

# Understanding SEBI: India's Regulatory Authority For Financial Markets

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**Abstract:** *The project titled "Understanding SEBI: India's Regulatory Authority for Financial Markets" delves into the pivotal role played by the Securities and Exchange Board of India (SEBI) in overseeing India's financial markets. This brief study offers a comprehensive insight into SEBI's historical evolution, its statutory framework, and its functions in regulating securities and commodity markets. It also explores the impact of SEBI on market integrity, investor protection, and the broader financial ecosystem of India. By examining SEBI's structure, powers, and responsibilities, this project aims to provide a concise yet informative overview of the organization's significance in the financial landscape of India.*

**Keywords:** Securities and Exchange Board of India

## I. INTRODUCTION

The Securities and Exchange Board of India (SEBI) functions as the overseeing authority for the securities and commodity markets in India, operating under the administrative jurisdiction of the Ministry of Finance within the Government of India. Its inception dates back to 12 April 1988 when it was established as an executive body, and it later gained statutory authority on 30 January 1992 through the SEBI Act, 1992.

### Historical Background

The inception of the Securities and Exchange Board of India (SEBI) in 1988 marked the beginning of regulatory control over the securities market in India. Initially established as a non-statutory entity, its transformation into a statutory and independent organization occurred with the enactment of the SEBI Act in 1992, which became effective on January 30, 1992. SEBI's headquarters are situated in Mumbai's BandraKurla Complex, and it further extends its reach through regional offices in New Delhi, Kolkata, Chennai, and Ahmedabad, catering to the northern, eastern, southern, and western regions of the country.

Before SEBI's establishment, the regulatory authority for securities lay with the Controller of Capital Issues, acting under the ambit of the Capital Issues (Control) Act of 1947.

The governance structure of SEBI comprises the following key roles:

The Chairperson, who is nominated by the Union Government of India.

Two members, who are officers from the Union Finance Ministry.

One representative from the Reserve Bank of India.

The remaining five members are nominated by the Union Government of India, with a stipulation that at least three of them must serve as whole-time members.

### Objectives of the Securities and Exchange Board of India (SEBI):

**Investor Protection and Education:** SEBI's foremost objective is to protect and educate investors. It aims to safeguard the interests of investors by implementing various measures such as the introduction of modern trading systems, settlement procedures, and dematerialization of securities. SEBI also provides information and guidance to help investors make well-informed decisions. It enforces rules governing corporate reorganization, securities issuance, and trading to maintain market integrity and protect investors.

**Resolution of Investor Complaints:** SEBI is committed to facilitating the resolution of investor grievances. It establishes a comprehensive mechanism for addressing complaints against listed companies and intermediaries. Through meetings and reminders, SEBI encourages companies and intermediaries to address investor issues promptly. In cases of non-

compliance with regulations, SEBI ensures appropriate enforcement actions. Stock exchanges and depositories have an arbitration structure to resolve investor complaints, and the investor protection fund assists in compensating investors in case of broker default. Additionally, the depository is responsible for reimbursing investors for losses resulting from depository negligence.

**Regulation of Capital Markets:** SEBI plays a pivotal role in regulating the Indian capital markets. The Capital Markets Division of the Department of Economic Affairs enforces SEBI's regulations. Within the framework of SEBI's laws, this division:

- Exercises preventive control over the capital markets.
- Promotes the establishment of self-regulatory bodies.
- Oversees and governs the operation of securities markets and stock exchanges.
- Formulates regulations to prevent systemic misconduct.
- Provides oversight and direction to the complaints department.
- Fosters educational opportunities for investors.

**Code of Conduct for Mutual Fund Intermediaries:** SEBI prioritizes investor interests and takes proactive measures to protect them. To ensure safe distribution, selling, and advertising practices, SEBI issues Mutual Fund Regulations and guidelines. Mutual funds are mandated to comply with SEBI's guidelines for preparing literature related to any scheme, including the Scheme Information Document (SID), addenda, performance reports, fact sheets, Statement of Additional Information (SAI), portfolio disclosure, and brochure. These measures help maintain transparency and accountability in the mutual fund industry, benefiting investors.

#### **Functions of SEBI:**

**Protective Functions:** SEBI serves a protective role, ensuring the protection of investors and the integrity of financial markets. It accomplishes this through actions such as monitoring for price manipulation, promoting fair market practices, enhancing investor awareness, and prohibiting fraudulent activities and unfair trade practices.

**Regulatory Functions:** The regulatory functions of SEBI aim to oversee and regulate the operations of financial markets. These functions encompass various activities, including:

- Formulating codes of conduct and guidelines for the effective functioning of corporate and financial intermediaries.
- Regulating corporate takeovers.
- Conducting audits and inquiries into market operations.
- Registering brokers, merchant bankers, and other market participants.
- Levying fees to support regulatory activities.
- Exercising and implementing regulatory powers.
- Regulating and registering credit rating agencies.

**Development Functions:** SEBI also plays a vital role in the development of financial markets. Its development functions include, but are not limited to:

- Providing training to intermediaries to enhance their capabilities.
- Promoting fair and transparent trading practices while curbing malpractices.
- Conducting research to better understand market dynamics and trends.
- Encouraging the establishment of self-regulatory organizations.
- Facilitating the buying and selling of mutual funds through Asset Management Companies (AMCs) via brokers.

#### **Powers of SEBI**

SEBI possesses a range of powers to effectively fulfill its functions:

**Quasi-Judicial Powers:** SEBI has the authority to make decisions regarding deceptive and unethical activities in the securities market. It is responsible for setting rules and regulations related to the capital markets to ensure fairness, transparency, and accountability.

**Quasi-Executive Powers:** SEBI can enforce its rules and regulations, prosecute offenders, and take legal actions to maintain market integrity. It also has the authority to inspect books of accounts and relevant documents in case of rule violations.

**Quasi-Legislative Powers:** To protect the interests of investors and ensure market stability, SEBI is empowered to create rules and regulations. This includes setting listing requirements, disclosure norms, and regulations to prevent insider trading.

SEBI's combination of protective, regulatory, and development functions, along with its powers, is crucial for maintaining the integrity of India's financial markets and protecting the interests of investors.

#### **Administration of SEBI:**

The Securities and Exchange Board of India (SEBI) is administered by a dedicated team of officials and personnel working collaboratively to regulate and oversee the Indian securities market. The core administrative functions of SEBI encompass the following:

**Regulatory Framework Formulation:** SEBI plays a pivotal role in shaping the regulatory landscape of the Indian securities market. It is responsible for crafting and issuing regulations, guidelines, and recommendations that govern various aspects of the market. This includes establishing rules pertaining to disclosure standards, listing requirements, and regulations governing market intermediaries.

**Registration and Oversight:** SEBI holds the authority to register and monitor various market intermediaries, which encompass entities such as mutual funds, stockbrokers, and depository participants. Periodic assessments are conducted to ensure compliance with regulatory standards.

**Market Surveillance:** SEBI conducts rigorous market surveillance operations aimed at detecting and preventing activities like insider trading, market manipulation, and other fraudulent practices. This involves monitoring trading activities, scrutinizing market data, and employing necessary enforcement measures to maintain market integrity.

**Investor Protection:** SEBI is dedicated to fostering ethical conduct within the securities industry with the primary objective of safeguarding the interests of investors. SEBI encourages companies to provide investors with comprehensive disclosures and takes legal action against any entities engaged in fraudulent practices that harm investor interests.

**Enforcement Measures:** In cases where market participants violate securities rules or regulations, SEBI has the authority to initiate enforcement actions. These actions may include penalties, legal proceedings, or restrictions imposed on individuals or companies engaged in trading securities.

**Market Development:** SEBI plays a pivotal role in advancing and nurturing the Indian securities market. Beyond investor protection, it actively promotes innovation, expands the market, and introduces new financial products. By facilitating market development, SEBI contributes to the growth and vibrancy of the Indian securities market.

The administration of SEBI entails a multifaceted approach to ensure the proper functioning of the securities market, protect investor interests, and encourage sustainable market development. SEBI's regulatory, oversight, and enforcement functions collectively work to maintain market integrity and enhance investor confidence.

#### **Description of SEBI's Role in Capital Markets:**

The Securities and Exchange Board of India (SEBI) plays a multifaceted role in the capital markets of the country. Here are its key functions:

**Rulemaking and Stock Exchange Oversight:**

SEBI possesses the authority to establish and enforce rules that regulate stock exchanges in India. An example of this is SEBI's role in defining trading hours, such as the stipulated 9 AM to 5 PM trading window.

**Licensing and Oversight of Dealers and Brokers:**

SEBI is responsible for licensing dealers and brokers operating in the capital markets. It also extends its purview to certain financial products, like ULIPs, ensuring that they are compliant with regulations. This oversight is aimed at safeguarding investor interests.

**Fraud Prevention and Insider Trading Regulation:**

SEBI wields significant powers to prevent fraud within the capital market. It can impose trading bans on brokers involved in fraudulent and unfair trade practices and levy penalties on intermediaries engaged in insider trading.

Mergers, Acquisitions, and Takeovers:

SEBI monitors and regulates mergers, acquisitions, and takeovers of companies in the capital market to ascertain that these activities are conducted in a manner that promotes business development rather than harming market competition.

Performance Audits of Stock Markets:

SEBI conducts performance audits of various Indian stock exchanges to enhance transparency in their operations, ensuring the fair and efficient functioning of these platforms.

Regulation of Carry-Forward Transactions:

SEBI stipulates that carry-forward transactions in share trading should not exceed 25% of a broker's total transactions and imposes a 90-day limit for carrying forward such transactions.

Collaboration with ICAI (Institute of Chartered Accountants of India):

SEBI maintains a collaborative relationship with ICAI, which is responsible for accrediting auditors of companies. This partnership aims to enhance transparency in auditing practices, particularly after the Satyam Scam, by ensuring that Chartered Accountants adhere to ethical standards.

Introduction of Derivative Contracts on Volatility Index:

To mitigate investor risk, SEBI permits stock exchanges to introduce derivative contracts based on the Volatility Index, subject to specific conditions.

Portfolio Management Reporting:

SEBI can require portfolio managers to submit reports to assess the performance of the capital markets, thereby ensuring transparency and adherence to regulatory standards.

Investor Education:

SEBI conducts regular workshops and educational initiatives to empower investors with the knowledge and information they need to make informed investment decisions. These initiatives contribute to investor confidence and market awareness.

SEBI's multifaceted role encompasses rulemaking, oversight, enforcement, and investor education, all aimed at promoting market integrity and safeguarding investor interests in the Indian capital market.

## **II. PROMOTION AND REGULATION OF SELF REGULATORY ORGANISATIONS**

During the 1995-96 period, SEBI (Securities and Exchange Board of India) implemented various initiatives aimed at both promoting and regulating self-regulatory organizations (SROs). These SROs played a vital role in ensuring compliance with rules and regulations in their respective sectors. Here are the key measures taken by SEBI during this time:

**Association of Merchant Bankers of India (AMBI):** SEBI granted recognition to AMBI, enabling them to establish professional standards for efficient services and best practices in merchant banking and financial services. The primary objectives were to encourage healthy business practices and oversee compliance with statutory rules and regulations within the merchant banking industry. AMBI, in collaboration with SEBI, worked on enhancing disclosure standards in offer documents and ensuring systematic compliance with statutory requirements.

**Association of Mutual Funds of India (AMFI):** SEBI facilitated the formation of the Association of Mutual Funds of India (AMFI). This organization acted as an SRO for the mutual fund sector. Regular consultations between SEBI and AMFI members were conducted to address various issues affecting mutual funds. In February 1997, SEBI held a meeting with mutual fund trustees to discuss their responsibilities in overseeing mutual funds, especially in the context of the SEBI (Mutual Funds) Regulations of 1996.

**Association of Custodial Agencies of India (ACAI):** Following the introduction of SEBI (Custodians of Securities) Regulations in 1997, custodians of securities formed ACAI. Although ACAI was in its early stages, SEBI engaged in a dialogue with ACAI to streamline custodial practices. The aim was to ensure that custodians operated in tandem with clearing and settlement systems. ACAI also communicated challenges faced by custodians while serving their clients, which primarily included foreign institutional investors, domestic mutual funds, financial institutions, corporates, and high-net-worth individuals.

**Registrars Association of India (RAIN):** RAIN was established as an SRO for registrars to an issue and share transfer agents. This organization played a crucial role in setting and upholding standards within its section

In summary, during the 1995-96 period, SEBI took various steps to encourage the formation of self-regulatory organizations and ensure that these organizations actively promoted and maintained high standards, compliance, and best practices within their respective industries. These initiatives were integral to the efficient functioning of the Indian financial markets.

#### **SEBI's Role in a Public Issue:**

**Mandatory Filings for Public and Rights Issues:** Companies planning to make a public issue or a rights issue of securities worth more than Rs 50 lakhs are required to submit a draft offer document to SEBI for its review and observations. SEBI plays a critical role in ensuring that the offer document complies with regulatory requirements.

**Observation Letter:** SEBI reviews the submitted offer document and issues an observation letter with its feedback and observations. This letter is valid for a period of three months from the date of issuance, and the company must open its issue within this timeframe.

**No SEBI Filing for Preferential Allotment and QIP:** In the case of preferential allotment and Qualified Institution Placement (QIP), there is no requirement to file an offer document or notice with SEBI. However, in QIP, the merchant banker handling the issue is responsible for filing the placement document with stock exchanges to make it available on their websites.

#### **Role Clarifications:**

(a) **Shift from Controller of Capital Issues:** Before the early nineties, the Controller of Capital Issues made decisions regarding a company's entry into the market and the pricing of securities for public offerings. However, with the establishment of SEBI and its disclosure-based regime, companies have gained the freedom to determine the issue price of their securities without regulatory interference. This flexibility allows them to take advantage of market forces.

(b) **SEBI's Governance Through DIP Guidelines:** SEBI governs primary issuances through its SEBI (Disclosures and Investor Protection) guidelines, commonly known as the DIP guidelines. These guidelines were introduced in 1992 and have since undergone multiple amendments to adapt to the evolving market environment. They provide a comprehensive framework for companies issuing securities to the public.

(c) **Compliance with DIP Guidelines:** Companies planning to raise funds through fresh issuances of securities in the primary market must ensure compliance with the SEBI (DIP) Guidelines, 2000. Merchant bankers, registered with SEBI, serve as specialized intermediaries responsible for conducting due diligence and ensuring compliance with these guidelines before filing the offer document with SEBI.

(d) **SEBI's Examination of Compliance:** SEBI, through its officials at various levels, scrutinizes compliance with the DIP guidelines. The regulatory body ensures that all relevant and material information is adequately disclosed in the draft offer document. This scrutiny helps maintain transparency and investor protection in the primary market.

### **III. ROLE OF SEBI IN PRIMARY & SECONDARY MARKET**

The Securities and Exchange Board of India (SEBI) plays a crucial role in both the primary and secondary markets, serving as the regulatory authority to protect the interests of investors and promote the development of the securities market. Let's reframe its role in these two markets:

#### **Primary Market:**

**Regulation of New Issuance:** In the primary market, SEBI oversees the issuance of new securities by companies, governments, or public sector institutions. It ensures that these entities follow necessary regulations and disclosure requirements.

**Investor Protection:** SEBI's primary goal is to safeguard the interests of investors by ensuring that they receive accurate and timely information about the securities being offered. This involves setting standards for disclosures in prospectuses and other documents.

**Market Development:** SEBI fosters the development of the primary market by regulating the underwriting process, which involves securities dealers. It plays a pivotal role in maintaining the integrity and credibility of initial public offerings (IPOs).

#### **Secondary Market:**

**Market Surveillance:** In the secondary market, SEBI maintains oversight to monitor trading activities and protect investors from fraudulent or manipulative practices. It enforces rules and regulations to maintain market integrity.

**Price Discovery:** SEBI's presence in the secondary market helps facilitate the discovery of fair market prices for securities. This is essential for investors and traders to make informed decisions based on market dynamics.

**Regulation of Trading:** SEBI ensures that brokers and traders in the secondary market operate within the framework of established rules and regulations, maintaining fair and transparent trading practices.

**Investor Confidence:** By regulating the secondary market, SEBI instills confidence in investors that they can trade securities safely and transparently, which is vital for the overall health of the financial markets.

#### **IV. CONCLUSION**

In conclusion, SEBI's role in both the primary and secondary markets is pivotal for the proper functioning of India's financial ecosystem. It not only safeguards the interests of investors but also fosters the development of the securities market, ensuring transparency, fairness, and integrity at every level of trading and investment.

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