19]

According to Arun K. Datta[20], "*The capital market is a complex of institutions investment and practices with established links between the demand for and supply of different types of capital gains*".[21]

According to F. Livingston[22] defined the capital market as "*In a developing economy, it is the business of the capital market to facilitate the main stream of command over capital to the point of the highest yield. By doing so it enables control over resources to pass into hands of those who can employ them most effectively thereby increasing productive capacity and spelling the national dividend".*[23]

Therefore, in view of the aforementioned definition, capital market concerns itself with generating of long-term funds and equity funds for government and corporate

[14]*See,* S. MOHAN, FINANCIAL SERVICES 92 (Deep & Deep Publications 2008).
[15]Alam, *supra* note 5.
[16]RAYMOND W. GOLDSMITH, THE FLOW OF CAPITAL FUNDS IN THE POSTWAR ECONOMY 22, 28 (Nat'l Bureau of Econ. Research 1965), http://www.nber.org/chapters/c1680.pdf (last visited Mar. 11, 2016).
[17]Alam, *supra* note 5.
[18]MOHAN, *supra* note 12.
[18]*See,* MOHAN, *supra* note 12.
[19]Alam, *supra* note 5.
[20]ARUN K. DATTA, GOVERNMENT, FINANCE AND CAPITAL MARKET 18 (1st ed. P.G . Book Mart 1963).
[21]*See,* G. RAMESH BABU, FINANCIAL MARKETS AND INSTITUTIONS 57 (1st ed. Concept Publ'g 2006).
[22]F. LIVINGSTONE, THE ENGLISH CAPITAL MARKET (Methuen, London 1929).
[23]Ashish, *supra* note 4.

sector. It thereby, mediates between the conflicting interest of both investors and corporates.[24]

1.3.ROLE OF CAPITAL MARKET VIS-À-VIS INDIAN ECONOMY

Capital, being the *sine qua non* for economic development, integrates the other factors of production. However, the investment of capital it will prompt financial advancement only if channelized into gainful exercises. The securities investment through capital market is the channel through which investible assets are steered to organizations. This is essentially because, through securities market a stock of investible assets are converted into a regular flow of goods and services in the economy. Hence, securities market sector is helpful for economic growth.[25]

Capital business sector assumes a critical part in advancing and maintaining the development of an economy. It is a vital and productive course to channel and prepare assets to endeavours, and give a viable source of interest in the economy. It assumes a basic part in activating the savings and converting it into investment with a perspective to ensure long-term economic growth. It consequently goes about as a noteworthy impetus in changing the economy into a more proficient, inventive and competitive field.[26]

Some roles played by capital market in development of Indian economy are as follows:

1. **Capital arrangement:** Capital market plays a key role in process of capital arrangement in the country. Rate of capital arrangement/development relies on savings of individuals. Since, the mobilisation of reserve fund is not enough to meet the requirements of commercial and industrial sector, hence, the capital market is a platform to activate and relocate the savings of individual and such reserve funds are, thereafter, contributed for gainful purposes in the corporate sector. In this way, investment of capital and venture prompts capital arrangement.[27]

[24]Alam, *supra* note 5.
[25]FERNANDO, *supra* note 6.
[26]Ashish, *supra* note 4.
[27]*Id.*

2. **Economic growth:** The development of industrial sector is ensured; due to the functionality involved in the capital market. Investment through capital market evens the whole process, as the fundamental motivation functioning of capital market is to exchange assets from masses to the industries. The capital markets it conceivable to loan assets to different tasks, both in the public and private segment.[28]
3. **Development of backward areas:** The capital markets give assets for carrying out infrastructural works in remote and backward areas also. This encourages the development in such regions.[29]
4. **Generates employment:** Capital market generates employment in the country:
    i) Direct employment in the capital markets such as stock markets, financial institutions etc.[30]
    ii) Indirect employment in all sectors of the economy, because of the funds provided for developmental projects.[31]
5. **Long-term capital to industrial sector:** Capital market ensures and satisfies the requirement of long-term capital to industries. The generation of fund takes place through issues and thereafter it remains with the company. The organization is never left without assets while investors are permissible to transfer such securities to another, validly under the law.[32]
6. **Generation of foreign capital:** Yet another benefit that the capital market provides to the economy is that, it make it conceivable generate or cause to generate foreign capital. Indian firms can produce capital from abroad markets by subscribing securities of foreign firms.[33]
7. **Developing role of financial institutions:** The different organizations functional in capital market are Industrial Financial Corporation of India (IFCI), State Finance Corporations (SFC), Industrial Development Bank of India (IDBI), Industrial Credit and Investment Corporation of India (ICICI), Unit Trust of India (UTI), Life Insurance Corporation of India (LIC), and so forth. There has been valuable contribution by these organisations to the

[28] *Id.*
[29] *Id.*
[30] *Id.*
[31] *Id.*
[32] *Id.*
[33] *Id.*

development of commercial enterprises. They have been financing, advancing and endorsing capital market.[34]

8. **Investment opportunities**: Capital market is an investment platform for general public by means of investment in bonds, shares, debentures, etc.[35]

Alike money market, capital market is also dichotomous. Analytically, it constitutes two sectors, namely organised and unorganised sector. In organised sector, the demand of capital is mainly satisfied by commercial, governmental and semi-governmental entities. Whereas, in unorganised sector, the supply of capital is met by banking companies, insurance companies, investment companies, financial corporations, global finance agencies.[36]

The demand on behalf of unorganized sector is constituted mostly by moneylenders and bankers (indigenous). On the other hand, the demand in organised sector is utilized as productive investment. Among, numerous reasons, for which finances are extremely hard to get from the organised sector, are financed unorganized sector. The presence of variety and extravagant rates of interest and lack of consistency in their business transactions portray both sectors. Further, organised sector is subjected to regulatory control by government and SEBI. There were several endeavours to cover the unorganised sector under the purview of same set of regulations and control these were not fruitful and this sector is *in toto* beyond the effective control of the government.[37]The organized sector has been subjected to increasing institutionalization. The public sector financial institutions account for a large chunk of the business of this sector.[38]

1.4.KINDS OF CAPITAL MARKET

The Capital Market includes the primary capital business sector and secondary capital business sector. The primary capital market is chiefly utilized for raising fresh capital

[34]*Id.*
[35]*Id.*
[36]FERNANDO, *supra* note 6.
[37]*Id.*
[38]*Id.*

by IPO, rights issue, offer for sale of equity or debt. The secondary market gives liquidity to these instruments, through trading on stock exchanges.[39]

1.4.1. PRIMARY MARKET:

In primary market, Capital is raised by means of rights issues of share, public offers and private placements. Public offer is the biggest wellsprings of capital in primary market for the company. A company, through a prospectus, invites public for subscribing its securities. This methodology is called as public offer done for the purpose of issue of securities to public. It is done, either under a fixed price or through a book building process. Each organization requires short-and in addition long haul money for proceeding with its operations viably. Fleeting fund i.e. the short-term money can be raised through different banks; financial institutions, lender, etc. Long-term funds can be obtained by issue of securities by the company or from other different entities. The underlying mechanism is that, public issue of securities and rights issue can do the issue of initial and subsequent capital in the primary capital market. As discussed above, the initial issue of securities is attributed public by issuing prospectus and in this manner, the public subscribe to such securities as mentioned in the prospectus, straightforwardly. Generally, the company as internal mechanism, issues bonus shares to generation of capital. If there should arise an occurrence of rights issue, existing shareholders are given pre-emptive rights to buy extra/additional securities of the organization. In both instances of rights and bonus issues of securities, the company is obliges to issue such securities to existing holders, as mandated by the provisions of the Companies Act. Bonus shares are primarily issued, by capitalization of reserve balance and undistributed profit of the company. Therefore, the notion of resource mobilization is absent.[40]

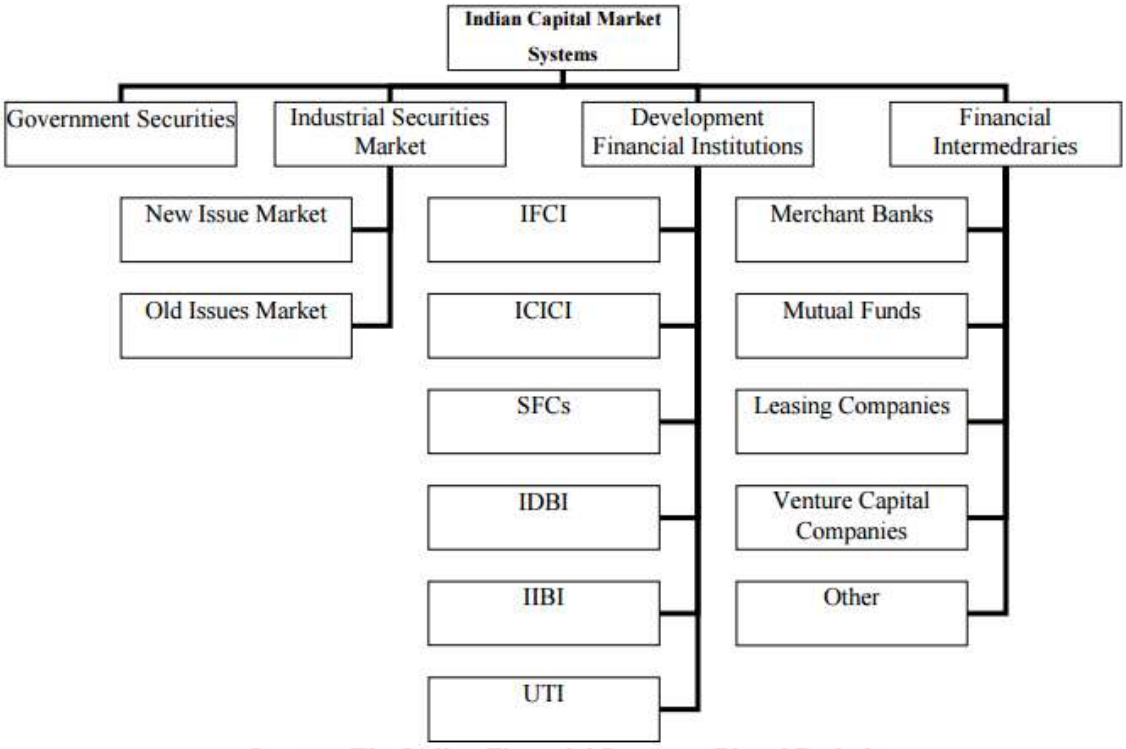
1.4.2. A CONCEPTUAL UNDERSTANDING OF WORKING OF PRIMARY MARKET:

For raising funds, securities are issued unswervingly to investor's (both individual and also institutional). Savings are associated with ventures by an assortment of intermediaries through a chain of financial products named as "securities". In this manner, the primary market, which constitutes the securities for issue, various

[39]Alam, *supra* note 5.
[40]SIDDHARTHA SHANKAR SAHA, INDIAN FINANCIAL SYSTEM AND MARKET 226 (1st ed. Tata McGraw-Hill Educ. Pvt. Ltd., New Delhi 2013).

financial institutions and the regulatory framework associated with them, completes the link for mobilization of funds. The fundamental purpose of capital market is the transfer fund from surplus unit (investors) to the deficit unit (company). Interestingly, this whole mechanism is a platform for companies to sale its securities in order to meet its investment requirements. During this process, it various organisations such the company i.e. issuer, the government play a crucial role or discharge their obligations, as the case may be. Therefore, the investors are not in a beneficial position. Investors are left to their own discretion and make choice as whether to rely on their economy's capacities to contribute as an investor or to save money respectively. This unavoidably upgrades their savings and eventually enhances the investment, thereby beneficial to the economy. The securities which are frequently thought about for raising assets are preference share; equity shares; debentures; bonds; and so forth.[41]

Indian Capital Market Systems



Source : The Indian Financial Systems , Bharti Pathak

[41] *Id.*

1.4.3. FUNCTIONAL ASPECTS OF PRIMARY MARKET

Disintermediation is a process in which the issuer directly accesses the prospective investors for fulfilling their requirement of fund for either expansion or for meeting the working capital needs. Instead, the issuer could also access the financial institutions and banks for funds. In this process, the money flows from investors to banks or financial institutions and then to issuer, hence it is called intermediation. The market in which new securities are issued and investors apply directly to the issuer for their subscription and allotment. In the primary market, the issuer directly contacts the public for gathering capital, whereas in secondary market the investors buy/sells the securities on the stock exchange. The public limited companies and Government organisations issues their securities to investors through a public issue or rights issue in the primary market, thereby adding to their capital base. This enables the issuer to meet their capital requirements for expanding their business, starting a new project, etc. The securities of the issuer are listed on stock exchange(s) after the public issue if it adheres to the requirements as set by stock exchanges.[42]

After this, the securities are traded in the stock market by listing the securities in one or more stock exchange. This enhances the liquidity of the securities which as well as facilitates trading. A public offer is an invitation to the public to buy the equity shares, preference shares or debentures. The issuer has to mention the details about securities intended to be issued in offer documents and so as to access financial viability and risk factor. This enables the investor to take better investment decision.[43]

The company issues a prospectus with the public issue and a letter of offer with the rights issue. This is called as Offer document. It contains information about the business of the company, management, collaborations, dividends, debts, taxation, listing, promoters, BOD and names of underwriters etc.[44]

Hence, the issuer is obliged to make sufficient disclosure in the offer document to enable the investor in arriving at a decision. There are risks associated with issuing of the public issue that it may not attract minimum subscription specified in the prospectus. Some factors like the promoters of the issue, the record of

[42] Alam, *supra* note 5.
[43] *Id.*
[44] *Id.*

accomplishment of the company, size of the issue, nature of the project and its viability etc. decides whether the risk associated with it is high or low. Therefore, here comes the role of underwriters, who are approached by the companies for their services.

The existing holders have the first right to subscribe to the 'Rights Issue'. Cum rights price is the price declared before the entitlement of rights issue and the price declared after the entitlement is called as ex-rights price. The two are differentiated by the market value of right entitlement. An existing holder can renounce his rights in favour of another completing the formality of signing the renunciation form. Thereafter, the company declare its interim and final dividend from the profit on the face value or par value of a share and not on its market price.[45]

A company issues bonus share to its existing shareholders from its reserves in proportion to their holdings to convert its reserves into equity. This can be done by transferring some amount from the reserve account to the share capital account by simply making a book entry. Such shares are issues free and the proportionate holding of shareholders remains same. There is a reduction in the price of shares once the bonus shares are issued.[46]

Steps involved are:

[45] *Id.*
[46] *Id.*

1.4.4. SECONDARY MARKET

The issuer of a company sells the new securities to the public in the primary market in form of IPOs and FPOs. In the secondary capital market, the issued securities are traded. Hence, it is called after market or stock market. The secondary market helps both buyers and sellers to come together and to facilitate the transfer of the securities. In the primary market, the money is directly mobilised from investor to the issuer; whereas in secondary market the funds and securities are transferred from one investor to another. Since the primary market facilitates capital formation in the economy, the secondary market provides liquidity to the securities to the securities, which is beneficial to the interest of shareholders. Thus, a relationship exists between primary and secondary market. In India, the stock market represents the secondary market.[47] Securities Contracts (Regulations) Act 1956 and SEBI Act 1992 regulate and supervise the operations and functions of stock exchanges.[48]

1.4.5. A CONCEPTUAL UNDERSTANDING OF WORKING OF SECONDARY MARKET:

In the secondary market broker facilitates the sale and purchase of securities between investors and company. This enables the investors' asses the risks and return before selling or purchasing securities. The holders can sell their securities in case for meeting their requirements and stock exchange is platform in this regard. The intermediaries assist in the trading of securities, which in turn are traded with the four corners of statutory framework. The procedure takes place under the supervision of SEBI. Therefore, the securities are traded in the secondary market once they are offered to investors in the primary market. Over-the-Counter (OTC) market and the Exchange-Traded market are two methods to suffice this purpose. Most of the trades in the government securities are negotiated in OTC markets. It is a formal market. It facilitates spot trading and ensures quick delivery and payment. Whereas, in the Exchange-Traded such facilities are not available and settlement of transaction takes its due time.[49]

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[47] *Id.*
[48] SIDDHARTHA, *supra* note 40.
[49] *Id.*

1.4.6. FUNCTIONAL ASPECTS OF SECONDARY MARKET

Secondary market or share market involves exchange of securities already sold and listed. Such transactions are effected in accordance with the mandates of SEBI. An investor who wishes to purchase security is required to purchase it through a broker registered under SEBI. Thereafter, the broker acts on behalf of the investor to sell or purchases the security. For its services, the broker is entitled to brokerage. Since in a secondary market existing securities or outstanding securities are traded, an equity investment creates a constant market till maturity period of the securities.

Differently from primary market, in secondary market only marketability and liquidity of existing or outstanding securities takes place. Additionally, it also provides for instantaneous valuation of securities. Secondary capital market is further classifies into: 1. Secondary capital market for corporate and financial intermediaries. 2. Secondary capital market for government securities and public sector bonds.[50]

In secondary market, stock exchange is the platform for selling or purchasing of existing or outstanding securities. The said trading of securities is categorised as exchange of securities in consideration of money amongst investors. It therefore, enables liquidity to securities traded on the exchange(s) prior to the commencement of original issue. For example, if an investor wishes to sell the securities, it is done in secondary market through stock exchanges. Hence, a stock exchange is a prominent institution of secondary market, which provides for exchange of securities. In simple terms, it is place to trade already issued securities. This distinguishes a secondary market from a primary market wherein the securities are issued directly by the issuer to the investor. As mentioned SEBI is a regulator of stock exchanges in India and every stock exchange within the mandates of GoI i.e. SEBI and under the Securities Contracts (Regulation) Act, 1956. Agencies involved are as follows:

[50]Ashish, *supra* note 4.

1.5.DEFICIENCIES IN INDIAN CAPITAL MARKET

The capital market has a technical methodology of functioning and works on various compliance and tracking system. An investor is not proficient to deal with such technicalities. Premier expectation of an investor is to accrue greatest benefits with minimum risks involved in the transactions. Subsequently, the investor makes a decision to invest provided adequate disclosures are made. Hence, in this whole transaction, role of an expert guidance cannot be ruled out.[51]Although several reformatory measures were introduced, yet the Indian capital market suffers from certain deficiencies, which are detrimental to the interest of investors or ipso facto other stakeholders involved in the capital market.

[51]Pooja Singhania, *Wealth Management and Its Regulatory Framework in India*, 41SCL (MAG.) 106 (2011).

Certain inadequacies can be classified are lack of diverse tradable assets, improper disclosure by companies and lack of regulatory control over it, issues related to secondary markets, insider trading, market price manipulation, unorganised segment in primary market and lack of regulatory control in it, failure of financial institutions in checking acts of neglect, etc. In pre-liberalisation period when the stock exchanges had the residuary part to play, these lacunas were not of much significance. However, in a market driven economy towards which we are moving, capital market sector is relied upon to perform diverse and multifaceted tasks. The argument becomes significant, firstly, owing to increasing role of private sector in the economy, which automatically implies an increasing demand of equity finance. Secondly, the investors must be able to diversify their savings through investment in a variety of assets. Thirdly, the stock market, as opposed to residuary role must perform the role of monitor. Therefore, for a financial system to function efficiently, it is a pre-requisite to drive the financial sector institutions efficiently. In perspective of its significance, various shortcomings and inadequacies prevalent in the capital market prevents it to work at an expected level.[52]

[52] FERNANDO, *supra* note 6.

CHAPTER 2

2. LEGAL REGULATORY FRAMEWORK

Apart from Securities Exchange Board of India, few other bodies also regulates the securities market in India. These chiefly include Department of Company affairs under Ministry of Corporate Affairs, Department of Economics Affairs and the Reserve bank of India. The previously mentioned bodies coordinate their activities by means of a high-level committee on capital and financial markets.[53]

The primary regulator of capital market is SEBI. The SEBI has full independence and power to control and build up the capital market in a manner consistent with the SEBI Act and other concerned laws. Standards governing the capital market are defined under Securities Contracts Act (SCRA), the SEBI Act and the Depositories Act. SEBI concurrently exercised jurisdiction over matters and transactions pertaining to sale and purchase of securities in money market, government securities and ready forward contract. The four main legislations governing the capital market are:

1. The SEBI Act, 1992 operates on three pillars. Firstly, protection of investor's interest. Secondly, development and regulation of securities market and thirdly to deal with matters incidentally connected with capital market.[54]
2. The Companies Act, 2013 which includes in its domain matters pertaining to issue, allotment and transfer of securities, disclosures requirements, underwriting, rights and bonus issues and payment of interest and dividends.[55]
3. The Securities Contracts Regulation Act, 1956 prescribes norms for regulations of management of stock exchanges and mechanism of securities trading.[56]
4. The Depositories Act, 1996.

[53] Shaik Abdul Majeeb Pasha, *A Study on Role of SEBI in Indian Capital Market: An Empirical Analysis*, [2(3)] INT'L J. OF MULTIDISCIPLINARY RES.396, 397 (2012) *available at*http://zenithresearch.org.in/images/stories/pdf/2012/March/ZIJMR/30_ZEN_VOL2_ISSUE3_MARCH12.pdf (last visited Mar. 12, 2016).
[54] Ashish, *supra* note 4.
[55] *Id.*
[56] *Id.*

It is vital to guarantee fluent working of capital market as it is proximately connected to the economic development of the nation. Various laws were adopted and reformatory measures were taken to deal with the issue. Prior to 1992-93, the financial market was segmented. However, the establishment of SEBI was the foundation of step for post-modern and current scenario of capital market in India

SEBI was initially setup as an administrative arrangement before SBI Act was enacted to provide it a statutory status. SEBI has been vested the majority of the powers mentioned under the Securities Contract Regulation (SCR) Act, which included stock exchanges, brokers, etc. under the domain of SEBI. It has likewise been designated with powers enshrined under the Companies Act. Apart from the power to regulate takeovers, registration of intermediaries, stockbrokers, venture capital funds, mutual funds, etc. SEBI is additionally empowered issue mandates to any company or individual related to issue of capitals, disclosure, and transfer of securities. It likewise has forces to investigate books and records, suspend and cancel registration.[57]

2.1.SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992.

Section 3[58] of the Act provides for establishment of SEBI. It shall be a body corporate with perpetual succession and a common seal. The Head Office of the board shall be at Mumbai though it may establish its officers at other places in India.[59]

Under section 12 of the Act, "No stock broker, sub-broker, share transfer agent, banker to an issue, trustee of trust deed, registrar to an issue, merchant banker, underwriter, portfolio manager, investment adviser and such other intermediary who may be associated with securities market shall buy, sell or deal in securities except under, and in accordance with, the conditions of a certificate of registration obtained from the Board in accordance with the regulations made under this Act"[60]

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[57] Rabi Narayan Kar, *Indian Capital Market and Regulatory Framework: Background, Performance and Emerging Issues*, available at http://www.icsi.edu/docs/webmodules/Programmes/31NC/INDIANCAPITALMARKETANDREGULATORYFRAMEWORK-RABINARAYANKAR.doc

[58] The Securities Exchange Board of India Act, 1992, No. 15 of 1992, § 3, *available at* http://indiacode.nic.in/

[59] MOHAN, *supra* note 12.

[60] The Securities Exchange Board of India Act, 1992, No. 15 of 1992, § 12, *available at* http://indiacode.nic.in/

Hence, the aforesaid intermediaries associated with the securities market are required to be registered with SEBI.[61]

Section 11(1) of the SEBI Act, 1992 is aimed to facilitate the objective of the act i.e. to protect investor's interest and regulate and promote securities market in India, by taking appropriate measure under the section. These measures provided under Section 11(2) are:[62]

"(a) regulating the business in stock exchanges and any other securities markets;

(b) registering and regulating the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers and such other intermediaries who may be associated with securities markets in any manner;

(ba) registering and regulating the working of the depositories 2[, participants], custodians of securities, foreign institutional investors, credit rating agencies and such other intermediaries as the Board may, by notification, specify in this behalf;

(c) registering and regulating the working of 3[venture capital funds and collective investment schemes], including mutual funds;

(d) promoting and regulating self-regulatory organizations;

(e) prohibiting fraudulent and unfair trade practices relating to securities markets;

(f) promoting investors' education and training of intermediaries of securities markets;

(g) prohibiting insider trading in securities;

(h) regulating substantial acquisition of shares and takeover of companies;

(i) calling for information from, undertaking inspection, conducting inquiries and audits of the 4[stock exchanges, mutual funds, other persons associated with the

[61] MOHAN, *supra* note 12.
[62] *Id.*

securities market], intermediaries and self-regulatory organizations in the securities market;

(ia) calling for information and records from any person including any bank or any other authority or board or corporation established or constituted by or under any Central or State Act which, in the opinion of the Board, shall be relevant to any investigation or inquiry by the Board in respect of any transaction in securities;

(ib) calling for information from, or furnishing information to, other authorities, whether in India or outside India, having functions similar to those of the Board, in the matters relating to the prevention or detection of violations in respect of securities laws, subject to the provisions of other laws for the time being in force in this regard:

Provided that the Board, for the purpose of furnishing any information to any authority outside India, may enter into an arrangement or agreement or understanding with such authority with the prior approval of the Central Government;

(j) performing such functions and exercising such powers under the provisions of 7[* * *] the Securities Contracts (Regulation) Act, 1956 (42 of 1956), as may be delegated to it by the Central Government;

(k) levying fees or other charges for carrying out the purposes of this section;

(l) conducting research for the above purposes;

(la) calling from or furnishing to any such agencies, as may be specified by the Board, such information as may be considered necessary by it for the efficient discharge of its functions;]

(m) performing such other functions as may be prescribed."[63]

[63] The Securities Exchange Board of India Act, 1992, No. 15 of 1992, § 11(2), *available at* http://indiacode.nic.in/

2.1.1. SEBI'S POWER VIA-A-VIS SECURITIES CONTRACTS (REGULATION) ACT, 1956

Certain amendments were made to Securities Contracts (Regulation) Act, 1956 with intent to empower SEBI to exercises powers in the securities market as a full-fledged sector regulator. Prior to the amendment, Central Government exercised the same. SEBI is thus empowered to:[64]

1. "Every recognised stock exchange shall furnish to the Securities and Exchange Board of India such periodical returns relating to its affairs as may be prescribed."[65]
2. Mandate or prescribe every recognised stock exchange to maintain and preserve books of account and other concerned documents.[66]
3. Call upon informations pertaining to affairs of the stock exchange or any member(s) any member thereof, from a recognised stock exchange. Additionally, it may appoint a person to conduct enquiry into the affairs of stock exchange or any members.[67]
4. Approve byelaws of stock exchange(s).[68]
5. Amend byelaws of stock exchange(s).[69]
6. Licensing of dealers in securities in certain areas.[70]
7. "Where securities are listed on the application of any person in any recognised stock exchange, such person shall comply with the conditions of the listing agreement with that stock exchange."[71]

It is an enabling provision, wherein, the Central Government, which are exercisable by Central Government under the Act, vests SEBI with certain powers. The delegated powers are subject to the conditions provided under the Act. However, the delegation

[64] MOHAN, *supra* note 12.
[65] Securities Contracts (Regulation) Act, 1956, No. 42 of 1956 § 6(1), *available at* http://indiacode.nic.in/
[66] *Id.*, § 6(1).
[67] *Id.*, § 6(2).
[68] *Id.*, § 9.
[69] *Id.*, § 10.
[70] *Id.*, § 17.
[71] *Id.*, § 21.

of power is not absolute and that such powers can be withdrawn (the argument is not feasible to be implemented). In effect, following powers has been delegated:[72]

1. Power to grant recognition to a stock exchange, under section 4.
2. Furnishing of Annual Report, under section 7.
3. Power to direct any stock exchange to amend the rules relating to the constitution of Stock exchange, which includes, admission of new member, readmission of members, qualification, suspension/expulsion, etc. of members of any stock exchange, under section 8.
4. Power to supersede governing body of any stock exchange, under section 11.
5. Power to suspend business of a recognized stock exchange, under section 12.
6. Power to prohibit contracts in certain cases, under section 161.

2.1.2. SEBI'S POWER VIS-A-VIS COMPANIES ACT.

Notwithstanding, the powers conferred under the SEBI Act and SCRA, SEBI has been vested with additional powers under Companies Act. In such matters the violation of which can be tried by the SEBI. These include the power to punish if an application is not accompanied by memorandum stating the salient features of prospectus. If the experts mentioned in the prospectus are linked to the formation and management of the company. If the shares are not issued within 3 months their allotment or if the shares are transferred within 2 months of their allotment. [73]

2.1.3. POWER TO REGISTER AND REGULATE INTERMEDIARIES OPERATION.

Regulation of various intermediaries in primary and secondary market in under the prime dominion of SEBI. For this purpose, SEBI has formulated Securities and Exchange Board of India (Intermediaries) Regulations, 2008. These regulations permit the SEBI to register such intermediaries and also to assess the working of the. The given underneath graph demonstrates the classes of Market Intermediaries functioning under SEBI.[74] As per Regulation 2(g), an intermediary includes same person(s) or entities as mentioned under Section 11(2)(b) and in Section 11(2)(ba) of SEBI Act.

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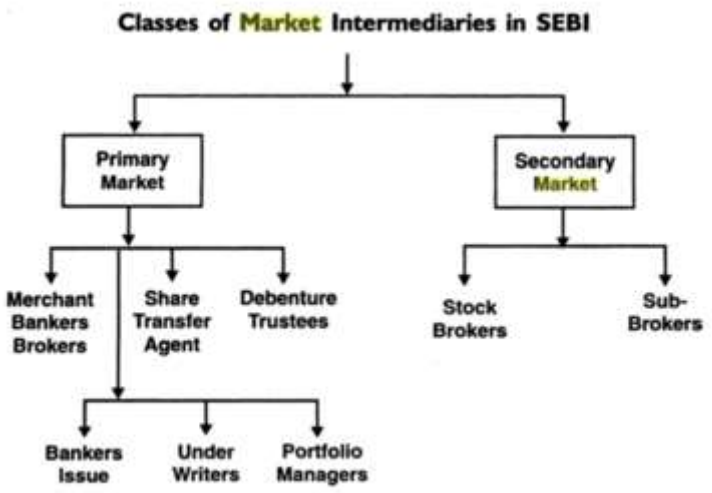
[72] MOHAN, *supra* note 12 at 76-77.
[73] *Id.* at 77.
[74] *Id.* at 77-78.



Source: Financial Services by S. Mohan

2.1.4. SECURITIES AND EXCHANGE BOARD OF INDIA (DISCLOSURE AND INVESTOR PROTECTION) GUIDELINES, 2000.

The Guidelines were framed to ensure that an issuer discloses certain vital information at the time of issue of securities, as long as the securities are listed in the stock exchange. The parameters for these divulgences including the time and mode of disclosures have been incarnated under the Companies Act and SEBI DIP Guidelines, Listing Agreement, Regulations in takeover, insider trading, et al. The motive for framing such these guidelines was *inter alia* investor protection. These mandatory revelations under the DIP Guidelines are made through different prospectus, advertisements, documents, annual report and quarterly statements, etc. spread through mass media, internet, websites of companies and stock exchanges and via EDIFAR (Electronic Data Information Filing and Retrieval) system maintained by SEBI. The disclosure pertains to information on shareholdings, substantial acquisition, financial performance, audit, buy back of shares, corporate governance, risk management, etc. All listed companies and organisations associated with securities markets are obliged to abode by SEBI DIP Regulations.[75]

[75] A. C. FERNANDO, CORPORATE GOVERNANCE: PRINCIPLES, POLICIES AND PRACTICES (2nd ed. Pearson Educ. India 2011).

SEBI framework for disclosure of essential information to public was periodically upgraded by introduction of new amendments to meet and manage repudiations of the Act, instances of malpractices and "to protect the Interest of Investors and Shareholders". These rules have been reconsidered and merged in mid-2000 as SEBI (Disclosure and Investor Protection) Guidelines, 2000.[76] These were issued by the Securities and Exchange Board of India under Section 11 of the Securities and Exchange Board of India Act, 1992.

On January 25, 2005, the SEBI (Disclosure and Investors Protection) Guidelines, 2000 were amended to include disclosures, uniformity, readability while balancing the interest of both investors and corporate. It enabled corporate to lessen size of advertisement, decide on its numbers of managers, etc. [77] The guidelines were further amended and were later replaced by 2009 guidelines.

2.1.5. SECURITIES AND EXCHANGE BOARD OF INDIA (ISSUE OF CAPITAL AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2009

Previously, SEBI (DIP) Guidelines 2000 dealt with the issue of securities. Presently, SEBI DIP Guidelines are supplanted by SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009. Under Rule-3, SEBI (ISSUE OF CAPITAL AND DISCLOSURE REQUIREMENTS) REGULATIONS, 2009, the regulations are applicable on

"3. Unless otherwise provided, these regulations shall apply to the following:

(a) a public issue;
(b) a rights issue, where the aggregate value of specified securities offered is fifty lakh rupees or more;
(c) a preferential issue;
(d) an issue of bonus shares by a listed issuer;
(e) a qualified institutions placement by a listed issuer;

[76] Sunil Kumar, Protection of Investors and Shareholders: A Critical Study of Role of SEBI (June, 2011) (unpublished Ph.D. thesis, Faculty of Law Maharshi Dayanand University, Rohtak) (on file with INFLIBNET Centre).
[77] Prakash Pandey, *Comments on Amendments to SEBI (DIP) Guidelines, 2000,* 59 SCL (MAG.) 22 (2005).

(f) an issue of Indian Depository Receipts"[78]

Primary market is a platform for generating capital for companies by means of sale of securities. The capital mobilised is required for new projects and in addition to existing projects with a perspective develop, modernise, diversify and upgrade the industry.[79]

SEBI's role is critical and imperative with respect to disclosure. Any organization making an IPO is required to document of draft offer with SEBI. If the issue size is upto 100 crore, the draft offer document is to filed with concerned RO of SEBI under whose jurisdiction the registered office of the company is located. Authorities of SEBI at different levels inspect the consistencies in it with SEBI ICDR Regulations 2009 to secure the compliance and ensure that all vital information is unveiled. SEBI observation letter, thus issues, is valid for a period of 3 months; the company needs to open its issue within this period.[80]

DISCLOSURE NORMS UNDER THE REGUALTIONS

i. PUBLIC OFFER:

As per Regulation 9(1) "The draft offer document filed with the Board shall be made public, for comments, if any, for a period of at least twenty one days from the date of such filing, by hosting it on the websites of the Board, recognised stock exchanges where specified securities are proposed to be listed and merchant bankers associated with the issue".[81]

It indicates to the first document filed by the company with SEBI and stock exchanges. It is subjected to the approval of them who after the filing of the same scrutinize it and convey their observations to the company. The company is obliged to include their observations in offer document. The same must be published by the issuer in one English national daily newspaper, one Hindi national daily newspaper

[78] SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009, Reg. 3, *available at* http://www.incometaxindia.gov.in/pages/rules/sebi-issue-capital-disclosure-requirement.aspx
[79] Sunil, *supra* note 76.
[80] *Id.*
[81] SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009, Reg. 9, *available at* http://www.incometaxindia.gov.in/pages/rules/sebi-issue-capital-disclosure-requirement.aspx

and one regional language newspaper in the manner provided under Regulation 9(3).[82] The objective of making an offer document public is to invite public comments.[83]

ii. RED HERRING PROSPECTUS

A red herring prospectus (RHP) filed with SEBI as a preliminary registration document. It is filed in a case of bookbuilding issue wherein neither the number of share nor the details are mentioned. *Ipso facto,* the lower limit and the upper limit of price bands are not disclosed. However, the issuer undertakes to determine and disclose the same later.[84]

RULES GOVERNIGN DISCLOSURES

As per Schedule VIII, SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 following instructions govern disclosure.

"(*1*) *Instructions:*

(a) Only relevant and updated information and statistics shall be disclosed in the offer document. Further, the source and basis of all statements or claims made shall be disclosed. Terms such as "market leader", "leading player", etc. shall not be used unless they can be substantiated by proper source of information, which shall be disclosed.

(b) All blank spaces in the draft offer document shall be filled up with appropriate data before registering the offer document with the Registrar of Companies or filing the same with the recognized stock exchanges.

(c) Simple English for easy understanding of the contents of the offer document may be used. The technical terms used in explaining the business of the issuer may be clarified using simple terms to ensure better understanding by investors.

[82] Sunil, *supra* note 76.
[83] *Id.*
[84] *Id.*

(d) Wherever it is mentioned in the offer document that details are given elsewhere in the document, the same shall be adequately cross-referenced by indicating the page and paragraph numbers.

(e) The offer document should not make any forward-looking statements that cannot be substantiated.

(f) Consistency may be ensured in the style of disclosures. If first person is used, the same may be used throughout. Sentences that contain a combination of first and third persons may be avoided.

(g) The issuer shall ensure that all material matters informed or reports circulated prior to the issue or thereafter by the issuer or any person on its behalf or attributed or attributable to the issuer having a material bearing in taking an informed decision shall also be covered in the offer document, except to the extent specifically disallowed under the regulations.

(h) The issuer shall ensure that in the document of the Red Herring Prospectus, the document shall only be referred to as 'Red Herring Prospectus' or 'RHP'."[85]

PRICING

Since 1992, companies have been permitted to uninhibitedly value their issues. SEBI does not assume any part in this process. However, the companies are mandated to justify the price band. The company is required to reveal in insight about the qualitative and quantitative variables in justification of issue price.[86]

2.1.6. SECURITIES AND EXCHANGE BOARD OF INDIA (SUBSTANTIAL ACQUISITION OF SHARES AND TAKEOVERS) REGULATIONS, 2011.

The takeover code guarantees those shareholders are accorded with fair and equitable treatment in connection to: (a) substantial acquisition, or (b) where the takeover of a listed company is done where they are shareholders. The takeover regulations

[85] SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009, Sch. II, *available at* http://www.incometaxindia.gov.in/pages/rules/sebi-issue-capital-disclosure-requirement.aspx
[86] Sunil, *supra* note 76.

mandate that the dissenting shareholders be provided with an exit opportunity in case of change in control or management of the company or in case of substantial acquisition. The code put-forth an affirmative obligation on the acquirer to provide an exit opportunity by undertaking an open offer to the shareholders of Target Company in the abovementioned circumstances.[87]

1. REGULATION 3: SUBSTANTIAL ACQUISITION OF SHARES OR VOTING RIGHTS.

"3. (1) No acquirer shall acquire shares or voting rights in a target company which taken together with shares or voting rights, if any, held by him and by persons acting in concert with him in such target company, entitle them to exercise twenty-five per cent or more of the voting rights in such target company unless the acquirer makes a public announcement of an open offer for acquiring shares of such target company in accordance with these regulations.

(2) No acquirer, who together with persons acting in concert with him, has acquired and holds in accordance with these regulations shares or voting rights in a target company entitling them to exercise twenty-five per cent or more of the voting rights in the target company but less than the maximum permissible non-public shareholding, shall acquire within any financial year additional shares or voting rights in such target company entitling them to exercise more than five per cent of the voting rights, unless the acquirer makes a public announcement of an open offer for acquiring shares of such target company in accordance with these regulations:

Provided that such acquirer shall not be entitled to acquire or enter into any agreement to acquire shares or voting rights exceeding such number of shares as would take the aggregate shareholding pursuant to the acquisition above the maximum permissible non-public shareholding. Explanation. — For purposes of determining the quantum of acquisition of additional voting rights under this sub-regulation,—

(i) gross acquisitions alone shall be taken into account regardless of any intermittent fall in shareholding or voting rights whether owing to disposal

[87] Rushab S. Dhandokia, *Dynamics of Control Under SEBI Takeover Regulations, 2011*, 44 TAXMANN ONLINE 97 (2014).

of shares held or dilution of voting rights owing to fresh issue of shares by the target company

(ii) In the case of acquisition of shares by way of issue of new shares by the target company or where the target company has made an issue of new shares in any given financial year, the difference between the preallotment and the post-allotment percentage voting rights shall be regarded as the quantum of additional acquisition.

(3) For the purposes of sub-regulation (1) and sub-regulation (2), acquisition of shares by any person, such that the individual shareholding of such person acquiring shares exceeds the stipulated thresholds, shall also be attracting the obligation to make an open offer for acquiring shares of the target company irrespective of whether there is a change in the aggregate shareholding with persons acting in concert."[88]

2. REGULATION 4: ACQUISITION OF CONTROL.

"4. Irrespective of acquisition or holding of shares or voting rights in a target company, no acquirer shall acquire, directly or indirectly, control over such target company unless the acquirer makes a public announcement of an open offer for acquiring shares of such target company in accordance with these regulations."[89]

3. REGULATION 7: OFFER SIZE.

"7. (1) The open offer for acquiring shares to be made by the acquirer and persons acting in concert with him under regulation 3 and regulation 4 shall be for at least twenty six per cent of total shares of the target company, as of tenth working day from the closure of the tendering period:

Provided that the total shares of the target company as of tenth working day from the closure of the tendering period shall take into account all potential increases in the number of outstanding shares during the offer period contemplated as of the date of the public announcement:

[88] Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, Reg. 3 available at http://www.amt-law.com/pdf/bulletins11_pdf/India_20121115_4.pdf
[89] *Id.*, Reg. 4.

Provided further that the offer size shall be proportionately increased in case of an increase in total number of shares, after the public announcement, which is not contemplated on the date of the public announcement."[90]

The duty to make an open offer, therefore, arises in two conditions – (1) when there is a takeover, *i.e.,* when there is change in 'control' of the public company and (2) when there is substantial acquisition of shares.[91]

Hence, it can be construed from the provision that the threshold for making an open offer when there is substantial acquisition of shares in the public is 25% of the shares or voting rights by the acquired in the target company. There isn't much ambiguity, but the chances of variable constructions arises the acquisition amounts to direct or indirect 'change in management control' of the company?[92]

In context of old takeover code, while interpreting the term control, the SAT in the case of ***SMS Holdings Pvt Ltd. v. SEBI***[93] observed that the word control sufficiently leaves a scope to the enforcement authority (i.e. discretion) to arrive at a decision of existence of *de facto* control.[94]

In ***M. Velayudhan v. Registrar***[95]**,** the Hon'ble High Court of Kerala highlighted a pragmatic aspect and held that to enable control over the Board of directors of a company, sufficient share capital can be acquired in it. However, it is equally possible that control over BoD can be acquired without acquiring substantial share capital. This may happen by virtue of an agreement, wherein the acquirer company advances fund to the target company under a valid agreement and in consideration of the same, the target company surrenders its share capital, thereby obtaining control over BoD of target company.[96]

[90] *Id.*, Reg. 7.
[91] Rushab, *supra* note 87.
[92] *Id.*
[93] (2004) 49 SCL 117(SAT)
[94] *Id.*
[95] (1980) 50 Comp Cas 33 (Ker).
[96] *Id.*

SALIENT FEATURES RELATING TO PROTECTION OF INVESTOR'S INTEREST UNDER TAKEOVER CODE.

i. ***Protective Rights vis-à-vis Controlling Rights -***

While making an investment, it is generally observed that, the investors successfully negotiate some substantive rights, including rights to affect major decision-makings. Although it is pervasive to always term these rights as 'protective rights' as it marginally differs from controlling rights. It is an accepted notion that, BoD controls a company and if the shareholders are in a position to appoint maximum director amongst them, it is evident that they would be in "control" of the organization.

Besides, if such rights are coupled with voting rights of shareholders in the company, arguably, he will be in position to control the strategic decision making of company, thereby, he would be considered to be in control of the company. This part illuminates about the basic rights amid negotiations, which apparently becomes a condition for investment.

ii. ***Board seats and Quorum –***

Subject to holding a minimum percentage of shares in the share capital of the company, the investors are usually able to secure a right to nominate an individual in the BoD of company. Such nominee is empowered to vote in meetings of BoD. In certain cases, the right extends to involvement of investor in committees of company and vote thereto. This guarantees that what can be possibly done at board level is rather done at the Committee's level; and the investor remains updated of the fact. The principal objective of conferring such rights is to ensure shareholder's participation in the governance of company.

iii. ***Affirmative Voting Rights or Veto Rights***

Affirmative voting rights provides security to minority shareholders. It functions as a blocking as it prevents the BoD to pass a resolution against the consent of minority shareholders.

It is general principles that, company's decision are taken by majority rule. This implies that under conventional circumstances wills of majority prevails in decision making, for they are holding more than 51% of the shares in the organization. Hence, veto rights are granted to equity investors as a prerequisite of investment.

Such rights are negotiated and forms part of shareholder's agreement. Veto rights are advantageous to private equity investors, who may not generally have any impact over decisions of BoD. Shareholder's agreement contains a list of matters and choices and put-forth the procedure to obtain shareholder's accent.

The object of conferring such rights is precisely that the company must take any decision that may result in change in current position of the company without the knowledge and approval of investors. Simultaneously, it guarantees good standards of corporate governance. Lastly, the existence of such rights is dependent upon the notion of 'control'.

iv. *Standstill Provisions* -

Again, this provision also exist a covenant in shareholder's agreement. The objective of its inclusion is that promoters do not alter the essential share of the company, which is the basic contours of investment, or deviate from the basis of investment. The provision is short lived and it terminates once the venture is made.

Judicial Precedents

Rhodia S.A v. SEBI[97] - In this case SAT ruled that Rhodia, controlled the management and affairs Danube, although it was not a shareholder. In context of the factual matrix of the case, it was observed that such a power vested with Rohida due to the veto rights vested in it in almost all major matters viz payment of dividends, issue of securities, acquisition and disposal of assests. Additionally, it funded Danube completely. Hence, it was concluded that, under the said circumstances, it couldn't be said that Rhodia didn't had the ability to control the affairs of Danube. Furthermore,

[97] [2001] 34 SCL 597 (SAT - Mum.)

the degree of control exercised by Rhodia was beyond what was agreed as affirmative veto rights.[98]

***Gujarat Ambuja's Case*[99]-** The case contains few landmark observations with regard to the interpretation of the term control. As per the facts of the case, there was an acquisition of shares of 14.45% by Ambuja Cement Holding Ltd. in the target company ACC. SEBI held that, in this case, there neither regulation 10 none 12 of the Takeover Code 1997 are violated. SAT in appeal made few important observations, which are compiled as under:

With regard to the corporate control practice in India, the ground reality is that most companies are de facto controlled by person who are in majority shareholders. Additionally, at least 50% plus majority required to appoint majority of directors, therefore, only a few companies in India can lay such claims. Further, the notion "control" is profoundly surrounded by the contractual covenants imposed by the company. However, the fact remains that a company can be controlled by even minority shareholdings (as low as 10-15 per cent) by means of influencing the constitution of BoD and formulating key policies, thereto. This becomes a reality even when the true test of "control" is satisfied.[100]

SAT further observed that, designation is merely a role that one individual plays in the management of the company and hence it is not a deciding factor for exercise of control. Nothing, therefore, can be deduced from the assertion that since the company is managed professionally and hence nobody has control over it.[101]

The SAT observed that, if the concept of control were narrowly interpreted, the whole object of the act would be frustrated.[102] SAT cited Wembly and observed that, "sometimes persons in a position to exercise the majority voting power may hold a minority even a very small position of the equity."[103]

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[98] *Id.*
[99] *Ashwin K. Doshi v. Securities and Exchange Board of India*, Appeal No.44/2001 SAT Mumbai.
[100] Rushab, *supra* note 87.
[101] *Id.*
[102] *Id.*
[103] *Ashwin, supra* note 99.

Citing Prof R. K. Hazari's "the structure of the Corporate Private Sector" (Allied publishers), SAT observed, "in fact, if the shareholding is widely dispersed, even a fractional holding of equity can suffice to ensure control over the company".[104]

Jet-Etihad deal **-** This is a situation where the foreign investor does not want to trigger an open offer and therefore does not want control. However, it wants the right to appoint directors in BoD and to every board committee, want its directors to count as quorum at BoD and shareholders meeting, a right to appoint vice chairman, appoint an auditor, and many other rights. Such rights would enable him to take control of the company.[105]

2.1.7. SECURITIES AND EXCHANGE BOARD OF INDIA (PROHIBITION OF INSIDER TRADING) REGULATIONS, 2015.

SEBI (Prohibition of Insider Trading) Regulations, 2015 has come into force with effect from 15th May, 2015. It replaces the Regulations of 1992, which was amended in 2002. The regulation was originally publicized as, SEBI (Insider Trading) Regulations, 1992 and later amended to SEBI (Prohibition of Insider Trading) Regulations, 1992 on 20.02.2002. The regulation of 2015 is with the same name and style with 2015 substitution of 1992.[106]

The Regulations of 2015 includes the following:

Regulation 2 (1) (g) defines an insider as:

"insider means any person who is:

(i) a connected person; or

(ii) In possession of or having access to unpublished price sensitive information."[107]

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[104] *Id.*
[105] Rushab, *supra* note 87.
[106] Saibal Chandra Pal, *SEBI (Prohibition of Insider Trading) Regulations, 2015 & Companies Act, 2013* (May 18, 2015), *available at* http://taxguru.in/company-law/sebi-prohibition-insider-trading-regulations-2015-companies-act-2013.html
[107] SEBI (Prohibition of Insider Trading) Regulations, 2015, Reg. 2(1)(g), *available at* http://www.sebi.gov.in/cms/sebi_data/attachdocs/1421319519608.pdf

"Note included under the provision states that since " generally available information" is defined, it is intended that anyone in possession of or having access to unpublished price sensitive information should be considered as " insider" regardless of how one came in possession of or having access to such information. Various circumstances are provided for such a person to demonstrate that he has not indulged in insider trading. Therefore, this definition is intended to bring within its reach any person who is in respect of or has access to unpublished price sensitive information. The onus of showing that a certain person was in possession of or had access to company, or who has received or has had access to such unpublished price sensitive information may demonstrate that he was not in such possession or that he has not traded or he could not access or that his trading when in possession of such information was squarely covered by the exonerating circumstances."[108]

Regulation 2 (1) (l) defines "***trading*** *to mean and include subscribing, buying, selling, dealing or agreeing to subscribe, buy, sell, deal in any securities and `trade' shall be construed accordingly."*[109]

"Note: Under the parliamentary mandate, since S 12A (e) and S 15G of the Act employs the term `dealing' in Securities it is intended to widely define the term `trading' to include the dealing. Such a construction is intended to curb the activities based on unpublished price sensitive information which are strictly not buying, selling or subscribing such as pledging etc., when in possession of unpublished price sensitive information."[110]

Regulation 2 (1) (n) defines "*unpublished price sensitive information* as *any information, relating to a company or its securities, directly or indirectly, that is not generally available which upon becoming generally available, is likely to materially affect the price of the securities and shall, ordinarily including but not restricted to , information relating to the following :*

(i) financial results,

(ii) dividends,

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[108] *Id.*
[109] *Id.*, Reg 2(1) (l).
[110] *Id.*

(iii) change in capital structure,

(iv) mergers, de-mergers, acquisition, delistings, disposals and expansion of business and such other transaction;

(v) changes in key managerial personnel ; and

(vi) material events in accordance with the listing agreement."[111]

"Notes : It is intended that information relating to a company or securities that is generally available would be unpublished price sensitive information if it is likely to materially affect the price upon coming into the public domain. The types of matters that would ordinarily give rise to unpublished price sensitive information have been listed above to give illustrative guidance to unpublished price sensitive information."[112]

S 2 (1) (d) defines `*Connected Person*' as :

"(i) *any person who is or has during the six months prior to the concerned act been associated with a company, directly or indirectly, in any capacity including by reason of frequent communication with its officers or by being in any contractual, fiduciary or employment relationship or by being a director, officer or an employee of the company or holds any position including a professional or business relationship between himself and the company whether temporary or permanent, that allows such person, directly or indirectly, access to unpublished price sensitive information or is reasonably expected to allow such access.*

(ii) *Without prejudice to the generality of the foregoing, the persons falling within the following categories shall be deemed to be connected persons unless the contrary is established –*

(a) an immediate relative of connected persons specified in `clause (i)' ; or

(b) a holding company or associate company or subsidiary company; or

[111] *Id.*, Reg 2(1) (n).
[112] *Id.*

(c) an intermediary as specified in S 12 of the Act or an employee or director thereof;

(d) an investment company, trustee company, asset company;

(e) an official of a stock exchange or of clearing house or Corporation; or

(f) a member of the board of directors or an employee of a public financial institution as defined in section 2(72) of the Companies Act,2013; or

(g) a member of the board of directors or employee of a public financial institution as defined in S 2(72) of the Companies Act,2013; or

(h) an official or an employee of a self-regulatory organization recognized or authorized by the Board; or

(i) a banker of the company; or

(j) a concern, firm, trust , Hindu Undivided Family, Company or Association of persons wherein a director of a company or his immediate relative or banker of the Company has more than ten per cent of the holding or interest."[113]

"Note: It is intended that a connected person is one who has a connection with the company that is expected to put him in possession of unpublished price sensitive information. Immediate relatives and other categories of person specified above are also presumed to be connected persons specified above are also presumed to be connected persons but such a presumption is a deeming legal fiction and rebuttable. This definition is also intended to bring into its ambit who may not seemingly occupy any position in a company but are in regular touch. With the company and its officers and are involved in eh know of the company's operations. It is intended to bring within its ambit those who would have access to or could access unpublished price sensitive information about any company or class of companies by virtue of any connection that would put them in unpublished price sensitive information."[114]

[113] *Id.*, Reg 2(1) (d).
[114] *Id.*, Reg 2(1) (d).

S 2 (f) defines `*immediate relative*' as :

"*a spouse of a person, and includes parents, sibling, and child of such person or of the spouse, any of whom is either dependent financially on such person, or consults such person in taking decisions relating to trading in securities*.'

Note: ` It is intended that the immediate relatives of a "connected person" too become connected persons for purpose of these regulations. Indeed this is a rebuttable presumption."

Section 195 of the Companies Act,2013

Section 195 of Companies Act, 2013 prohibits insider trading and any insider as defined in the Act if found guilty of the same. A penalty for jail term upto the term of 5 years can be imposed on a person found guilty of insider trading. Section 195(1)(a) defines insider trading in terms of price sensitive information. Section 195 is applicable on actions of directors, key managerial persons, any other person or their agents dealing with securities or their agents based on `*non-public price sensitive information'* directly or indirectly.

Section 195 of the Companies Act, 2013 which deals with insider trading apparently intend to include public companies, private companies, and listed companies under its dominion. However, with regard to its applicability on marketable securities, no clarification is provided neither in the statute nor by MCA.[115]

Apparently, the definition of insider trading under Companies Act, 2013 and SEBI (Prohibition of Insider Trading) Regulations, 2015 differs. Companies Act defines and includes the acts of "directors, key managerial persons, any other person or their agents dealing with securities or their agents based on `*non-public price sensitive information'* directly or indirectly."[116] On the other hand, the regulation defines the term 'insider' differently and includes any person who is connected with the company

[115] Avimukt Dar, Kriti Bhatia, *India: Insider Trading: A Confused Watchdog?*, MONDAQ (Jul. 13, 2015), *available at* http://www.mondaq.com/india/x/412000/Corporate+Commercial+Law/Insider+Trading+A+Confused+Watchdog.

[116] Companies Act, 2013, No. 18 of 2013§ 195, *available at* http://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf

having access to unpublished price sensitive information. Owing to the wider scope of the definition prescribed in the regulation, a case can be initiated against the person by SEBI under it. Hence, the regulations being more specific has an overriding effect and shall prevail over the provisions of Companies Act. Additionally, the penalty will be imposed on the defaulters if proven guilty under Section 15G of SEBI Act, as opposed to the term of imprisonment prescribed under the Companies Act, 2013.[117]

2.1.8. SECURITIES AND EXCHANGE BOARD OF INDIA CONSULTATION PAPER ON CROWD-FUNDING, 2014

Crowdfunding, basically, is pooling the money from numerous people to implement an idea of business. Rather than depending on a few substantial investors, it company generates money from numerous small donors. Crowd funding empowers anybody to utilize the internet to gage the estimation of individuals' idea and use online platform for their own success coupled with own judgment and experience to make wise decisions.[118]

The Consultation Paper, issued by SEBI comprehensively encompasses the legal and strategic position of crowdfunding in other countries. This is vital to determine the techanilities involved in the subject, the lacuna in the prevalent models and thereafter determine a model, which is most suited in Indian context. Along these lines, it discusses different probabilistic models for crowdfunding in India. The consultation paper has attempted to define the term in context of three key words; firstly, solicitation of funds; secondly, multiple investors; and thirdly using web-based platforms. This attempt has made it amply clear that, while drafting a policy for crowdfunding the concerned regulator (SEBI) shall, not only, have to reconcile the difference between the crowdfunding and other financial legislations but also Information & Technology Law. Another fact that makes it more peculiar is that the proposed implementation of crowdfunding in India will be in the form of equity, debt and fund based crowdfunding.

[117] Saibal, *supra* note 106.
[118] STEVEN DRESNER, CROWDFUNDING: A GUIDE TO RAISING CAPITAL ON THE INTERNET (1st ed. John Wiley & Sons 2014).

Under the circumstances mentioned in the crowd-funding consultation paper, apparently crowdfunding shall be administered under the provisions of SEBI Act and Company Act. The corresponding issue arising therefore is the extent of regulatory jurisdiction of SEBI with regard to crowdfunding. Simultaneously, in context of Companies Act, the moot point shall be whether solicitation of funds using a web based platform can be categorised as public offer or private placement.[119]

Additionally, there are certain inherent conflict between the notion of crowdfunding and principles laid down under company law. The same not to be subtle. As per the proposed definition of crowdfunding by SEBI, it is entirely clear that crowdfunding is based upon the generation of capital form public at large. Section 2(68)(iii) of the Companies Act a private company from accepting public deposits or invite pulic to subscribe its securities. Ipso facto, the companies or startup, which will be requiring capital from investors, ought not be a private company while the primary beneficiaries of crowdfunding are supposed to be mall and new private limited companies. Hence, the whole idea is contradictory to the scheme of Section 2(68). Therefore, SEBI while formulating the policy on crowdfunding has to remain sacrosanct and should harmonise the conflict between the two concepts.[120]

Furthermore, a private limited company can invite for subscription of its securities to not more than 50 persons. An offer becomes a public offer when it is made to more than 50 persons. Since such offer becomes a public offer, therefore, all compliance requirements with regard to prospectus and draft offer document are to be satisfied. It therefore, vitiates the very purpose of crowdfunding as the primary beneficiaries are small companies and start-ups.[121] This aspect was also highlighted in Sahara India Real Estate Corporation Limited v. SEBI.[122]

Probable Draft

A conceivable solution can be achieved by drafting the regulations meticulously. The procedural structure, which can be proposed in the draft regulations, shall have some

[119] Rupin Pawha , Prashant Pranjal & Ananya Mohan ,*Crowdfunding: Is India Ready?*, [2015] COMPANY L. J. 50, 50-55 (2015) *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2605329 (last visited Mar. 13, 2016).
[120] *Id.*
[121] *Id.*
[122] (2011) 5 Comp LJ 401 (SAT).

necessary aspects (a) offer is made through an electronic or website based crowdfunding platform and only registered investor shall have access to it. The platform shall be specified for companies, intermediaries and investors. (b) The said crowdfunding must be registered with regulator as per the norms of various financial norms of SEBI. (c) Further, the company who wish to generate capital through crowdfunding must also enroll itself and shall submit its proposed business model via-a-via the area where the money will be spent. (d) The crowdfunding platform, shall keep records of enlisted/registered investor who shall have authorised access to the crowdfunding platform to invest on the companies displayed on it.[123]

2.2.SECURITIES CONTRACTS (REGULATION) ACT, 1956.

The Securities Contracts (Regulation) Act, 1956 was enacted with an intent to regulate business in securities market avoid undesirable transactions by regulating the business of sale, purchase and transfer of securities.[124] It manages and regulates stock markets, listing of securities therein and deals with contracts in securities. It additionally supervises and keeps a vigilant eye over transactions of stock exchanges in India with a purpose to identify undesirable transactions. Section 2(j) defines stock exchange. Section 3 and 4 of the Securities Contract (Regulation) Act, 1956 contains the provisions relating to recognition of Stock Exchanges.

Under section 10(1) The SEBI may either on a request from the governing body of a recognised stock exchange or on its own motion make bye-laws for all or any of the matters specified in section 9 or amend any bye-laws made by such stock exchange under that section. According to Section 21, were securities are listed on the application of any person in any recognised stock exchange, such person is obliged to comply with the conditions stipulated in listing agreement entered with that stock exchange.

The recent development in this regard is the notification of Securities Laws (Amendment) Act, 2014 ("SLAA") on August 22, 2014. The amendment amended

[123] Rupin, *supra* note 119.
[124] Sunil, *supra* note 76.

SEBI Act, SCRA and Depositories Act and resultantly granted more powers to the capital market regulator.[125]

2.3.COMPANIES ACT, 2013.

The foremost method to protect the interest of investor is the exercise of due care by directors of company while carrying out their official function. Section 166 of the Companies Act facilitates this purpose. It obliges the director to take due and reasonable care, act in good faith and exercise independence while making managerial decisions. The genesis of this provision is the fiduciary relations that exist between the member and management of the company. The defaulters are prescribed with a fine of Rs. 0.1 million. However, the legislation does not comprehensively provide any objective standard to determine whether the director has carried out his function appropriately. Therefore, the interpretation of the provision is done contextually on a factual basis.

Section 195 deals with prohibition and punishment of insider trading, as discussed above and need not to be reiterated.

2.3.1. CLASS ACTION SUITS

A class action is a legal suit or claim that permits multiple individuals to sue for damages in furtherance of common intention. Class action suit can be characterized as representative and not as group litigation. By filing such a suit, the shareholders claim the recovery of losses occurred due to alleged mismanagement, fraud or misleading disclosure by the company. Hence, it is a claim by shareholders against the management of the company and the amount awarded in the judgment is distributable among the shareholders.[126]

J J Irani Committee (2005) recommended to codify the laws related to class actions in India. The report was submitted to the Ministry of Company Affairs. The primary purpose of the Committee's proposal was to protect the interest of investors and

[125] Vidya Sunderam, *More Power to SEBI to Tackle Scams - Amendment to Securities Laws in India*,53 TAXMANN ONLINE 506 (2015).
[126] Advait Gohil & Mohit Kalavatia, *Shareholder Class Action in India: An Introduction in the Companies Act, 2013Shareholder Class Action in India: An Introduction in the Companies Act, 2013*, 44 TAXMANN ONLINE 77 (2014).

furthermore to accord protection to shareholders. The Committee strongly felt the need to include the notions of class action, and derivative action in company law.[127]

Thereafter, section 245 was included in Companies Act, 2013 recognising class action law suits. It permits a group of investors to proceed against the management of the company, provided they have common interest in the matter. The remedy is also available against auditors or a section of shareholders who are allegedly involved in activities detrimental to the interest of plaintiff(s). The predominant purpose of class action suit is to restrict the company from committing an act which is beyond the scope of Articles of Association or Memorandum of Association or prevent the breach of same.[128]

Summing up, Section 245 is an enabling provision for depositors and shareholders to claim damages in the form of compensation from the management of the company i.e. directors including auditors, advisors, etc. The remedy lies against the unlawful and fraudulent acts that are injurious to the interest of shareholders or depositors.

[127] *See*, FERNANDO, *supra* note 75.
[128] Companies Act, 2013, No. 18 of 2013§ 245, *available at* http://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf

CHAPTER 3

3. PROTECTION MEASURES OF INVESTOR

Retaining the confidence of investors is the foremost and standout factor for development of securities market. It also ensures sustainable development of securities market provided highest priority is rendered to investors. Simultaneously, the investors must get assurance of secured interest and protected through fair deal.[129]

3.1.REGULATION OF STOCK BROKER

The term Investor protection is a wider meaning and incorporates various measures designed to protect the investors from malpractices of companies, brokers and various other intermediaries. SEBI is a guard of the stock trades of India. SEBI has issued extensive rules representing issue of shares, et al, and has comprehensively laid gritty standards for brokers, sub-brokers via other intermediaries.[130] A broker is said to be a member of stock exchange and permitted to trade on the stock exchange. The regulator must recognise the stock exchange whereas the broker is registered with SEBI. A sub broker is a person registered with SEBI and is affiliated to stock exchange.[131] SEBI is empowered by virtue of Section 30 of SEBI Act to make rules, regulations or guidelines to regulate stick brokers and sub brokers. Hence, SEBI (Stock Broker & Sub Brokers) Regulations, 1992 were issued to regulate them.

Section 11(2) of the SEBI Act contains measures available with SEBI to implement the legislated desire of investor protection. It includes "*registering and regulating the working of intermediaries like stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers etc. associated with securities markets"*.[132]

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[129] Vijay, *supra* note 3.

[130] Dr. V. Neelaveni, *Role of SEBI As a Regulatory Authority*, [10(2)] INT'L MONTHLY REFEREED J. OF RES. IN MGMT. & TECH. 31, 33-35 (2013) *available at*http://www.abhinavjournal.com/images/Management_&_Technology/Nov13/4.pdf (last visited Mar. 14, 2016).

[131] *Id.*

[132] Dr. K.V.S.N. Jawahar Babu & S. Damodar Naidu, *Investor Protection Measure by SEBI*, [1(8)]ARTH PRABANDH: J. OF ECON. & MGMT. 72, 72-80 (2012).

This is primarily due to the fact that, investor protection is one of the most important elements of a thriving securities market or other financial investment institution. Simply put, investor protection is the effort to make sure that those who invest their money in regulated financial products are not defrauded by brokers or other parties. It's important to note that unlike government insurance for monetary deposits, investor and customer protection does not extend to covering losses when the securities or products decrease in value. Investors have to assume the existence of risk as part of their opportunity for gains. Investor protection focuses on making sure that investors are fully informed about their purchases that insider activity does not threaten the worth of some portfolios for the enrichment of others, and those holdings are not simply "lost" in instances of brokerage failure.[133]

To ensure that the interest of the investor is protected, SEBI has focused on the flow of information on the trading side. SEBI started by insisting that the brokers' notes to their clients indicated the price and the brokerage separately for the orders that they executed for their clients SEBI then followed it up by asking brokers to account for their own proprietary funds deployed in the trade and client funds separately. Rudimentary as it might sound, these were big steps forward in improving transparency levels in trade execution.[134] Following SEBI's directive, exchanges have improved the flow of trade-related information by taking advantage of technology and minimizing instances of gaps in flow of information as in the case of off market transactions, such as block trades, which are now required to be routed through the electronic trading systems of the stock exchange.[135]

Trade manipulation practice is equally serious practice prevalent in the securities market. These are resorted by the brokers and traders in the securities market and also involves the owner, manager or promoter of companies who resort to such techniques for their personal advantage. Under such practices there is an unwarranted fluctuation in the prices of the securities, creation of fake market securities through circular trading or any other means. Trade manipulation practices are common with both small

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[133] *Id.*
[134] G Sabarinathan, *SEBI's Regulation of the Indian Securities Market: A Critical Review of the Major Developments*, [35(4)] VIKALP 13, 13-26 (2010) *available at*http://www.vikalpa.com/pdf/articles/2010/Vik354-02-ResGSabarinathan.pdf (last visited Mar. 14, 2016).
[135] *Id.*

as well as well-established companies. Therefore, such practices are detrimental to the interest of investors who shares are subjected to these practices. To control these menace, SEBI has issued SEBI (Fraudulent and Unfair Trade Practices) Regulation, 2003.[136]

Besides, regulatory control, all participants of the capital market vis company, brokers, sub-brokers or any other intermediaries must abide by the ethical conduct of high standards of honesty, integrity ad transparency. This plays a crucial role in maintaining investor's confidence.[137]

3.1.1. REGULATORY FRAMEWORK ON STOCK BROKERS AND SUB BROKERS

Under regulation 3 of SEBI (Stock Broker & Sub Brokers) Regulations,1992, a stock broker is to be registered mandatorily. Regulation 4 prescribes that, a stock broker applies in the prescribed format for grant of a certificate through the stock exchange or stock exchanges, as the case may be, of which he is admitted as a member.[138]

Regulation 17 prescribes the obligation of stock brokers to maintain a book of account. Further**,** Regulation 18A provide for appoint of a compliance officer by every stock broker for the purpose of looking after the affairs, rights, dispute redressal of grievance of shareholders and investors.

In addition to the previously mentioned, a stockbroker under regulation 7 must, at all times, abide by the code of conduct prescribed. This obliges the broker to maintain high standard of integrity, not to indulge in market manipulation or other related malpractices, exercise due care in conduct of his business and comply with statutory requirements. Further, he owes a duty that while transacting with the clients i.e. investors, he shall execute the orders faithfully execute the orders pertaining to buying and selling of securities. The same shall be done at the best available market price. The broker is not obliged to refuse a small investor for buying and purchasing securities, merely on the ground that the volume of business involved is less.[139] In context of business and commission, a stock broker is not allowed to furnish any

[136] *Id.*
[137] Dr. Neetu Prakash, *Role of SEBI in Investor Protection*, [2007] 75 SCL 139 (MAG).
[138] Sunil, *supra* note 76.
[139] *Id.*

information which is false or misleading or such information which gives fraudulent and misleading advice or information to the clients so as to induce them to sell or purchase securities, thus, earning commission. There should be fairness in his dealings with client.[140]

3.2.PROTECTION FROM INSIDER TRADING.

Insider trading refers to the dealings by corporate insiders, officers, promoters, employees, etc., in their own company. Insider trading *per se* is not considered undesirable. It is only the unethical dealings of insiders, which are considered against the interest of investors. The instances of such unethical behaviour include trading by insiders on the basis of unpublished price sensitive information, trading during the *close window* period, non-disclosure of trade by an insider. Dealing in securities includes an act of buying, subscribing, selling or agreeing to buy, subscribe, sell or deal in any securities.[141]

According to Lord Lane[142] the rationale behind the prohibition on insider trading is "*the obvious and understandable concern… about the damage to public confidence which insider dealing is likely to cause and the clear intention to prevent so far as possible what amounts to cheating when those with inside knowledge use that knowledge to make profit in their dealings with others*."[143]

SEBI as a sector regulator has played a key role in preventing the instance of insider trading and increase transparency in trading mechanism; in order to withhold the confidence of investors. Insider, as discussed above includes a person who is connected to management of the company or is deemed to have been connected with company's management. Such person is supposed to have access to the confidential information such as unpublished price sensitive information relating to securities before a public issue is announced. The insiders is a person (e.g. employee, director, etc.) holding a position under professional or business relationship with the company. Price sensitive information is the information that relates to the prices of the securities of the company and if published, may materially or substantially affect the prices of securities offered to be issued. It includes information related to dividends, buybacks,

[140] *Id.*
[141] Vijay, *supra* note 3.
[142] *Attorney General's Reference (NO.1 of 1988)*, (1989) 2 A11 ER 1.
[143] Sunil, *supra* note 76.

and information pertaining to proposed merger or amalgamation, disposal of assets or transfer of assets and any signification plan of business of the company.[144]

Cases of insider trading debilitates confidence of equity investors in the reasonableness and trustworthiness trading mechanism of the securities markets, therefore, such case are dealt as fundamental concerns by SEBI. SEBI came up with SEBI (Prohibition of Insider Trading) Regulations, 1992. However, due to poor execution, it lacked strength and the defaulters could easily evade its provisions. Subsequently, these regulations were amended over the years. Currently, SEBI's fundamental concern is to check the happenings of insider trading and the methodology established for this purpose requires the companies, stock exchanges, brokers, etc. to abide by the mandates of SEBI. [145] The objective was to provide a level playing field and ensure that all investors are kept on equal footing. Hence, under section 195 of Companies Act, 2013, new provisions regarding insider trading has been inserted to ensure transparency and accountability in a company's management and safeguard investor's interest.

3.3.PROTECTION FROM FRAUDULENT AND UNFAIR TRADE PRACTICE.

Prior to the SEBI Act, 1992, the securities market was prove to fraudulent trade practices. Since the investors were vulnerable to such practice, they lost their faith and opted to pull back their investment. During the early years of its establishment, SEBI faced serious challenges to fraudulent trade practices. Owing to the technical nature of securities market and ignorance of statutory provision, the investors was high confused about the methodology of securities market. This paved way for companies to carry on unfair practices. A few reprobates accrued benefit due to lack of awareness and complexities. They made false statements, concealed material facts to make quick money. It was important to stop those practices for sustainability of securities market.[146] Therefore, in exercise of the powers conferred by section 30 of the Securities and Exchange Board of India Act, 1992, the Board makes regulation,

[144] Neelaveni, *supra* note 130.
[145] Oommen A. Ninan, *SAT's Commendable Role in Finetuning the Capital Market*, THE HINDU, Nov. 10, 2003 at *available at*http://www.thehindu.com/biz/2003/11/10/stories/2003111000010200.htm (last visited Mar. 14, 2016).
[146] Sunil, *supra* note 76.

namely the Securities and Exchange Board of India (Prohibition of Fraudulent and unfair Trade Practices relating to Securities Market) Regulations, 2003.

Under Regulation 2(9), fraud has been defined in context of protection of investors' interest. It includes "the act of an issuer of securities giving out misinformation that affects the market price of the security, resulting in investors being effectively misled even though they did not rely on the statement itself or anything derived from it other than the market price."[147]

Regulation 4 prohibits of manipulative, fraudulent and unfair trade practices.[148] It *per se* provides for "prohibition of misleading advertisement and advertisement that contains information in a distorted manner and may impact the decision making of the investors."[149] The regulation further places restrictions on the activities of brokers, sub-brokers and other intermediaries.

Under regulation 5, SEBI is empowered to investigate on such transactions pertaining to securities, which it believes is detrimental to the interest of the investors or security market. On the previously mentioned grounds and based on the report of such investigation, under Regulation 6, SEBI is empowered to suspend or cancel the registration of intermediaries.

The task of protecting investor is also played by Company Law Board. In ***Chatterjee Petrochem (Mauritius) Co.* v. *Haldia Petrochemicals Ltd.***[150] it was observed by the Company Law Board that, "if the Directors are already document and have it their possession, then non-circulation of same with draft resolution will not vitiate the resolution."[151]

Supreme Court even applied the principle of equity to prevent shareholders from the oppression of the company. In ***Needle Industries (India) Ltd. v. Needle Industries Newey (India) Holding Ltd.,*** it was held that "An isolated act cannot lead to a

[147] SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003, Reg. 2(9) *available at* http://www.sebi.gov.in/acts/futpfinal.html
[148] SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003, Reg. 4 *available at* http://www.sebi.gov.in/acts/futpfinal.html
[149] SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003, Reg. 4 (2) (k) *available at* http://www.sebi.gov.in/acts/futpfinal.html
[150] (2008) 143 Comp Cas 726 (CLB).
[151] *Id.*, ¶ 76.

presumption of oppression and even a resolution in contravention of law may be in the interest of shareholders and the company."[152]

In ***Price Waterhouse and Co. v. Securities and Exchange Board of India and Whole Time Member Mr. M.S. Sahoo***[153], the Hon'ble High Court of Bombay held as follows:

"Under the provision of SEBI Act and the regulations issued thereof, SEBI has appropriate jurisdiction to inquire and prove into the matters pertaining to fabrication and manipulation of books of accounts and balance sheets of the company. It further stated that, SEBI could adopt appropriate regulatory measures in order to protect investor's interest and in the interest of securities market. Under the same it can debar a CA from auditing the books of account of a listed company."[154]

3.4.PROTECTION FROM UNHEALTHY TAKEOVERS – TAKEOVER CODE, 2011.

Under the amended Takeover code of 2011**,** a company can acquire up to 25% in a firm without requiring to make an open offer. The new takeover code also raised the open offer size from a minimum of 20% at present to 26%, providing an exit for more investors. Another important aspect of investor protection is that, under the new code, considering the average promoters shareholding prevalent in the Listed Companies and the international practices, the threshold limit has been increase to 25%. It will be beneficial from the point of Private Equity and Institutional investors who had to restrict themselves to 14.99% stake in every listed company in terms of existing regulations as otherwise it would necessitates the open offer to the shareholders of the Target Company for which they are in no way interested to do as their objective is not to acquire the control over the company. The increase in threshold would however, reduce the number of open offers and hence might be viewed negatively from the point of view small shareholders.

Overall, the new regulation has achieved a couple of noteworthy objectives, which are the focal points for the investor protection regime in India. To begin with, SEBI has

[152] (1981) 3 SCC 333.
[153] 2010 (112) Bom LR 3871.
[154] *Id.*

opened the doors increased investment by increasing the trigger limit that may have a positive and potential impact on the capital market. Second objective is that the procedure of acquisitions has been refined as the 2011 code will be applicable in those cases where the acquirer acquires or wish to acquire control in the management of the company.[155]

In ***Shirish Finance & Investment (P) v. M Sreenivasulu Reddy***,[156] a division of Bombay High Court elucidated the object of Takeover Code as: "The regulations pertain to a system which brings transparency in the transactions of mergers and takeovers. Thereafter, it facilitates the decision making of the investors regarding whether they should retain their securities or should they sell them. This permits fairness and transparency in the transactions, thereby, ensuring protection of investor's interest."[157]

In ***Punjab State Industrial Development Corporation Ltd. v. SEBI***[158] the SAT held that the takeover code has a limited role as it only provided remedial measures against mismanagement. Further, it does not intent to ensure proper management of the business of the company. It only confirms that shareholders are treated with equality and equal opportunity are provided to all shareholders, in case of takeover, merger or acquisition. Thereby, the SAT laid down fair treatment test.[159]

Subhash A. Gandhi v. SEBI[160], in context of old takeover code it was held that, regulation 7 is aimed to ensure transparency in the procedure and to assist the regulatory authority in this regard. The provision safeguards the interest of investors by providing them exit opportunity, if the merger, acquisition or takeover has not happened to the satisfaction of shareholders.

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[155] Karan Talwar , *Anti-Acquirer and Proshareholder? an Analysis of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011*, 5 NUJS L. REV.129 (2012), http://nujslawreview.org/wp-content/uploads/2015/02/karan-talwar-and-nivedita-saksena.pdf (last visited Mar. 20, 2016).
[156] (2002) 35 SCL 27 (Bom).
[157] Sunil, *supra* note 76.
[158] (2001) 32 SCL 631 (SAT).
[159] Sunil, *supra* note 76.
[160] (2005) 58 SCL 176(SAT).

3.5.INVESTOR EDUCATION & PROTECTION FUND AND INFORMAL GUIDANACE SCHEME.

SEBI (Investor protection and Education Fund) Regulation, 2009 are framed under Section 11 of SEBI Act, 1992. It severs the specific purpose of protection of investor's interest. It provides for organising educational activities for investors including training, seminars, etc. It creates awareness among investors through print and electronic media. It funds investor's association recognised by SEBI. It provides legal aid and assistance to such associations with regard to securities that are listed or are proposed to be listed. It ensures refund of security deposits of investors, which are kept by stock exchanges in case the stock exchange is derecognised. It provides travel expenses to members of Committee. It provides salary, allowances and expenses to the office of Ombudsman.[161]

Under the regulations, an Advisory Committee constituted recommending the measure, which ought to be taken for investor education and protection. A meeting of the Committee is summoned in every 3 months. Quorum for such a meeting is four members.[162]

One of the specific objective, as mention above of IPEF is to provide aid to investors association in case of a legal proceeding. Regulation 6 prescribes certain conditions for the same and additionally Legal Proceedings Guidelines, 2009 has been issued by SEBI to lay down *modus operandi* of obtaining such aid.[163]

3.5.PROTECTION OF INVESTOR THROUGH CORPORATE GOVERNANCE.

Corporate governance is a method to take full advantage of the Shareholder's Long term value and is also used to create a corporate custom of awareness, precision and candidness. It includes laws, rules, regulation, and guidelines for maximising the same. Corporate governance mainly works and depicts the ability of the company's

[161] Ashok Saxena, *Investor Protection and Education Fund Regulations on Sebi: An Overview*, 97 SCL (MAG.) 21 (2010).
[162] *Id.*
[163] *Id.*

management to take appropriate managerial decision vis-a-vis the rights of shareholder apart from stakeholder, specifically.[164]

According to Rafael La Porta et al (1999) "corporate governance to a large extent is a set of mechanisms through which outside investors protect themselves against expropriation by the insiders".[165]

It is a well-established fact that members of any company are benefited with many rights by the virtue of Companies Act, 1956 or as the result of MOA or AOA entered by the company and even sometimes general laws also provide them many benefits such as Indian Contract Act, 1872. An 18-member committee was formed on corporate governance headed by a leading industrialist, Kumar Mangalam Birla to look defend investors benefits. This committee made around 25 of recommendation out of which 19 were considered mandatory and every companies listed in the stock exchanges are under the duty to adopt these recommendations because of the contract e resulting from listing agreement between stock exchanges and the companies.[166]

Every shareholder of the companies though not directly involved in the management of the companies but have certain rights and duties to function even without involving in the corporate affairs of the companies. Shareholders can contribute to the company's affairs by opting high paradigm of corporate behaviour under good corporate framework without letting themselves involved in daily activities of the company.[167]

"A Quick Reference Guide for Investors" has been published by the Securities and Exchange Board of India (SEBI) lays down the rights enjoyed by the shareholders of the company as under:-

- To obtain the share certificate, on allotment or transfer of the share within reasonable time.

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[164] FERNANDO, *supra* note 75.
[165] Rafael La Porta et al., *Investor Protection and Corporate Governance,* 58 J. OF FIN. ECON. 3, 3-27 (2000) *available at*http://scholar.harvard.edu/files/shleifer/files/ip_corpgov.pdf?m=1360042297 (last visited Mar. 19, 2016).
[166] FERNANDO, *supra* note 75.
[167] DR. SWAMI PARTHASARTHY, CORPORATE GOVERNANCE: PRINCIPLES,MECHANISM&PRACTICE 327 (1st ed. Dreamtech Press 2006).

- To obtain the annual report, the balance sheet, profit & loss report and auditor's report copies.
- To contribute their presence in the general meetings either personally or via proxies by participating in the voting process.
- To get dividend within reasonable time after the approval of the general meeting
- To acquire rights, bonus etc. within reasonable time with prior approval.
- They can call for AGM by filing an application to Company Law Board (CLB).
- They can look into or inspect the minute books of the general meeting and can ask for the copies of it if required.
- They have right to file a case against the of both civil and criminal nature.
- They can ask for winding up of the company.
- In case of winding up they have right to receive residual proceeds.

As a group of shareholders:

- Demand for extraordinary meeting
- They can ask for voting on any resolution
- They can file application before Company Law Board asking for investigation of the company's affairs.
- They can claim relief case of oppression or mismanagement of the company by filing an application to the Company Law Board.

Rights of a Debenture-holder

- They have rights to obtain any benefit or redemption within reasonable time.
- They can request a copy of the Trust Deed.
- They can ask for winding up of the company in case company if not able to pay its debt.
- They can put their grievance in front of the debenture trustee.

However, the above mentioned rights are not absolute rights they may change as per the requirement; therefore no one can claim them absolutely. E.g. transfer of securities not an absolute right, such transfer can be refused by the Company as per legislative provisions.

Responsibilities of Shareholders

As it is clear from the abovementioned text that shareholder's enjoy various rights but as a general principle with every right there exists corresponding duty to be fulfilled by person enjoying any such rights. This is also true in case of shareholders. Duties include:

- They should keep an eye of the company's affair and must be informed.
- They should always be alert.
- They should take part in annual general meeting and should actively participate in the voting process.
- They should exercise their rights on their own or in group.

Right related to trading of securities.

Every shareholder has a hold on their securities and they can trade their securities as and when they want at price whatever he deems fit. He can sell his securities himself, or through any agent or representative authorised by him, or all the way through recognised stock exchange. Similarly, he may any time purchase any securities at a price he may deem fit or agreed mutually from any person or stock exchange.

3.6.PROTECTION OF INVESTOR THROUGH OMBUDSMAN.

The SEBI with the objective to safeguard the interest of the investors with regard to securities have constituted an Office of the Ombudsman to acknowledge the problem of the investor to sort them out. Therefore, SEBI using its power under section 30 along with section 11(1), made a new regulation in order to provide protection to the investor and to redress their grievances named as "Securities and Exchange Board of

India (Ombudsman) Regulations 2003", which talks about constitution the office of Ombudsman.[168] However, it was not implemented. The current mechanism is:

Sl. No.	*Complaints*	*Legislative provision*	*Relief provided*
1	Delay in refund of excess application money or allotment letters	Section 73 of the Companies Act, as amended in 1988	Payment of interest for the delayed period beyond 70 days from the closure of subscription list @ 15 per cent
2	Delay in transfer of shares	Section 133 of the Companies Act.	A time limit of 2 months provided in the Act for effective transfer. As per the Listing Agreement, the time limit is only 1 month from the lodgement of shares
3	Refusal of transfer of shares	Section 22(A) of the SC (R.) Act. (This section lists the reasons for which transfer of shares can be refused)	Transfer can be refused only for specific and valid reasons given in the Act and not otherwise
4	Problem of odd lots	Listing Agreement provides for issue of certificates in marketable lots and avoidable odd lots	Need for consolidation of odd lots and ensuring the issue of shares only in marketable lot through conversion of debentures or rights issue, provision of an odd lot trading session and listing out broker willing to trade
5	Take-over bids	New clauses 40(a) and 40(b) of Listing Agreement	Purchase or acquisition of shares beyond 5 per cent to be notified to the Stock Exchange. Acquisition beyond 10 per cent puts an obligation on the transferer and intermediary to notify the Stock Exchange and the public; and offer to the other shareholders of the company to buy at offer price or the highest market price during the preceding six months
6	Insider trading, rigging and other malpractices	SEBI (Insider Trading) Regulations Act 1993	The investors have to guard themselves regarding the price and their investments, besides making a complaint to SEBI
7	Delay and non-payments of interest/fixed deposits by companies	Section 58(B) of the Companies Act	Appeal to the Company Law Board
8	Delay and non-payment ofdue sornon-delivery of shares by brokers	Rules and byelaws of the Stock Exchange.	Complaint to the grievance cell of the Stock Exchange concerned
9	Non-supply of debenture trust deed, refusal to inspection	Section 163, 196, 219, 304 of the Companies Act.	Appeal to the Company Law Board and lodge complaint with the trustee

Source: Agarwal, Sanjiv A Manual of Indian Capital Markets

[168] Sunil, *supra* note 76.

CHAPTER 4

4. LEADING CASES AND INSTANCES

At the point when investors finance firms, they normally get certain rights or powers that are for the most part are secured through the enforcement of regulations and laws. Few of these rights incorporate disclosure and accounting rules, which furnish financial investors with the data they require to exercise various rights. These rights are derived from contracts. If there should be an occurrence of a question, the courts adjudicate contracts between contracting parties and set up precedents shaping the common law.[169]

4.1.THE SAHARA CASE (2013)[170]

Sahara case will stand out forever as the one that conveyed the attention on investor protection, not on account of the duped investors' protest, but rather in light of the fact that a SEBI as vigilant regulator and Supreme Court the highest court of the land issued all around guidelines, scrutinized vital aspects and passed historic judgment on the infringement of its regulatory framework, and imprisoned the culprits.[171]

4.1.1. SUMMARISED FACTS

Sahara went under investigation when Sahara Prime City, a real estate endeavour of the group, documented a Draft Red Herring Prospectus (DRHP) with SEBI on September 30, 2009. While observing this DRHP, SEBI doubted that the two companies of Sahara Group, Sahara India Real Estate Corp Ltd (SIRECL) and Sahara Housing Investment Corp Ltd (SHICL) were involved in substantial scale money raising practices. SEBI additionally received two complaints claiming illicit and illegal means undertaken by these two organizations to issue bonds as OFCDs (Optionally Fully Convertible Debentures), to people. Both the group companies had coasted an issue of OFCDs and began gathering subscriptions from investors from

[169] Rafael, *supra* note 165.
[170] S*ahara India Real Estate Corpn. Ltd. v. SEBI*, (2013) 1 SCC 1.
[171] Uma Shashikant, *Sahara: A Landmark Case that Brought Focus on Investor Protection*, THE ECON. TIMES, Mar. 10, 2014 at ET Commentary *available at* http://articles.economictimes.indiatimes.com/2014-03-10/news/48083867_1_sahara-companies-3-crore-investors-sahara-group (last visited Mar. 15, 2016).

April 2008 until April 2011. Amid this period, the organization had an aggregate accumulation of over Rs 176.56 billion.[172]

Around 30 million investors invested as "private placement". The capital was raised ignoring the prerequisites pertinent to the public offerings of securities. The RBI issued an open notification cautioning investors against Sahara, while the matter was still being investigated by SEBI, expressing that investors ought to verify the company's name which issues the deposit receipt and also whether the same is authorised by RBI to do so. Hence, SICIL and SIIDL were not approved to accept public deposits. While taking cognizance of the issues relating to OFCDs, SEBI passed an order in June, 2011 ordering the two companies to give back the money so gathered to the investors, furthermore prohibited the two companies from accessing the securities market till next orders.[173]

Sahara then appealed against the order of SEBI, before Securities Appellate Tribunal however the Appellate Tribunal affirmed SEBI's decision. Thereafter, Sahara filed an appeal under the watchful eye of the Supreme Court against the order of the Appellate Tribunal. The Supreme Court opined that the SEBI Act, 1992 is a special piece of legislation and empowers SEBI to investigate and decide the matter with an ultimate aim to secure the interests of the investors. It was observed that, powers granted to SEBI under the act are not derogatory to other legislation viz companies act and the same ought to be perused amicably with such other provisions so that there is no clash of jurisdiction between the Ministry of Corporate Affairs and SEBI in sensitive matters where interests of the investors are in question. For sustenance of this view, the Court laid accentuation on the legislative intent and the statement of objectives for the enactment of SEBI Act and the insertion of Section 55A in the Companies Act 1956 to delegate exceptional powers to SEBI in matters related with issue, allotment and exchange of securities. The Court observed that as per provisions enumerated under Section 55A of the Companies Act 1956, SEBI is legitimately entitled to regulate public listed companies and those public companies, which trade their securities in the recognised stock exchange. Provided that the matter pertain to issue

[172] Shambha Dev, *AN ANALYSIS of PONZI SCHEMES and the STATE of FINANCIAL REGULATION in INDIA*, 4 NLIU CORP. L. E J. 1, 9-24 (2014) *available at*http://www.nliu.ac.in/publication/others/cbcliv.pdf (last visited Mar. 15, 2016).
[173] *Id.*

and transfer of securities and non-payment of dividend. It was contended by Sahara that OFCDs were "hybrid" instruments and therefore falls beyond the scope of the definition provided Section 2(h) of Securities Contract (Regulation) Act, 1956 ("SCRA"). The Court held that in spite of this fact, it doesn't cease being a "Security" under the Companies Act, SEBI and SCRA. The meaning of "Securities" under S.2(h) of SCRA is a comprehensive one and covers every single "Marketable Securities". Sahara had offered OFCDs to a large number of individuals and along these lines there is no reason to scrutinize the marketability of such instrument. Furthermore, since the name itself contains the expression "Debenture", it is therefore a security. It was contended on behalf of Sahara that the provision of SCRA are not applicable as OFCDs were akin to convertible bonds based upon the price mutually determined at the time of issue. Therefore, SCRA is not material relation to Section 28(1)(b) and thus lacks the jurisdiction on this case. The contention was dismissed by Supreme Court and clarified that the contention of inapplicability of SCRA by virtue of section 28(1)(b) does not pertain to convertible bonds to such person to whom such share, convertible bonds are issued so as to have shares at his option. Therefore, the Act is inapplicable only with regard to the rights attached to bonds and not the bond itself. Further clarifying the situation, the SC opined that the only convertible bonds, shares or warrants are excluded from the domain of the Act and not debentures which are a separate category under Section 2(h).[174]

Since, the OFCDs were issued to more than 50 person it is a public offer and the intention of parties to make it look like a private placement does not matter much. Therefore, in light of Section 67(3) of Companies Act 1956 issue was public offer and SEBI has jurisdiction on the case.[175] The Supreme Court ordered to refund of investor's money and Sahara was prohibited from raising money by means of public issue. Meanwhile, the company switched to new area of operation, the Sahara Credit Co-operative Society.

On the issue, that whether SEBI is empowered to govern unlisted companies that did not intend to get their securities listed by virtue of Section 55A, the SC held in affirmative. The SC held SEBI is empowered by the virtue of Section 55A to control

[174] *Id.*
[175] *Id.*

certain provisions for listed and unlisted companies that proposed to get their securities listed on recognized stock exchanges. It happened so, that the Sahara Companies were not listed and they did never claim of getting them listed.[176]

It was opined that the intention has to be contextually determined from the acts of Saharas. Since they made a public offer for the issue of securities, it therefore, mandatorily requires to be listed required mandatorily to enlist such securities. It can construed that there was a deemed intention based on the fact the companies were not able to do certain acts which require listing and later contends that they never intended to list their securities.[177] Lastly, Section 11 of SEBI Act is applicable to cases pertaining to investor's interest and regulation of securities market. Therefore, under the circumstances of the present case, SEBI has jurisdiction over the matter.

On the issue of nature of SEBI DIP guidelines, whether having statutory or departmental force, it was held that they have statutory force and are not merely departmental guidelines.[178]

It was held by the Supreme Court held that the DIP Guidelines had "statutory power" and that the issuance of OFCDs were in violation of the DIP Guidelines as well as those of the SEBI ICDR Regulations.

On the issue whether section 73 of the Companies Act, 1956 impose any affirmative obligation on the company, the SC held that the principle of listing imposes a legal obligation on company to assist public in recognition of their commitments and obligations. Further, if a company wish to list their securities impliedly consent to the obligations. This is done by means of application to SEBI, issue of prospectus and thereafter maintenance of listing in the stock exchange. The Court held that disclosure is a rule and not exception.[179]

The legal obligations concerned with listing was referred to, by the Court and it stated that the it should assist and help people in public companies in recognizing their

[176] Jayant Thakur, Some highlights of Supreme Court's decision in Sahara Companies' matter, INDIACORPLAW Blog (Sep. 7, 2012) available at http://indiacorplaw.blogspot.in/2012/09/some-highlights-of-supreme-courts.html
[177] *Id.*
[178] *Id.*
[179] Akshay Amritanshu, *Sahara India Real Estate Corpn. Case: An Analysis*, 56 PRAC. LAW. 61 (2013).

commitments and obligations. Court held that, public companies which are legitimately obliged to list their securities are regarded to have acknowledged the continuing duties, by prudence of their application, prospectus and the consequent support of listing on a recognised stock exchange. Revelation/Disclosure ought to be the guideline and not the exemption. The Court then alluded to Section 73 of the Act which spoke about the allotment of shares and debentures to be managed in on stock exchange.

The Court expressed that Section 73(1) of the Act lays down an obligation on each company which is planning to offer shares or debentures to people in general to apply on a stock exchange for enlisting the securities. Once the offer is made to public (more than 49 investors) they had no choice or alternatives but to opt for listin their securities on a recognized stock exchange. If an unlisted company communicated its intention, by conducting in a certain manner, to offer its securities through public issue by issuing prospectus, it is also under an obligation to list its securities in a recognised stock exchange.[180]

4.1.2. CONCLUSION

The case is an example of delay on the part of Sahara companies. The SC whiel hearing tha matter observed that "*You have no intention of returning the investors' money. Your intention is very shaky. Your every step is shaky. We cannot interpret our order according to your need. You are justifying your conduct, which is not justifiable*."[181] Even the CJI mentioned: "*we are more concerned about the common man, who has invested his money in the*

Therefore, it can be argued that the judgment is a landmark vis-à-vis securities law, company law and protection of investor's interest. SC elucidated the principle that the no one should allowed to take advantage of the interpretation and loophole in the statute and the same should not be taken for granted The case has reclassified securities concerning privately of public listed companies and private companies.[182]

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[180] *Id.*
[181] J. Venkatesan, *Your Intention Is Shaky, Supreme Court Tells Sahara,* THE HINDU, Dec. 04, 2012 at*available at* http://www.thehindu.com/todays-paper/tp-business/your-intention-is-shaky-supreme-court-tells-sahara/article4162088.ece (last visited Mar. 16, 2016).
[182] Akshay, *supra* note 179.

It nonetheless, challenges the functioning of regulatory authority, their credibility and efficiency. The ROC dispite of being aware about the fact that large sums of money were appropriated from public by means of public issue, it failed to coney the same to higher authorities. Even SEBI failed to caught hold of the defaulters and the case was finally noticed when the companies file the offer document with SEBI. Hence, it questions the role of SEBI as a guard of investors.[183]

In such case, the safeguard measures adopted by the regulator are the deciding factor in ensuring investor protection.

Firstly, it must be ensured that company which raises money through public issue must have adequate net worth. This is important to ensure that the money invested by the investors is used for the prudent purpose and that the issuer has financial strength to deal with adversities. Oppositely, one of the Sahara companies was incurring loss while the net worth of other company was only Rs. 11 Lakh. Obviously, neither of them had the financial strength to make a public issue.[184]

Secondly, there is a definite process to raise the money. Disclosures must be made to prospective investors (through prospectus) in a given manner and format. The prospectus is to be observed by SEBI to assure the accuracy and adequacy in the disclosure. Collecting bankers, registrars, transfer agents and merchant bankers are required to be appointed before proceeding with the Public issues.[185] In the instant case, none of such entity was appointed and to add to the melancholy the disclosures were improper. The absence of exact information or electronic records of the investors have negatively affected the investors.

Third, the amount so obtained from the public must be taken care of, especially when the individuals are not straightforwardly included in its utilization. SEBI's administrative structure requires clear fund accounting, its audit review and supervision of final use. It additionally requires for developing a mechanism of a

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[183] *Id.*
[184] Uma Shashikant, *Sahara: A Landmark Case that Brought Focus on Investor Protection,* THE ECON. TIMES, Mar. 10, 2014 at ET Commentary *available at* http://articles.economictimes.indiatimes.com/2014-03-10/news/48083867_1_sahara-companies-3-crore-investors-sahara-group (last visited Mar. 15, 2016).
[185] *Id.*

debenture trustee if the security refers to a borrowing. Such safeguards were missing in this case.[186]

Most of the safeguarding provisions in the prospectus were marker as "not applicable". The funds were kept in a bank account of the Sahara India group, which consented to "share" its account with the money raising companies. Since every one of these were privately owned companies or partnership firms, none of the records are accessible for open examination, notwithstanding the involvement of the amount. The annual returns of some of these companies were also not filed with the registrar of companies.[187]

4.2.SHUBHKAM VENTURE CASE[188]

The obligation of the acquirer to make a mandatory public offer arises in 2 situations under the provisions of SEBI Takeover Code. Firstly, according to regulation 10 and 11, if the acquirer acquires shares or voting rights past certain defined threshold limit. Secondly, according to regulation 12 if the acquired acquires control in the management of the company regardless of whether it has acquired shares or voting rights in the company.[189]

4.2.1. SUMMARISED FACTS

Subhkam Ventures (I) Private Limited acquired shares in excess of the threshold limit of 15% shares in the target company-MSK Projects Limited. The acquirer made an open offer in accordance with regulation 10 of the Takeover Regulations, the SEBI was of the view that, it additionally ought to make the open offer as per regulation 12 of the Takeover Regulations; as there was change in control of the target company as per certain provisos in the shareholders' agreement between MSK and Subhkam.[190]

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[186] *Id.*
[187] *Id.*
[188] *Subhkam Ventures (I) (P.) Ltd. vs. SEBI*, 99 SCL 159 (SAT).
[189] Relief for Investor Community on "Control" Debate, IndiaCorpLaw Blog (Jan. 17, 2010) available at http://indiacorplaw.blogspot.in/2010/01/relief-for-investor-community-on.html.
[190] Swetha Prashant, *Subhkam Ventures (India) Private Limited V. SEBI: Heralding Good Times for Pipe Deals*, 102 SCL (MAG.) 55 (2010).

4.2.2. ANALYSIS

On examining the issue whether regulation 12 of the Takeover Regulations has been triggered as argued by the SEBI, the SAT has drawn a subtle distinction between proactive and reactive power of an investor for determining the parameters for the definition of control under the Takeover Regulations. It observed that the term control, as defined under the Takeover Regulations, is proactive rather than reactive. It also rightly observed that the power of an investor to prevent a company from doing a certain action by itself would not tantamount to controlling the company. Therefore, the real test, as prescribed by the SAT, to see if an investor is in control of the company, is to determine whether it is the investor who is the driving force and providing motion to the listed company or not.

On examination of issue pertaining to applicability of regulation 12, the SAT draw a subtle difference between protective and reactive right of an investor for deciding the factors for the meaning of control under the Takeover Regulations. The term "control" under the Takeover Regulations is observed as being proactive rather than reactive. SAT also held that an investor's power of preventing a company from committing certain act by itself will not amount to the controlling of the company. Hence, the genuine test, as endorsed by the SAT, to check whether an investor is in control of the company, is to figure out if the investor is the main thrust and is giving a drive to the listed company or not. The SAT explained the situation with the help of very interesting metaphors as follows:

> *"The test really is whether the acquirer is in the driving seat. To extend the metaphor further, the question would be whether he controls the steering, accelerator, the gears and the brakes. If the answer to these questions is in the affirmative, then alone would he be in control of the company. In other words, the question to be asked in each case would be whether the acquirer is the driving force behind the company and whether he is the one providing motion to the organisation. If yes, he is in control but not otherwise. In short, control means effective control."*[191]

[191] *Subhkam, supra* note 188.

Finally, the SAT concluded, with respect of affirmative rights that veto rights will not compose any kind of "control" as per the Takeover Code. The object of conferring such rights is precisely that the company must take any decision that may result in change in current position of the company without the knowledge and approval of investors. Simultaneously, it guarantees good standards of corporate governance. The matters which are not in the daily operations of a company do not require any vote of approval from the shareholders, and hence the investor cannot be said to be in control of the company. Ultimately, "control" is a proactive power and cannot be termed as reactive power.[192]

4.3.REEBOK FRAUD CASE.

Reebok Fraud case is a significant example of corporate fraud in India. It emerged as the companies Adidas India merged with Reebok India. Section 234 of the Companies Act empowered the examination/investigation by the RoC. In the examination, abnormalities and irregularities were found in the account books of Reebok, allegedly. Approximately Rs. 870 crores or more was evaluated to have been scammed. Consequently, the Managing Director Subhinder Singh Prem and the Chief Operating Officer Vishnu Bhagat were arrested. The frauds affected the shareholders of both companies.[193]

It was found to the astonishment of the probing authorities that a "systematic" mismanagement was incorporated for making way for the fraud. The governance and operation of the company were seriously mismanaged to the cost of investor's interest. The facts that hampered investor's interest, concealing the true data on storage facilities, etc. The set forth under Companies Act were deliberately skipped with a motive to evade tax (instead avoid tax). The Serious Fraud Investigating officer (SFIO), through its conduct also played a key role. SFIO, in its report stated that the involvement of management (COO & MD) in fraud was due to lack of corporate governance. The report affirmed that the organization had distorted the records and

[192] *Id.*
[193] Sahil Arora & Utkarsh Soni, Abstract, *Investor Protection in the Aftermath of the Reebok Fraud Case: An Appraisal of the Need for Corporate Governance in Non-Listed Companies,* XI CAPITAL MARKETS CONF. , http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2263081 (last visited Mar. 21, 2016).

inflated the sales.[194] Hence, The need for corporate governance mechanism in India has been pointed out by this case so as to protect the interests of the investors and shareholders.[195]

A compelling lawful security is essential for good corporate administration. Various measures were taken over the years vis. many committees were appointed to recommend changes in corporate governance mechanism and make it more effective. However, none of them focused on corporate governance in unlisted companies.[196] Clause 49 of the Listing Agreement, which is the base of corporate governance in India, is relevant to listed company. SFIO is the investigating body to probe into the cases involving complex investigation. It also deals with a case have international ramifications or involves public interest. However, SFIO does not possess the required powers to manage such matters and it needs statutory powers vis-à-vis statutory recognition. This aspect was considered while drafting Companies Act, 2013 and the SFIO has been given necessary powers statutorily.[197]

The structure of corporate ownership determines the standards of corporate governance in company. *Ipso facto*, the standards of best practices applicable to listed companies are not *per se* applicable to unlisted companies. Additionally, the unlisted companies are generally sole proprietorships or are privately owned and might not have the shareholders.

Corporate governance is not only confined to protecting the interests of the investors. The monitoring functions and the responsible accountability of a company also form indispensible part of the principle of corporate governance.[198] The corporate fraud in the case of the Reebok India Company has highlighted that management of the

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[194] Note, *SFIO Report Finds Reebok Guilty of Fudging A/Cs: Sources*, June 11, 2013 *available at*http://www.moneycontrol.com/news/cnbc-tv18-comments/sfio-report-finds-reebok-guiltyfudging-acs-sources_895198.html (last visited Mar. 21, 2016).

[195] Sahil, *supra* note 193.

[196] Sumant Batra, *India: An Overview of Corporate Governance of Non-Listed Companies, Corporate Governance of Non Listed Companies*, 2006 OECDCORP. GOVERNANCE OF NON LISTED COMPANIES 167 (2006), http://www.oecd.org/corporate/ca/corporategovernanceprinciples/37190767.pdf (last visited Mar. 21, 2016).

[197] Jea Swanson, *India Seeks to Overhaul a Corporate World Rife with Fraud*, THE NEW YORK TIMES, Aug. 15, 2013 at B5 *available at*http://dealbook.nytimes.com/2013/08/15/india-seeks-to-overhaul-a-corporate-world-rife-with-fraud/?_r=0 (last visited Mar. 21, 2016).

[198] *See*, CADBURY, REPORT ON COMMITTEE OF THE FINANCIAL ASPECTS OF CORPORATE GOVERNANCE (Gee Publishing, London 1992).

company and the auditors may be involved in corporate frauds that are eventually detrimental to the interest of shareholders and signifies the lacuna in monitoring and accountability standards of company. In light of such a exposure, it is critical to protect investor's interest in an unlisted companies. In this case, the interest shareholder of parent companies was at stake. The case illuminates how the shareholder of a public company is affected by the scams in its private unlisted subsidiary. Additionally it affected employees, customers as Reebok had hundreds of franchise.

CHAPTER 5

5. CHALLENGES TO INVESTOR PROTECTION REGIME IN INDIA.

In spite of the fact that there exist a specific redressal mechanism, the idea of protection of investor's interest is still suffering from certain vital lacuna prevalent in the regime devised for protection of investor's interest. Absences of awareness, assortment of powers between various regulators, jurisdictional conflicts and limitations pertaining to the execution of legislative spirit have all acted against investors. The argument is substantiated by the fact that, despite of apparently far reaching system for protection of investor's interest, a series of scams has taken place which highlights various operational limitations of present mechanism.

Certain aspects are highlighted as under:

5.1.INVESTOR AWARENESS AND EDUCATION REGIME.

SEBI has implemented a number of steps to regulate Capital Market. However, with regard to investor awareness and education, the efforts taken are virtually ineffective. Little appears to have been done to comprehend the particular needs of an investor and to make him mindful about his rights under the regime. The fundamental methodology regulator in executing the legislation intent of ensuring investor's protection has been that of cure as opposed to prevention. SEBI and MCA have focused more on giving symptomatic cure to the ills of the business sector, rather than fortifying the interior resistance by making the investors mindful about the market. Consequently, the regulations framed are lacking the approach to serve the reason of its formulation, i.e. protection of investor’s interest. Additionally, the investors are not informed enough to exercise their rights, essentially in light of the fact that they have restricted exposure to the information.[199]

Few such analogies can be drawn from following practical instance:

(a) Since prospectus, issue advertisements and share application forms are required to be English. SEBI or MCA have never attempted to survey the number of

[199] Vijay, *supra* note 3.

investors who are able comprehend English and among them how many can decodify the complexities involved in the aforesaid documents. One is astounded to see that even the statutory advertisements which are required to be published via vernacular medium are published in English.[200]

(b) The SEBI rules require that the company should state the risk factor associated in the venture, in its prospectus, advertisement, et al. It has been observed that these rules are compiled only virtually as a mere ritual or formality. Thereby, the risk factor howsoever grave, are not uncovered to investors.[201]

(c) Issuer is obliged to inform and disclose the risks involved in a specific instrument to the investor. The same is subjected to discretion of the issuer and it is done in a manner most suited to them. For instance, it is required for companies accepting public deposit, to disclose in the application form whether the deposits are unsecured and ranking pari-passu with other unsecured liabilities. The issuer makes this announcement in a dark corner of the application form, and that too in smallest font, while other contents such as loan rates and corporate mottos are printed noticeably. In addition, it has been watched that largely only the photostat duplicate of just that some portion of application form that should be filled in by the investors is printed.[202]

5.2.LIMITATIONS OF SEBI

In spite of the fact that it was established as a sentinel for ensuring investor's interest, regulating stock markets and promoting capital market, still it confronts various issues/constraints. Some of these are as per the following:

- SEBI, as authorised by Central Government is empowered to edge its principles and regulations for effectively observing capital markets. These tenets and regulations are subjected to approval of Central government. This has led to useless deferrals and impedance by the Ministry of Finance and has influenced the working of SEBI. Ideally, for efficient function of the system,

[200] *Id.*
[201] *Id.*
[202] *Id.*

government ought to coordinate with SEBI to lay down such regulations so as to accomplish proficient productivity.[203]

- In certain case, SEBI is required to obtain permission from Central Government before lodging criminal complaint. This, in turn has caused unnecessary delays.[204]

- SEBI as a regulator has been unsuccessful in tackling scams; that occurred over the years since its establishment. SEBI has been accused to fail in taking appropriate reforms after such scams were spotted. The SEBI has gone more than half away to assist potential defaulters to evade a big payment crisis. At whatever point the genuine extortionists get up to new traps, surveillance takes a lot of time to catch up with them. The SEBI is seen to be accommodated the needs of corporates than that of the investors than financial specialist cordial. It fizzled to punish fraudulent organizations, as well as remained an observer when same organizations re-entered the business sector with new issues.[205]

5.3.FALL IN INVESTOR POPULATION

A number of guidelines and regulations were issued by SEBI since 1992, amended and reformed from time to time for up-keeping the investor's interest and keeping their investment safe. Nonetheless, SEBI has not been completely effective in its central goal as clear from the report of Swaroop Committee (2009) which expresses that the investor's population in India is on a decline. The fundamental explanations behind this lofty fall in investor populace can be attributed to the widespread acts of neglect and malpractices apparent in the capital market and absence of satisfactory mechanism to deal with investor's grievances in a time bound manner.[206]

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[203] Sarvesh Khatnani, *Role of SEBI in Capital Market: Developments and Challenges*, THE CORP. L. REP., Oct. 30, 2013 at *available at* http://corporatelawreporter.com/2013/10/30/role-sebi-capital-market-developments-challenges-1/6/ (last visited Mar. 16, 2016).
[204] *Id.*
[205] *Id.*
[206] Parmod Kumar, *Role of SEBI in Investors' Protection in India*, [2(12)] TACTFUL MGMT. RES. J.9 (2014) *available at*http://tmgt.lsrj.in/UploadedArticles/260.pdf (last visited Mar. 16, 2016).

5.4.IPO GRADING

The notion of Initial public offering grading was implemented in India with intent to provide fundamental information pertaining to IPO in a simple way, thereby increasing the pricing efficiency of IPO. The favourable circumstances it conveys and with lot of positives associated with it, was aimed to aid the investors in making informed and right investment choices. After weighing both quantitative and qualitative arguments, it can argued that even this initiative by SEBI has had a constrained effect on binding the investors for IPO.[207]

5.5.CROWDFUNDING

As per the proposed definition of crowdfunding by SEBI, it is entirely clear that crowdfunding is based upon the generation of capital form public at large. Section 2(68)(iii) of the Companies Act a private company from accepting public deposits or invite pulic to subscribe its securities. Ipso facto, the companies or startup, which will be requiring capital from investors, ought not be a private company while the primary beneficiaries of crowdfunding are supposed to be small and new private limited companies. Hence, the whole idea is contradictory to the scheme of Section 2(68). Therefore, SEBI while formulating the policy on crowdfunding, has to remain sacrosanct and should harmonise the conflict between the two concepts.[208]

The Consultation Paper, issued by SEBI comprehensively encompasses the legal and strategic position of crowdfunding in other countries. This is vital to determine the peculiarities involved in the subject, the lacuna in the prevalent models of various jurisdictions and thereafter determine a model, which is most suited in Indian context. Along these lines, it discusses different probabilistic models for crowdfunding in India. The consultation paper has attempted to define the term in context of three key words; firstly, solicitation of funds; secondly, multiple investors; and thirdly using web-based platforms. This attempt has made it amply clear that, while drafting a policy for crowdfunding the concerned regulator (SEBI) shall, not only, have to reconcile the difference between the crowdfunding and other financial legislations but also with Information & Technology Law. Another fact that makes it more peculiar is

[207] V Ashamol, TA Renjith & Joseph George, *Legal Framework of Initial Public Offering (IPO) Grading in Protection of Investors* , [3(9)] J. OF INT'L ACAD. RES. FOR MULTIDISCIPLINARY 225, 225-233 (2015).
[208] Rupin, *supra* note 119.

that the proposed implementation of crowdfunding in India will be in the form of equity, debt and fund based crowdfunding.

5.6.GLOBALISATION OF SECURITIES MARKET

There is an increased need for investor protection due to global competition among regulators. While regulating globalised capital market it must be kept in mid that, though exchanges all across the globe will merge but the sovereign investor-protector regimes implemented in different remain intact. Simultaneously, as the capital markets merge and companies look to seek more investment across the globe, the possibility of securities frauds committed by MNC will also increase. The situation will leave the investors vulnerable.[209]

5.7.INSIDER TRADING: CHALLENGES ON DUAL FRONTS.

Section 195 of the Companies Act, 2013 which deals with insider trading apparently intend to include public companies, private companies, and listed companies under its dominion. However, with regard to its applicability on marketable securities, no clarification is provided neither in the statute nor by MCA.[210]

Apparently, the definition of insider trading under Companies Act, 2013 and SEBI (Prohibition of Insider Trading) Regulations, 2015 differs. Companies Act defines and includes the acts of "directors, key managerial persons, any other person or their agents dealing with securities or their agents based on `*non-public price sensitive information'* directly or indirectly."[211] On the other hand, the regulation defines the term 'insider' differently and includes any person who is connected with the company having access to unpublished price sensitive information. Owing to the wider scope of the definition prescribed in the regulation, a case can be initiated against the person by SEBI under it. Hence, the regulations being more specific has an overriding effect and shall prevail over the provisions of Companies Act. Additionally, the penalty will be

[209] Shelley Thompson, *The Globalization of Securities Markets: Effects on Investor Protection,* [41(4)] THE INT'L LAWYER 1121, 1121-1144 (2007).
[210] Avimukt, *supra* note 115.
[211] Companies Act, 2013, No. 18 of 2013§ 195, *available at* http://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf

imposed on the defaulters if proven guilty under Section 15G of SEBI Act, as opposed to the term of imprisonment prescribed under the Companies Act, 2013.[212]

Another problem associated with laws governing prohibition of insider trading is that, one one hand the listed companies are covered under the jurisdiction of SEBI while on the hand unlisted companies are regulated by the RoC i.e. MCA. Since, SEBI (Prohibition of Insider Trading) Regulations, 2015 is a specific law, hence it should prevail. However, Section 195 of Companies Act, 2013 declares nothing about its applicability to the unlisted companies. This has led to non-uniformity and thus, the regulations need reforms. It can justly argued that two sets of provisions should not exist to deal with violations of same nature. This will, undoubtedly bring about confused circumstance when any cause of action arises.

5.8.CONFLICT BETWEEN MULTIPLE REGULATORS

The genesis of apparent conflict between multiple sector regulators vis-a-vis regulation of Capital market can be said to be section 29 of securities Contracts (Regulation) Act, 1956 (SCRA). It is an enabling provision, wherein, the Central Government, which are exercisable by Central Government under the Act, vests SEBI with certain powers. The delegated powers are subject to the conditions provided under the Act. However, the delegation of power is not absolute and that such powers can be withdrawn (however the argument is not feasible to be implemented). In effect, following powers has been delegated:[213]

(a) Power to grant recognition to a stock exchange, under section 4.
(b) Furnishing of Annual Report, under section 7.
(c) Power to direct any stock exchange to amend the rules relating to the constitution of Stock exchange, which includes, admission of new member, readmission of members, qualification, suspension/expulsion, etc. of members of any stock exchange,under section 8.
(d) Power to supersede governing body of any stock exchange, under section 11.
(e) Power to suspend business of a recognized stock exchange, under section 12.
(f) Power to prohibit contracts in certain cases, under section 161.

[212] Saibal, *supra* note 106.
[213] MOHAN, *supra* note 12.

SEBI derives its jurisdiction under the provision of SEBI Act and Companies Act. Under Section 11, 11A, 11B, 11C, 12 and 12A elaborates the powers and functions of SEBI. Section11 (1) accommodates the general and specific functions of SEBI. In the ***Sahara case***, the issue emerged with regard to the jurisdiction of SEBI over unlisted companies. SEBI took cognizance of the matter and under Section 67(3) of Companies Act, 1956 issued a show cause notice to both the companies of Sahara group. SEBI, thereafter, direct both the companies to regulate and deposit information. SHICL appealed to SAT and thereafter to Supreme Court asserting that an unlisted company does not go under the domain of SEBI and is controlled by Unlisted Public Companies (Preferential Allotment) Rules 2003 by the Registrar of Companies and not SEBI. The Supreme Court contemplating Section 55A of the Companies Act 1956 expressed that any public issue by an unlisted company if made to more than 49 people would go under the domain of SEBI. The Court, while applying the doctrine of harmonious construction with Section 55A of the Companies Act and the SEBI Act arrive at such a conclusion. Hence, the conflict of jurisdiction between ROC and SEBI was resolved.[214] Another important case, pertaining to conflict among various sector regulators is that of Etihad Airways – Jet Airways case, wherein, former offered to purchase a 24% share in Jet Airways. The whole transaction was subjected to clearances from concerned sector regulator i.e. SEBI, Foreign Investment Promotion Board and Cabinet Committee on Economic Affairs and CCI.[215] Since, the compliance requirement under the jurisdiction of Foreign investment Promotion Board and Cabinet Committee on Economic Affairs were met, hence GoI approved the transaction. However, since the whole transaction can be, *ipso facto* divided into various spheres, both SEBI and CCI were empowered to exercise their power in their own sphere of jurisdiction. CCI approved the transaction, but SEBI sent a notice to Jet Airways stating that the transaction is in violation of regulation 4 of Takeover Code, 2011.

In a research work published in Indian Law Journal, it is suggested that the conflicts can be harmonised by (a) having a super regulatory body, or (b) providing concurrent jurisdiction to various sector regulator, or (c) concurrent jurisdictional powers of

[214] Pranshu Paul, *Conflicts of Jurisdiction Between SEBI and Other Regulators,* [7(2)] I. L. J. (2007).
[215] *Id.*

various sector regulators, or (d) mandatory consultation and lastly (e) judicial interpretations.[216] The same are summarily discussed as under:

5.8.1. SUPER LEGISLATIVE AUTHORITY

An approach that can be adopted by the Indian legislature is to create a super regulatory body over and above all the regulatory bodies in India. The Raghuram Rajan Committee on financial sector reform (1998), was the first to introduce the notion of establishing a uniform sector regulator in India. However, the report was released weeks before the 1998 global financial crisis and hence no significant change occurred in this regard.[217] A latest development in this regard the recommendation of Financial Sector Legislative Reforms Commission (FSLRC) headed by Justice B N Srikrishna, which suggested a roadmap for implementation of same.[218]

5.8.2. CONCURRENT JURISDICTION

Multiple legislations govern rules and regulations of financial sector in India. Hence, the researcher proposed that: "Another approach as followed by Brazil can be adopted in India, wherein only the sector specific regulator would have jurisdiction on all issues of the sector, comprising of functions of the cross-sector regulator also".[219] The method is also prevalent in few sectors in India, wherein, for e.g. Electricity Regulatory Commissions (ERCs) have concurrent jurisdiction over the competition issues.[220]

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[216] *Id.*

[217] C. R. L. Narsimhan, *A Super Regulator for Financial Stability*, THE HINDU, Mar. 21, 2010 ("Finally, the idea of having a unified financial sector regulator over the medium-term is borrowed from the Raghuram Rajan Committee on financial sector reform. The committee submitted its report in September 1998, days before the global crash. It is unlikely that the committee would have persisted with its recommendations on financial sector regulation if it had released its report a few months later.") *available at* http://www.thehindu.com/business/a-super-regulator-for-financial-stability/article261185.ece (last visited Mar. 17, 2016).

[218] PTI, *Super Regulator Might Soon Become a Reality; Roadmap on FSLRC Soon*, BUS. STANDARD, July 7, 2014 *available at*http://www.business-standard.com/article/finance/super-regulator-might-soon-become-a-reality-roadmap-on-fslrc-soon-114070600412_1.html (last visited Mar. 17, 2016).

[219] Pranshu, *supra* note 214.

[220] Amit Kapur & Mansoor Ali Shoket, *Emerging Challenge in the Regulatory Domain: Clarity on Jurisdiction on Competition Issues in Electricity and Broadcasting Sectors*, MANUPATRA , http://www.manupatrafast.com/articles/PopOpenArticle.aspx?ID=9fc0e102-e715-4701-a640-4182e436c75f&txtsearch=Subject:%20Competition%20/%20Antitrust#f4 (last visited Mar. 17, 2016).

5.8.3. COLLABORATIVE APPROACH.

Under this mechanism, the researcher proposes that: "Collaborative powers under cross-sectors can be given to sector specific regulators"[221]. The Collaborative approach model is followed in Mexico, wherein the specific sector regulator decides only penalty. Whereas, conclusions as to all other preceding aspects of investigation, assessment of fair competition, the judgment is arrived after collaboration of all other concerned sector regulator.

5.8.4. MANDATORY CONSULTATION

Yet another modus operandi for resolving the disputes of parallel jurisdiction of multiple sector regulators, as suggested by the researcher is that of mandatory consultation. "As per the practice in Argentina according to their Law No. 25.156 for example, the competition regulator has to mandatorily consult about the issues in a preliminary manner by the sectoral regulator before it can take cognizance of the matter or pass any order. This kind of a law would create that all cross-sector regulators have to communicate with the sector specific body and take preliminary consultation on the matter."[222]

5.8.5. COURT INTERPRETATION

The Sahara case has been a classic example of judicial interpretation in this context. The case has effectively laid down the principle that, being the matter of public interest and that of protection of investor's interest; both SEBI and MCA should exercise concurrent jurisdiction in the matter.

This, however, ought to be the remedy of last available with parties, regulators intending to get relief from such conflicts. The contention can be supported by the fact, such regulators are founded with sole motive to reduce judicial burden and ensure speedy disposal of matters.

However, the problem associated with Court's interpretation can be summarised as under:

[221] Pranshu, *supra* note 214.
[222] *Id.*

> "The jurisdiction is limited in two important ways: first, the Court can only pass on issues that are brought before it; and second, the Court is constrained, to some extent, by its past decisions and by constitutional and legislative texts. The problem, however, is that those constraints underdetermine the Court's decisions in most cases, so the Court essentially makes its final choice among the legally viable options based on the moral and political values of the Justices, and not simply on the basis of legally binding standards."[223]

As per above discussion, India possess a multiple sector regulatory regime, demarcating their area of operations are of fundamental significance. Each regulator ought to function within the for corners of powers provided under the respective statute of its establishment.[224] In a case pertaining to Chicago Board of Trade and Securities and Exchange Commission it was observed that sector regulators in case of conflicts should not follow 'my way or the highway' approach. The main intent of empowering regulator is to ensure better administration of the specific sector, thereby avoiding head-on conflict.[225]

5.9.LACUNAE IN INVESTOR PROTECTION REDRESSAL MECHANISM.

In spite of the fact that there is a redressal mechanism is in existence, grievances of investors are not addressed adequately and settled to the satisfaction of investors. Various factors as discussed in above points acts as hindrances to settlement of investor's dispute. Notwithstanding the existing framework to comprehend the interest of investors and protection of it, their confidence in investment of their capital has suffered a blow. The Capital Market has been susceptible to fraud, market manipulation and scams related thereto over the years. This has passed on a picture that investors have lost their confidence. The tool to control such frauds has been an adhoc mechanism. It is therefore necessary to comprehend the issues associated with

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[223] Brian Leiter, *Constitutional Law, Moral Judgment, and the Supreme Court As Super-Legislature,* 66 HASTINGS L. JOURNAL 1601 (2015) *available at* http://chicagounbound.uchicago.edu/cgi/viewcontent.cgi?article=11995&context=journal_articles (last visited Mar. 17, 2016).

[224] Gopal Jain, Warring regulators in an undefined world, REDIFF (Apr. 26, 2010), *available at* http://business.rediff.com/column/2010/apr/26/guest-warring-regulators-in-an-undefined-world.htm

[225] *Id.*

these scams, emerging out of multiple factors and create a permanent mechanism to address them.

Some Major Indian Scams

1. **"Harshad Mehta scam (market manipulation), 1992:** the scam pertains to market manipulation is one of the foremost stock market scams in India. The manipulation was the result of prevalent inefficiencies in in system of GoI bond market transaction. Rs. 54 billion were involved in the scam amidst initial the years of economic liberalisation."[226]

2. **"MNCs efforts at consolidation of ownership, 1993:** A Rs. 5000 billion scam took place in 1993 wherein the companies reportedly were involved in several transactions to consolidate their ownership by issue equity shares to their controlling groups at steep discount. It affected the interest of investors."[227]

3. **"Vanishing companies scam, 1993–94:** The scam took places 1993-94 when the stock market index rocketed to 120 per cent increment. Taking advantage of the situation 3911 companies raised over Rs. 25,0000 million and vanished. They didn't started their business project for which they raise money as promised in the prospectus. The scam was the result of government's decision to allow obscure companies to make public issues at large share premium. Therefore, the companies and investment banks mislead in the prospectus issued, thereof."[228]

4. **"M. S. Shoes (insider trading), 1994:** The scam pertains of insider trading, wherein a majority shareholder of the company influenced brokers Stock Exchanges in order to manipulate share prices erstwhile the rights issue. Consequently, the share prices crashed and the broker defaulted. Bombay

[226] FERNANDO, *supra* note 75.
[227] *Id.*
[228] *Id.*

Stock Exchange was forced to close its operation for 3 days. The cam involved a huge amount Rs. 170 million."[229]

5. **"Sesa Goa (price manipulation at BSE), 1995:** This was caused by two brokers who later failed on their margin payments on leveraged positions in the shares. The exposure was around Rs. 45 million."[230]

6. **"Rupangi Impex and Magan Industries Ltd. (price manipulation), 1995:** Rs. 11 million market scam took place as the majority vis-avis dominant shareholder were involved in the practices of price manipulation."[231]

7. **"Fraudulent delivery of physical certificates, 1995:** by the year 1995, post liberalisation, anonymous trade practices and nationwide settlement of transactions were frequent. Resultantly, there were fraudulent delivery of shares into the market."[232]

8. **"Mutual funds scam, 1995–98:** The scam pertains to unethical banking of public sector banks which allegedly raise Rs. 15,0000 million crore by promising huge returns to investors; However, the scheme collapsed and the money of investors was lost."[233]

9. **"CRB scam through market manipulation, 1997:** the scam exposed the regulatory ineffectiveness of SEBI and RBI to prevent the cases of market manipulation. In this instance, Charted Accountant; which included finance and non-finance companies created CRB Group of companies. The company's main objective was to manipulate market. Allegedly, the non-finance companies provided money to finance companies to manipulate prices and the finance companies used to generate money from external

[229] *Id.*
[230] *Id.*
[231] *Id.*
[232] *Id.*
[233] *Id.*

sources and manipulated performance numbers. It involved an amount of Rs. 7 billion."[234]

10. **"Market manipulation by Harshad Mehta, 1998:** this was another scam done by Harshad Mehta. This time he colluded with the management of BPL, Sterlite and Videocon and manipulated the share prices. Resultantly, the share market crashed. Allegedly, there were tamping of records done by the top management of the BSE in order to avoid a trading payment crisis. The case highlights the failure of regulatory framework of SEBI."[235]

11. **"Price manipulation by Ketan Parikh, 2001:** Widely known as Ketan Parekh scam were allegations of fraud in IT stock prices fall crisis with respect to an illegal *badla* market at the Calcutta and banking fraud. He identified companies for investment which were listed as ***high growth companies with a small capital base***. Exploited this factor (low liquidity) to his advantage. These companies were known as K10 companies. The shares were held through KP's company, Triumph International. He started trading of these shares within the network of his own companies at no profit no loss with the malafide intention of creating buying pressure for shares of K-10."[236]

12. **"Dramatic slide in the stock market, 2004:** Between May 14 and 17 2004, there was a dramatic fall in the scrips of Reliance, Hindustan Lever, State Bank, Infosys and ONGC. On May 17, Sensex fell by 11.14 per cent. SEBI has found a dozen players whose names have not been divulged, were responsible for the price rigging and have been put on notice. Earlier on May 14 also, the stock market crumbled. On that day, the largest loser in sensex was the State Bank of India with a dip of 14.77 per cent. In all these falls, the market capitalisation worth millions of rupees was wiped out and consequently investors' confidence was badly shaken.[3]In the aftermath of its investigations, in May 2005, SEBI banned the Swiss investment firm USB Securities from issuing participatory notes and other off-shore

[234] *Id.*
[235] *Id.*
[236] *Id.*

derivative instruments for one year for not cooperating in the process of investigation by the market regulator."[237]

13. **"Satyam computer scam, 2009:** One of the most recent scam that caught the headlines of news is Satyam computer scam. The founder Ramalinga Raju, admitted openly about his involvement in this scandal. He was involved in the practices of falsifying accounts, creation of fictitious assets, and embellishment of profit of the company. Meanwhile, none of the BOD or the employees was aware about such happenings in the company. Raju showed in the balance sheet of the company that the quarter ending on 30 September 2007, it had a bank balance as inflated case of upto Rs. 0.4 billion rupees. At the time of fraud, the company was the 4th largest computer services provider company in India."[238]

Regardless of these noteworthy advancements and reforms that took place, the aforesaid scams testifies that the measures adopted aren't sufficient to deal with the challenges and that the capital market has been on a decline. However, the market recuperated significantly and has sensed an upward thrust (post Sahara and Satyam). Yet, the securities market confronts numerous difficulties and issues that should be determined.

While bringing future reforms, the authorities should be mindful of the severe consequences of scams and the standard to control them should be enhanced. Firstly, the mechanism of investor education and awareness need an urgent up-gradation otherwise it impedes corporate governance and flow of information. Secondly, the legal system should be responsive to the need small investors and provide them with quick grievance redressal. Thirdly, the entire mechanism to trade securities should be more straightforward and transparent. Bentham's theory of utilitarianism can be invoked to argue that, disclosure norms should be such that it provides maximum benefits to the maximum investors. The company should not be allowed to take advantage of legal loopholes, deny market data, etc. to the investors as it a prerequisite for making wise investment choices, and attain market efficiency. Fourthly, there should be strict screening of all instance of insider trading, fraud,

[237] *Id.*
[238] *Id.*

market manipulation. Lastly, in order to improve the trading situation, payment mechanism, etc. the need arises to integrate stock, which is largely the trend in emerging economies of the world.[239]

[239] Rabi, *supra* note 57.

CONCLUSION

Investor protection is the driving force for the growth and development of capital market. Once the investors are assured that they are protected, they tend to invest with utmost confidence, which is a positive sign for a developing economy like India. Development if capital market and protection of investor's interest are coextensive. It accelerates the economic development by, firstly, increasing the savings; secondly it converts the savings into investment and thirdly, it eases the procedure of investment. *In toto,* it brings up productivity and increases economic development.

An investor protection regime is the combination of norms governing the same as well as their proper implementation. An essential attribute of investor protection regime is to avoid inequality among small and big investor. At the same time it must also be flexible with regard to future prospects. However, the possibility of abuse of powers cannot be ruled out, despite of having a sound investor protection regime. Under such circumstances, a sustainable legal regime plays a vital role in protection of investor's interest; which in turn is a sine qua non for orderly development if capital markets. The statement is true with regard to any jurisdiction and particularly in context of India. The sustainability of investor protection regime also proximately relates to a free functioning judiciary; as already discussed in previous chapters of this report.

As a primary regulator of capital market, SEBI has undertaken a number of reformatory steps. Some has been successful; however, some still lacks necessary force to be complied in spirit. This is chiefly true in context of investor awareness and education regime. Explaining the lacuna in its implementation, it can be argued that a little appears has been initiated to comprehend the needs of investors and enable them to take mindful decisions. This aspect was highlighted by the committee formed after Ketan Parekh scam and still the situation remains marginally same.

The reason can identified as the present nature of regulatory regime. Over the years, the regulatory regime has evolved as ad-hoc mechanism; after a scam has been noticed. The measures adopted are essentially preventive in nature. It therefore, leaves a lot of scope for market manipulation. The regulators have not concentrated on

consolidation the internal mechanism to serve the interest of investors. Therefore, in view of the aforesaid, it can be argued that owing to a non-conceptual approach the initiative taken by SEBI concerning investor protection has been, at various instances, proven insignificant and ineffective. The same can be testifies from the fact that SEBI was unable to check reoccurring scam in capital market.

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