

Enforcing Investor Protection

Guest Column

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The securities market is, unfortunately, susceptible to manipulation. The securities laws, fortunately, have very powerful provisions to protect investors.

Securities laws belong to a genre which holds that it is not possible to visualise all possible circumstances. For example, the Sebi Act empowers Sebi to regulate not only the intermediaries listed in the Act, but also an intermediary who may be associated with the securities market in any manner. The Act also confers on Sebi substantial powers of subordinate legislation to make regulations to fill up the gaps in laws and deal with matters of detail, which change rapidly with time. This enables Sebi to deal swiftly with any new misdemeanour in the market and keep the laws relevant all the time.

Generally, there is broad separation of powers among the agencies associated with law: the legislature makes the law, the executive administers it and the judiciary enforces it. If any deficiency is noticed while administering or enforcing the law, the legislature amends it and, till that time, a person can operate in the deficient areas with impunity. The securities laws, in contrast, do not follow the strict separation of powers. These confer on Sebi, substantial quasi-legislative and quasi-judicial powers, in addition to executive powers. It makes regulations, adminis-

ters regulations and adjudicates disputes under the regulations. This enables it to make and enforce laws proactively and, preferably, before the harm is done.

All three cognate pieces of securities legislations, namely, the Securities Contracts (Regulation) Act, 1956, the Sebi Act, 1992, and the Depositories Act, 1996, provide for adjudication proceedings for imposition of monetary penalties. It was doubtful for a while if the imposition of monetary penalty under the securities laws required establishment of *mens rea* (guilty mind). It is now conclusively settled with a ruling from the highest court that the adjudication proceedings are not criminal or quasi-criminal proceedings. These deal with failures to comply with statutory civil obligations. Penalty is attracted as soon as non-compliance with the statutory obligation is established even if there is no *mens rea*.

The law prescribes a penalty of a specified amount for most of the violations. For example, if any person indulges in fraudulent and unfair trade practices relating to securities, he shall be liable to a penalty of ₹25 crore or three

times the profit made from such practices, whichever is higher. It also provides that the adjudicating officer shall have due regard to certain factors while determining the amount of penalty. It is not very clear if the adjudicating officer has any discretion or is bound to levy the prescribed penalty irrespective of the gravity of the violation and intention behind it.

As offences under the securities laws are generally civil in nature and it is hard to have evidence for certain offences like unfair trade practice or insider trading, the preponderance of probability is the required level of evidence. Its implication is that if it is likely that a person has committed a violation of law, even if there is no clear evidence to establish it, he will be deemed to have violated the law.

The securities laws empower Sebi to resort to a number of penal actions simultaneously. An intermediary found guilty of market manipulation can be penalised by suspending or cancelling its certificate of registration. The directors or partners of the intermediary can be directed not to deal in securities for a specified period. The violat-

ion can be adjudicated and monetary penalty imposed. The intermediary and its officers can be prosecuted for the same offence. Every violation could, thus, attract multiplicity of proceedings and penalties against the same person for the same offence. This is in addition to penalties levied by self-regulatory organisations such as stock exchanges against brokers. Such multiplicity of actions does not constitute double jeopardy.

The securities laws allow Sebi to issue any directions, including innovative directions matching the circumstance. For example, Sebi routinely directs culprits to disgorge their unlawful gains. It restrains the culprits from holding the position of director of any listed company. It even directs the culprits to make a public offer to acquire shares from public shareholders at a price to be determined by the stock exchange and acquire the shares offered in response thereto. All these directions have been upheld by the higher authorities. In fact, the powers of Sebi to issue directions have no limits provided these are exercised in the interests of investors in securities or the securities market.

These powerful provisions serve as deterrent for potential offenders, while the Securities Appellate Tribunal (SAT) guards against any possible misuse of these provisions. In fact, SAT is singularly responsible for the quality of enforcement process under the securities laws and the development of case laws and jurisprudence.

(The author is former full-time member of Sebi)

Securities laws arm Sebi with very powerful provisions to protect investors

Sebi has substantial quasi-legislative, quasi-judicial as well as executive powers

The Securities Appellate Tribunal, in turn, guards against misuse of these provisions

