

[2023] 151 taxmann.com 552 (Article)

Investigation Under Sebi Act, 1992 PART-I**MAHI YADAV**

Special Public Prosecutor (SPP), Union of India. Standing Counsel for CGST & ED

OUTLINE :

The entire Indian stock market collapsed after Harshad Mehta (Wikipedia) scam in 1992, resulting in the loss of nearly 40% of the market value, or \$1 billion. This prompted the authorities to re-evaluate and restructure existing financial systems, including the implementation of a totally reformed stock transaction system and setting up of an online security system. One of the major recommendations given by the Narasimham Committee was the establishment of an independent regulatory authority *i.e.* the Securities and Exchange Board of India (hereinafter referred as "**Board**"¹) and enactment of the Securities and Exchange Board of India Act, 1992 (hereinafter referred as "**Act**")² for the securities² market to replace the fragmented and ineffective regulatory structure.

SEBI is the regulatory authority in India responsible for overseeing the securities market in order to maintain market integrity, protect investors, and encourage financial development in the market.

INVESTIGATION :

The Act mandates the Board to conduct investigations, by conducting thorough investigations and taking appropriate enforcement actions, SEBI plays an important role in deterring potential wrongdoers, maintaining fair market practices, and promoting a transparent securities market, such investigations are important to ensure the integrity of the securities market.

a. Initiation of Investigation:

An investigation is often initiated on a reasonable basis of belief that there has been a violation of Securities Laws or Regulations or that a securities transaction is being handled in a manner that is detrimental to investors³, including any past transactions because the Act is retrospective in nature. The Hon'ble Madras High Court in *Ritu Devi v. Securities and Exchange Board of India*⁴, has reiterated the statement in "*Para 22.....which clearly means the past transactions as well. Therefore, these two clauses are to be read disjunctively and not conjunctively, because even for past transactions the section 11-C (1) (b) applies*". Further, SEBI appoints an officer (hereinafter

referred as "investigating authority⁵") to conduct the investigation. The officer is responsible to investigate the affairs of such intermediary or persons associated with these securities market or any other person and to report thereon to the Board in the manner provided in Section 11C of the Act⁶.

b. Powers of Investigating Authority:

The officer has powers similar to that of a Civil Court. Furthermore, they can access and seek information from any person specified in 11(2)⁷ of the Act including stock exchanges, depositories, clearing corporations, registrars, and other relevant entities⁸. Moreover, they can also has powers to summon any person involved in the matter being investigated to provide information, produce documents, or appear for examination⁹. The summoned person is obligated to cooperate and provide the required information or documents.¹⁰ The examination is typically conducted under oath and the statements of the examined persons are recorded.¹¹ If necessary, the Investigating Authority has the power to seize and impound relevant documents, records, or other material objects that are deemed important for the investigation, this includes books of accounts, registers, contracts, or any other documents relevant to the matter being investigated, for such period not later than the conclusion of the investigation as he considers necessary and thereafter to return the same to the person, the company *etc.*¹²

c. Actions by SEBI:

Based on the report submitted by the officers before the Board, Board decides further actions against the suspected persons. These actions may include initiating enforcement proceedings¹³, imposing penalties, issuing directions, prosecuting offenders,¹⁴ or taking any other regulatory measures as deemed necessary or as per legislation to address the violations and safeguard the interests of investors and the integrity of the securities market.

Role of Other Regulatory Authorities/Agencies:

SEBI, may request assistance and cooperation from other agencies in order to finish its investigations properly. These Authorities play an important role in providing essential information, knowledge and expertise in their respective domain, legal support and coordination including legal guidance, interpreting relevant laws and regulations *etc.*, to SEBI in conducting thorough investigations and ensuring effective enforcement of securities laws and regulations. This cooperation enhances the efficiency, credibility, and integrity of SEBI's Regulatory and Enforcement Actions.

Some of the most significant Regulatory Authorities/Agencies are -

1. Financial Intelligence Unit-India (FIU-IND) :

The FIU is the central national agency responsible for receiving, processing, analysing, and disseminating information related to suspicious financial transactions and money laundering.¹⁵ It plays a critical role in investigations involving SEBI by providing intelligence and insights into financial transactions that may be linked to market manipulation, insider trading, or other fraudulent activities. The FIU collaborates with SEBI by sharing relevant financial intelligence, supporting investigations with transactional analysis, and helping to establish connections between entities or individuals involved in suspicious activities.

2. Reserve Bank of India (RBI):

SEBI may seek assistance from RBI, the central banking institution, particularly in cases involving financial institutions regulated by RBI. RBI can provide SEBI with information, data, and expertise related to financial transactions and regulatory compliance.

3. Stock Exchanges :

SEBI works closely with stock exchanges, such as the National Stock Exchange (NSE) and the Bombay Stock Exchange (BSE), to gather information and evidence related to trading activities, market manipulation, and other violations. Stock exchanges provide SEBI with trading data, order details, surveillance reports, and other market-related information.

4. Depositories and Registrars :

Depositories, such as the National Securities Depository Limited (NSDL) and the Central Depository Services Limited (CDSL), and registrars play a critical role in maintaining records of securities ownership and transactions. SEBI may seek information from these entities during its investigations, especially when there are concerns regarding shareholding patterns, insider trading, or manipulation of securities records.

CHALLENGES :

Despite the implementation of the Act and compliance procedures, SEBI and regulatory authorities continue to confront significant challenges in investigation because of the following reasons-

1. Timely unavailability of Information :

In some cases, SEBI may face delays in obtaining information from market participants, intermediaries, or other entities involved in the investigation. This can be due to factors such as deliberate non-compliance, technical limitations, or legal constraints. Such delays can impede the progress of investigations and necessitate legal interventions. In ***Mahesh Kumar Patel v. Adjudicating Officer, Securities & Exchange***¹⁶ "Para 15...Timely submission of information is very important in conducting investigation proceedings and non-cooperation by an entity can be detrimental to the interest of investors and securities market"

2. Jurisdictional Issues :

Determining jurisdiction and establishing the applicability of securities laws in certain cases can be challenging. SEBI's powers are limited to matters falling within the scope of the SEBI Act and relevant regulations. In the matter of *Mahesh Kumar Patel (supra)*, The appellant in this case argued "that they were not registered as an intermediary with SEBI, therefore they were not abide by law. However, the Tribunal upheld SEBI's contention and ruled that the contention of the appellant that it was not within the jurisdiction of SEBI was erroneous."

3. Insider Trading and Market Manipulation :

Detecting and proving insider trading and market manipulation can be challenging due to the covert nature of these activities. SEBI needs to employ advanced data analysis techniques, surveillance systems, and market intelligence to identify suspicious patterns and establish violations. In ***Rakesh Agrawal v. Securities Exchange Board of India***"Inequitable and unfair practices such as insider trading, market manipulation and other security frauds affect the integrity, fairness and efficiency of the securities market, and impair the confidence of investors"¹⁷

CONCLUSION :

It is evident as per above discussion that, SEBI's investigation has played an important role in maintaining the integrity of the Indian securities market, Moreover they also strive to protect investors, maintain market integrity and foster a robust regulatory framework that facilitates long-term growth in the securities market. To address the issues raised above, SEBI can invest in continuous training and development programmes for its investigators in order to improve their knowledge and skills. Additionally, they should also improve cooperation with other regulatory organisations, law enforcement organisations etc.

■ ■

-
1. "Board" means board as defined in Section [2\(1\)\(a\)](#) of the SEBI Act, 1992, read with Section 3 of the SEBI Act, 1992 which states the "Establishment and Incorporation of the Board".
 2. "Securities" means securities as defined in Section [2](#) of the Securities Contracts (Regulation) Act, 1956.
 3. Section [11\(c\)](#) of Securities and Exchange Board of India Act, 1992(India).
 4. [\[2012\] 24 taxmann.com 216/172 SCL 240 \(Mad.\)](#)
 5. Regulation 2(1(d)) of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003, Substituted Vide Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) (Amendment) Regulations, 2022 w.e.f. January 25, 2022.
 6. Regulation 5 of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating To Securities Market) Regulations, 2003.
 7. Section 11(2) of Securities and Exchange Board of India Act, 1992(India).
 8. Regulation 6 (1) of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003.
 9. Regulation 6 (3) of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003.
 10. Regulation 8 of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003.
 11. Regulation 6 (6) of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003.
 12. Regulation 6 (9) of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003.
 13. Regulation 10 of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003.
 14. Regulation 11 of Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003.
 15. www.dor.gov.in
 16. 2005 SCC ONLINE SAT 106
 17. [\[2004\] 49 SCL 351 \(SAT - Mum.\)](#)