ONE CODE TO DISCIPLINE THEM ALL


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THE proposed Securities Markets Code consolidates the three existing laws into a single legislative framework. There are good reasons for such a rationalisation.

Consider this. The Securities and Exchange Board can initiate three types of proceedings—under Section 11B of the Sebi Act, resulting in preventive and remedial directions; enquiry proceedings, which could lead to suspension or cancellation of registration; and adjudication proceedings, which could culminate in the imposition of monetary penalties. Comparable provisions exist under the other two securities enactments as well.

In practice, the same case often triggers parallel proceedings before different authorities within Sebi. Although these proceedings are legally independent, authorities lower in the institutional hierarchy generally tend to arrive at findings similar to those reached at higher levels. Conflicting findings remain possible, too. More fundamentally, the nature of the sanction is determined at the stage of initiating proceedings, before the gravity of the contravention is fully established.

The SMC seeks to address these concerns by consolidating the multiple enforcement tracks into a single adjudicatory proceeding. An adjudicating officer, who may be anyone from a division chief or the chairperson, may determine the contravention first and then impose appropriate outcomes. The framework embeds proportionality and deterrence by requiring consideration of factors such as intent, duration and frequency of the contravention, unlawful gains, investor harm, impact on market integrity, conduct of the noticee before and after the contravention, precedents, and aggravating or mitigating circumstances.

This is a significant improvement. Yet, the consolidation of proceedings also concentrates discretion in ways that may create new risks for consistency, predictability and credibility.

Under the earlier framework, monetary penalties could be imposed by a division chief, while more severe sanctions such as cancellation of registration or market restraints were generally imposed by a whole-time member. There was, thus, a broad correspondence between the seriousness of the contravention, the severity of the sanction and the rank of the authority imposing it. The SMC may enable subordinate legislation to prescribe the level of officer who may act as AO, depending on the case's gravity. Such calibration would strengthen institutional credibility and reinforce confidence in the outcomes.

The SMC also departs from the earlier model under which adjudication procedures were prescribed through rules framed by the government. It instead proposes that procedures be specified through Sebi regulations. This risks collapsing the distinction between rule-making and enforcement, since

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The draft Securities Markets Code proposes a much-needed rationalisation of laws. But it leaves adjudication outcomes dangerously open to discretion. By proposing that procedures be decided according to Sebi norms, not government ones, it risks collapsing the wall between rule-making and enforcement

the same authority would frame the norms, initiate proceedings, appoint AOs, and prescribe the adjudicatory process. Retaining government-made procedural rules would preserve a healthier institutional separation.

The more serious concern, however, lies in the architecture of enforcement discretion. Under Clause 20, the AO may impose one or more of five broad categories of measures: suspension or cancellation of registration, cease-and-desist directions, monetary penalties, disgorgement, and other appropriate directions. The code does not indicate when one remedy should be preferred over another, or when multiple remedies should be imposed.

The discretion widens further once the AO enters a particular category. "Appropriate directions" alone contain a menu of 11 measures, including restraining a person from dealing in securities, suspending trading, annulling trades, and directing divestment of holdings. Each of these then requires further calibration.

These remedies are not interchangeable. Disgorgement is restorative, aimed at stripping away unlawful gains made or losses avoided. Monetary penalties are punitive and deterrent. Market-access restraints are preventive and protective. Suspension or cancellation of registration addresses institutional fitness. Corrective directions seek to restore market integrity or undo the effects of wrongful transactions. A serious contravention may, therefore, justify one remedy or several in combination.

This creates what may be called the code's cascading discretion problem. Even on a conservative estimate, the framework generates a very large matrix of possible enforcement outcomes. The AO must choose not only among sanctions, but also among their combinations, scope, duration and intensity. Without a structured framework, similar cases may attract materially different outcomes. Unless a differentiating principle is clearly articulated, enforcement risks appearing uneven and arbitrary.

The absence of ex ante guidance also weakens deterrence. Regulated entities cannot reliably anticipate regulatory consequences, and enforcement risks becoming less predictable and less normatively coherent. There is also a danger of over- or under-enforcement.

The solution is not to reduce regulatory discretion, but to structure it. A modern securities code should not merely list the medicines available to the regulator; it must also prescribe when, why, and in what combination they are to be administered.

(Views are personal)