

The making of India's regulatory state



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India's transition from a predominantly controlled economy to a market economy is often described in the language of liberalisation, privatisation, and globalisation. But a market economy requires more than the withdrawal of the state from resource allocation. It requires a reconfiguration of the governance edifice so that markets can function with freedom, confidence and integrity.

Changes in governance edifice

That transformation produced two major institutional changes. First, regulations became the bulk of laws governing markets. Traditionally, Parliament could anticipate contingencies and provide for them in legislation. That became increasingly difficult as technology, financial products, business models and market practices changed rapidly, while legislation took much longer to make or amend. Legislation, therefore, had to establish essential principles, objectives and boundaries, leaving details to regulations that could respond quickly to changing market conditions.

Second, regulators emerged to govern markets through regulations. The government had historically been both player and referee: The Department of Telecommunications and Mahanagar Telephone Nigam in telecommunications, Life Insurance Corporation and GIC in insurance, and Unit Trust of India in fund management. A private firm could hardly regard the government as a neutral rule-maker, licensor, investigator, and disciplinary authority, while competing with state-owned enterprises. The separation of the player from the referee led to the creation of regulators: Telecom Regulatory Authority of India (Trai), Insurance Regulatory and Development Authority of India (Irdai), Securities and Exchange Board of India (Sebi) and Competition Commission of India.

As CB Bhavne famously put it: When a problem develops at 30,000 feet, "Fly, we must; repair, we must." A regulator must respond within the existing statutory framework without waiting for legislative repair. The rise of regulators was, therefore, an institutional counterpart of economic liberalisation.

Regulators are, in effect, mini-states: They make regulations, administer them and adjudicate violations. The concentration of quasi-legislative, executive and quasi-judicial functions within the same institution created a new governance challenge: Reconciling functional expertise and regulatory independence with separation of powers, procedural fairness and accountability.

Regulatory architecture 1.0

The evolution of India's regulatory architecture is best understood through the experience of the securities market, which became a laboratory for the regulatory state. Solutions developed there were subsequently adapted, with appropriate modifications, across other domains.

Not all solutions originated in legislation. Some emerged from market practice

or regulatory innovation. Public consultation, consent settlements and disgorgement, for instance, began as regulatory innovations and subsequently found statutory recognition. India's regulatory state was, therefore, shaped not only by Acts of Parliament, but also by institutional experimentation, regulatory practice and learning.

The securities market was a natural starting point for two reasons. First, reform began with freedom of entry, and entry required access to capital. The securities market provided a mechanism for enterprises to raise capital from investors. Second, it was already predominantly private. This required replacing administrative control with market-based rules and institutions. The repeal of the Capital Issues (Control) Act, 1947, in 1992 ended government control over the allocation and pricing of capital, paving the way for market-determined allocation under regulatory oversight.

Sebi was constituted as a non-statutory body on April 12, 1988. The Sebi Act, 1992, gave it statutory status. Its statutory mandate was to protect investors, promote the development of the securities market and regulate it. Regulation and development were deliberately combined because India was not merely policing an established market; it was building market infrastructure. The development of screen-based trading, dematerialisation, derivatives markets, and other institutions illustrates this promotional role.

The 1992 Act established the proposition that market governance could be entrusted to a statutory authority, subject

to significant governmental control. Sebi regulations required prior governmental approval; criminal complaints required prior sanction; and intermediary registration was governed by government-made rules. Its jurisdiction did not cover companies. The

experience demonstrated that a statutory mandate alone could not produce effective regulation.

The 1995 amendments addressed these deficiencies. Sebi's jurisdiction was extended to intermediaries and persons associated with the securities market and to companies in respect of listing and trading of their securities. It was empowered to issue directions to any person in the interests of investors or the orderly development of the market, to prevent conduct detrimental to investors or the market, or to secure the proper management of regulated entities. The government's power to exempt persons from registration was removed, the jurisdiction of civil courts was excluded in matters within Sebi's statutory domain, and good faith protection was extended to Sebi and its officers. The reforms of 1995 may, therefore, be regarded as Regulatory Architecture 1.0: The central objective was functional empowerment.

Appellate review

The Sebi Act, 1992, initially equipped the regulator with the power to suspend or cancel intermediary registrations. That soon proved inadequate. Such sanctions could affect innocent third parties, while misconduct by unregistered persons could fall outside their reach. Prosecution was available, but was neither swift nor warranted for many contraventions. The response was to introduce monetary penalties.

This raised an institutional question: Could Parliament confer coercive financial powers on an agency outside the government? The legislative response was to surround those powers with safeguards.

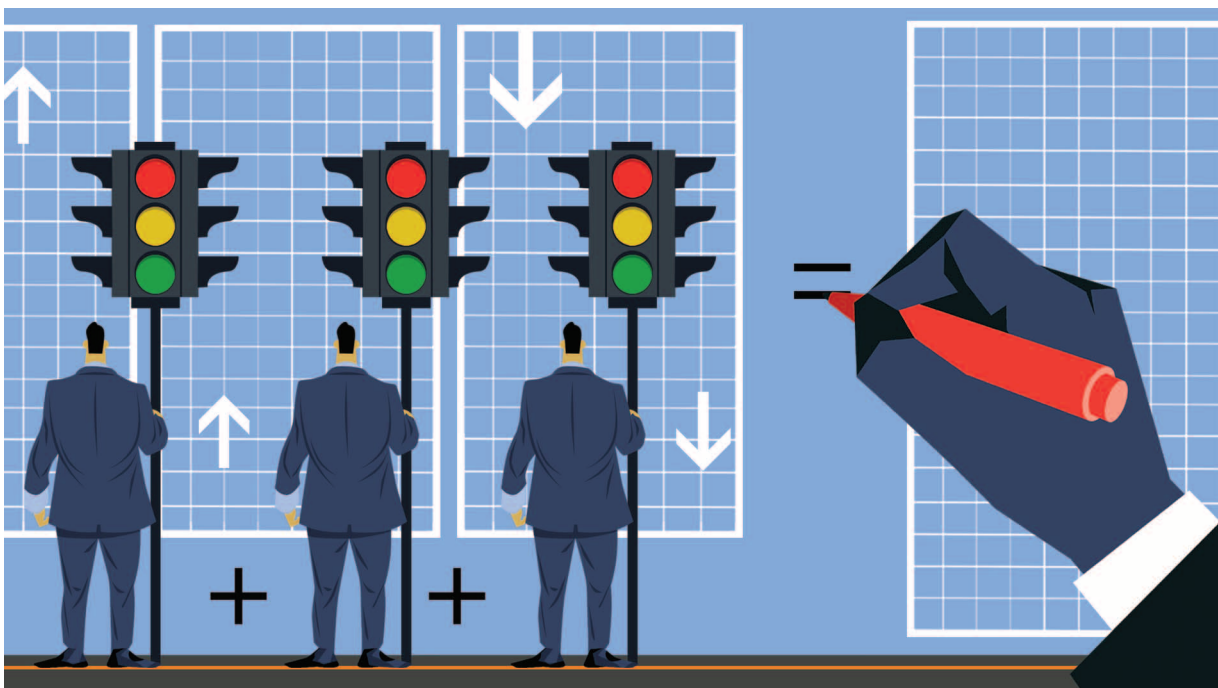


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The statute specified the contraventions and penalties; an adjudicating officer determined whether a contravention had occurred; and an appellate remedy was provided. The Securities Appellate Tribunal (SAT) was established to hear appeals against monetary-penalty orders, with further appeal to the High Court. Sebi could, therefore, regulate and enforce, while an independent appellate forum reviewed the exercise of its coercive powers.

The initial appellate architecture remained fragmented. Sebi's orders went to a government-appointed Appellate Authority, while monetary-penalty orders went to SAT. The weakness became apparent in 1998 when Sebi's order against Hindustan Lever in an insider-trading matter was set aside by the Appellate Authority. Sebi challenged the decision before the Bombay High Court. The episode highlighted the difficulty of subjecting an independent regulator to executive appellate review when the government itself exercised significant powers over the regulator.

The 1999 amendment extended SAT's jurisdiction to appeals against orders passed by Sebi itself. In 2002, it was converted into a multi-member tribunal comprising judicial and technical members, with further appeal to the Supreme Court on questions of law. This institutional innovation travelled across sectors.

The model evolved beyond single-regulator, single-sector tribunals. The Appellate Tribunal for Electricity (APTEL) acquired jurisdiction beyond electricity; SAT acquired appellate jurisdiction over other financial regulators; and the National Company Law Appellate Tribunal (NCLAT) emerged as a broader cross-sector appellate tribunal under the Companies Act and Insolvency and Bankruptcy Code (IBC), subsequently extending to CCI, National Financial Reporting Authority (NFRA) and Insolvency and Bankruptcy Board of India (IBBI).

Finances of the regulator

The financing of a regulator shapes its institutional character. In 1988, Sebi was required to sustain itself through contributions from public financial institutions; in 1991, it received a share of listing fees from stock exchanges. The 1992 Act authorised it to levy fees, but the fee regulations were challenged. The government did not provide grants. Instead, it advanced an interest-free loan of ₹115 crore, which Sebi repaid in full by 2009.

In 2001, the Supreme Court upheld

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Sebi's power to levy regulatory fees, rejecting the argument that the levy was a tax. This was a significant institutional milestone. Registration fees and market-linked charges, together with expanding market volumes, provided Sebi with a stable revenue stream and eventually a substantial surplus. Sebi became a self-financing regulator without grants from the government, establishing an important principle: The regulated sector should bear the cost of regulation.

Regulators are generally empowered to levy fees to meet the costs of carrying out their statutory functions. Many regulators, however, remain dependent on government grants. A sound framework should, therefore, secure adequate and predictable funding without turning regulation into a source of revenue for the sovereign. A regulatory levy should remain a charge calibrated to the cost of regulation, and not become taxation by design or drift.

Acceptance of the regulator

Creating a regulator was only the beginning: its authority had to be accepted by those subject to it, by the executive and by the institutions reviewing its decisions. Sebi's legitimacy evolved through practice, appellate review, stakeholder engagement and judicial clarification.

The securities market had historically operated through exchanges, brokers and other institutions that had developed relationships with government. Sebi required them to accept a new source of authority outside the governmental hierarchy. GV Ramakrishna captured the change memorably: "The road from Dalal Street to Mittal Court is not via North Block." Market participants could no longer approach the finance ministry to influence or reverse regulatory decisions. The creation of an independent appellate route through SAT made that authority contestable without making it subordinate to the executive.

Regulators developed mechanisms for engagement with stakeholders. Sebi was among the first regulators to institutionalise public consultation in regulation-making in 2002. Over time,

consultation became an important feature of Indian regulatory practice. Consultation brought market information and expertise into rule-making and helped address the democratic deficit inherent in delegated legislation. The relationship thus evolved from resistance to engagement.

The executive, too, had to adjust to regulators exercising substantial powers independently of ministries, while it remained accountable to Parliament. The advantages became apparent: Greater continuity and predictability, specialised expertise, institutional distance from day-to-day political pressures and insulation of the executive from unpopular regulatory decisions. The executive, however, retained statutory oversight, including powers to issue policy directions and, in specified circumstances, to supersede a regulator's board. Regulatory independence, therefore, meant freedom from routine administrative control, not independence from the constitutional executive.

Appellate tribunals, meanwhile, had to recognise the limits of their role. The Supreme Court clarified in PTC India Ltd vs CERC and BSNL vs TRAI that while tribunals review regulatory orders, the validity of regulations is a matter for constitutional courts. The institutional division thus became clearer: Regulators make rules and orders, tribunals review regulatory orders, and constitutional courts review subordinate legislation.

Regulatory architecture 2.0

If the 1995 amendments empowered the regulator, the Securities Markets Code Bill, 2025 (SMC), before Parliament, brings the governance of the regulator to the forefront and may be regarded as Regulatory Architecture 2.0.

Drawing on three decades of regulatory experience, judicial scrutiny and global practice, the SMC addresses the concerns that emerged with regulatory maturity: Democratic legitimacy, proportionality, transparency, conflicts of interest and institutional accountability. The governing board is designed as a genuine principal, with independent and part-time participation to hold management accountable. Tenure, eligibility, removal safeguards and conflict-of-interest provisions seek to protect regulatory independence without creating institutional dependence on the appointing authority. Transparency, regulatory impact assessment and periodic evaluation of regulatory effectiveness become elements of statutory governance.

A defining feature is the replacement

of the "circular raj" with a transparent hierarchy of regulatory law. Regulations must be made by the governing board following public consultation, with comments and the regulator's response disclosed. Subsidiary instructions are confined to clarifying ambiguity and prescribing ancillary procedures; they cannot substitute for regulations. Both regulations and instructions are subject to parliamentary scrutiny. Periodic review and regulatory-impact assessment add an evidence-based discipline to rule-making.

Architecture 2.0 strengthens the separation between investigation and adjudication. The SMC consolidates enforcement into a single adjudicatory process, enabling a proportionate response from suspension and cease-and-desist orders to monetary penalties, disgorgement and remedial directions. Natural justice is reinforced through disclosure of the allegations and material relied upon, an opportunity to respond and reasoned orders. A statutory firewall prevents those involved in inspection, investigation, interim orders or settlement consideration from adjudicating the same matter.

Common architecture for regulators

India has spent three decades building its regulatory state, sector by sector. This experimentation was necessary as each sector presented different economic, technological and institutional problems. But regulatory design is still far from settled. Some regulators require prior governmental approval before making regulations; others do not. In some, human resources are governed by government rules; in others, the regulator has greater autonomy. Some governing boards include external or part-time members; others do not. Appointment, tenure, removal, financial arrangements, rule-making procedures and accountability mechanisms also vary. The time has now come to move beyond sector-by-sector design towards a common institutional architecture for regulators.

The Constitution provides the foundational architecture of the state, irrespective of the business of individual ministries. The Companies Act provides a common institutional framework for companies despite their diversity. A similar common framework could provide the basic governance architecture for regulators: Board governance, independence, tenure, appointment and removal, conflicts of interest, rule-making, consultation, regulatory impact assessment, transparency, financial autonomy, inspection and investigation, adjudication, appeals, performance evaluation and accountability. The Financial Sector Legislative Reforms Commission proposed such a framework for financial regulators in 2013, and the Tribunals Reforms Act, 2026, has moved tribunals towards a common framework.

India's regulatory state was not created by a single law or in a single year. It evolved through experimentation, institutional adaptation, judicial clarification, and legislative reform. The Sebi Act, 1992, established the statutory regulator; the 1995 amendments gave it the powers and enforcement architecture necessary to function effectively; and that institutional model travelled across sectors. Regulatory Architecture 2.0 governs Sebi and mandates the exercise of regulatory power with responsibility and accountability. The next step should be a governance code for regulators.

The author played a key role in shaping the Securities Laws (Amendment) Act, 1995, which established Regulatory Architecture 1.0. He subsequently served on five regulatory bodies. Views are personal