
[2023] 152 taxmann.com 419 (Article)

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Date of Publishing: July 18, 2023

Sebi Investigation-Part-II (Criminal Proceedings)



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Outline

Securities and Exchange Board of India (hereinafter referred as "**SEBI**"), as the Country's Regulatory Authority for the securities market, plays a pivotal role in maintaining market integrity and protecting investors interests. After conducting an investigation¹ against the wrongdoers, if the SEBI finds sufficient evidence of criminal/illegal behaviour including Insider-Trading, Market Manipulation, Money Laundering, Forgery or falsification of documents etc., SEBI can initiate criminal proceedings. When SEBI initiates criminal proceedings the matter is typically presented before the appropriate Court for a trial for further investigation and legal action. SEBI itself does not have the authority to conduct criminal trials or impose criminal penalties, instead, it can collaborate with Law Enforcement Agencies such as the Police or the Central Bureau of Investigation (CBI).

The specific outcomes and penalties resulting from criminal proceedings are determined by the Judicial System. If found guilty, individuals or entities involved in the violations may face several penalties, which can lead to fines, imprisonment or other legal consequences as determined by the Courts.

It's important to remember that SEBI's role is primarily regulatory and investigatory, and the decision to pursue criminal proceedings is based on the severity of the violations and the evidence collected during the investigation. The Judicial System will ultimately determine the guilt or innocence of the suspected persons and administer appropriate legal remedies if necessary.

Unveiling Violations through SEBI Investigation:

SEBI's investigation process is comprehensive, meticulous and guided by the principles of fairness and transparency. Upon receiving information or detecting suspicious activities, SEBI launches an inquiry to gather evidence, scrutinize market transactions, and interview relevant parties. These efforts are aimed at uncovering potential violations, such as fraud, insider trading, market manipulation, and non-compliance with disclosure norms. The diligent investigative teams at SEBI leave no stone unturned in their pursuit of truth, employing advanced techniques and collaborating with industry experts to ensure a thorough

examination. In *Rakesh Agrawal v. Securities Exchange Board of India* [2004] 49 SCL 351 (SAT - Mum.), the Securities Appellate Tribunal held that SEBI had the right to invoke Section 24² for a severe offence like insider trading and that it was outside of its authority to overturn its directive to begin criminal prosecution.

The Threshold for Criminal Proceedings

The Legal Framework:

The legal framework for criminal proceedings in the securities market includes various acts and statutes. SEBI Act³, the Securities Contracts (Regulation) Act, 1956 (SCR Act)⁴, and the Depositories Act, 1996⁵ provide the foundation for enforcing securities regulations and prosecuting offenses. These Acts define criminal offenses related to securities violations and outline the powers and functions of SEBI in initiating legal action, it is important to note that SEBI continues to rely on the broad criminal procedure framework established by the CrPC⁶ and does not have a separate criminal proceedings regime.

The Securities Laws (Amendment) Act, 2014⁷ introduced amendments that prescribed for the Central Government to designate a special court for speedy trial of such alleged criminal offences.

Initiating Criminal Proceedings:

While SEBI has regulatory and enforcement powers, criminal proceedings fall within the purview of the judicial system. After conducting the investigation, SEBI may find evidence proving serious criminal offenses which require legal action. These offenses may include intentional misrepresentation, fraudulent activities or acts that undermine the integrity of the securities market. Recognizing the severity of such violations, SEBI refers the case to law enforcement agencies, such as the police or the Central Bureau of Investigation (CBI), to initiate criminal proceedings in the appropriate Court. The Hon'ble Supreme Court in ***Swedish Match AB v. SEBI***⁸, **para no. 106** "...While functioning in its judicial capacity, it has wide discretion. It can initiate criminal proceedings in terms of Section 24 of the Act".

Court Proceedings and Trials include:

- (a) Filing of Charge sheet⁹: After SEBI completes its investigation and refers the case to the appropriate law enforcement agency, such as the police or the CBI, the agency conducts further investigation and prepares a charge sheet. The charge sheet outlines the allegations against the accused, detailing the specific offenses committed under the SEBI Act.
- (b) Court Proceedings: The case is presented before the relevant Court, which could be the Hon'ble Magistrate Court or the Hon'ble higher Court, depending on the nature and severity of the offense. The Court serves as the impartial forum for the Judicial determination of the offense. The accused is notified of the charges and given the opportunity to present a defence.
- (c) Examination of Evidence: During the trial, the prosecution presents the evidence collected during the investigation, including documents, witness testimonies, expert opinions, and any other relevant information. The Court examines the evidence presented by the prosecution, assessing its credibility, relevance, and admissibility. The defence has the opportunity to cross-examine witnesses and challenge the prosecution's evidence. Apart from this, the Court also listens to the arguments of both sides.
- (d) Verdict and Judgment: Based on the evidence, arguments, and application of the relevant Act, the Court arrives at a verdict. If the Court finds the accused guilty beyond a reasonable doubt, it pronounces a Judgment, stating the conviction and specifying the

penalties or sentences to be imposed. The Judgment may include fines, imprisonment, disgorgement of illicit gains, or other penalties as provided for under the SEBI Act.¹⁰

- (e) Appeal Process: Following the Judgment, the accused or the prosecution may have the right to appeal the decision to a higher Court, seeking a review of the Judgment. The Appellate Court assesses the legal arguments, evidence, and application of the SEBI Act, and may either uphold the lower Court's decision, modify it, or order a retrial.¹¹

Compounding of the offences:

Section 24A of the SEBI Act, permit the Securities Appellate Tribunal¹² or a Court before which such proceedings are pending to compound offences brought before it notwithstanding any provision to the contrary in the Code of Criminal Procedure, 1973, provided they are not offences punishable with imprisonment or with fine and imprisonment.¹³ In a circular dated 20 April 2007, SEBI issued guidelines for consent orders under Sections 15T of the SEBI Act and Section 23A of the Depositories Act, 1996, and for compounding of offences under Section 24A of the SEBI Act, Section 22A of the Depositories Act and Section 23N of the Securities Contracts (Regulation) Act, 1956. It noted that compounding of an offence "may cover appropriate prosecution cases filed by SEBI before the criminal courts" and "can take place after filing criminal complaint by SEBI"¹⁴. The Hon'ble Supreme Court in **Prakash Gupta v. SEBI**¹⁵ held that the application for compounding cannot be allowed without SEBI's consent and clarified the interpretation of Section 24A.

Extra-Territorial Criminal Proceedings:

SEBI's criminal proceedings are generally limited to the jurisdiction of India. However SEBI, has been using its powers to frame regulations under Section 30¹⁶ of the SEBI Act, and has enacted several regulations, which have extra-territorial operation. However, its powers do not extend to initiating extraterritorial criminal proceedings against individuals or entities based outside of India. If a violation involves activities conducted outside of India, SEBI may cooperate and collaborate with international regulatory bodies or Law Enforcement Agencies to gather information and evidence. SEBI can share its findings with relevant authorities in other jurisdictions for further action under their respective laws. This helps in promoting cross-border enforcement and ensuring the global integrity of the securities market. In **SEBI v. Pan Asia Advisors Ltd.**¹⁷, the question of extra territorial applicability of laws that are repugnant to the SEBI Act and other regulations was not examined by the Supreme Court which still remains a grey area.

CONCLUSION:

Criminal proceedings in Court are of paramount importance for several reasons. Firstly, they act as a deterrent, sending a strong message that violations of securities laws will not go unpunished. This helps to maintain market integrity, safeguard investor interests, and promote fair practices within the securities market. Furthermore, criminal proceedings in Court foster investor confidence. When investors witness regulatory bodies actively pursuing legal action against offenders, it strengthens trust in the securities market. Investor confidence is essential for market stability, as it encourages participation, attracts investment, and promotes a level playing field for all market participants.

1. Section 11(c) of Securities and Exchange Board of India Act, 1992 (India), read with Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating To Securities Market) Regulations, 2003
2. Section [24](#) of SEBI Act, 1992 which states the provision regarding certain "offences".
3. Section [24](#) of SEBI Act, 1992, read with Section [26\(1\)](#) of SEBI Act, 1992.
4. Section [23](#) & [23M](#) of the Securities Contracts (Regulation) Act, 1956.
5. Section [20](#) of the Depositories Act, 1996.
6. Section [26D](#) of SEBI Act, 1992 which states the provision regarding "Application of Code to proceedings before Special Court".
7. The Securities Laws (Amendment) Act, 2014.
8. [\[2004\] 54 SCL 549 \(SC\)](#)
9. Section 173 of The Code Of Criminal Procedure, 1973
10. Chapter "VIA" of Securities and Exchange Board of India Act, 1992(India), Chapters VI A and VI B containing sections [15A](#) to [15J](#) and [15K](#) to [15Z](#) respectively, inserted by Securities Laws (Amendment) Act, 1995 w.e.f. 25-1-1995.
11. Section [26C](#) of Securities and Exchange Board of India Act, 1992(India)
12. Section [15k](#) of SEBI Act, 1992 states the "Establishment of Securities Appellate Tribunal", Substituted by Part VIII of Chapter VI of the Finance Act, 2017 vide Gazette Notification No. 7, and Extraordinary Part II Section 1 dated March 31, 2017. This shall come into force from April 26, 2017.
13. Section 24A of SEBI Act permits compounding of offences by the court where prosecution proceedings are pending
14. Circular No. EFD/ED/Cir-1/2007
15. [\[2021\] 128 taxmann.com 362/167 SCL 560 \(SC\)](#).
16. Section 30 of Securities and Exchange Board of India Act, 1992 which states the provision regarding "Power to make regulations."
17. [\[2015\] 59 taxmann.com 80/\[2016\] 134 SCL 311 \(SC\)](#).