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SCAMS, SEBI AND THE INDIAN STOCK MARKET

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ABSTRACT

SEBI, as a regulator, is seen introducing several measures and keep on changing them from time to time to bring Indian stock market as par with international standards.In the past two decades many reforms, frauds and other activities have affected the performance of stock market. Therefore, it becomes essential to unfold different issues that surmount the Indian securities market and to study the way SEBI has been performing to safeguard the interest of investors. Being descriptive in nature, the present study examines the cases taken up by SEBI and the achievement made by SEBI in completing these cases. The present study covers a period of 22 years i.e. from 1993-94 to 2014-15 and it is based on secondary data gathered.The method of percentage change has been used and thepaper includes table and graph. The data has been classified and tabulated using MS-EXCEL.

KEYWORDS: *Stock exchange, SEBI, BSE, Scams, Investigation.*

INTRODUCTION :

The Indian stock market has been advancing leaps and bounds. The growth has not been only in respect of number of listed companies but also in terms of turnover and market capitalization. SEBI, as a regulator, is seen introducing several measures and keep on changing them from time to time to bring Indian stock market as par with international standards.The Indian securities market is a major source of finance for individuals, corporate and government. The regulators in the market make sure that the market participants behave in a desired manner so that the market flourishes continuously and the interest of investors can be protected.

Though the stock exchanges were in action, there was no legislation for their regulation till the Bombay Securities Contracts Control Act was enacted in 1925. This Act came into force to regulate and control certain contracts for the purchase and sale of securities in the city of Bombay (now Mumbai) and elsewhere in Bombay

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Presidency. This Act did not show any significant improvement on securities trading as gambling in shares went unhindered. To regulate the growing dimensions of securities market activity, government realized the need for creating an Act, which can help in the growth of the business. This led to enactment of the Capital Issues (Control) Act in 1947 and the Securities Contracts (Regulation) Act (SCRA) in 1956. These Acts came into existence to check the flow of the capital in the market and to regulate the transaction of securities by exercising control over stock exchanges.

After this, the Companies Act, 1956 came with the rules for companies in relation to issue, allotment and transfer of securities and even for disclosure of the public issues. In the same manner, SEBI Act, 1992 protects investor from unfair means and regulates the market. The responsibility for regulating the Indian securities market is generally carried by Securities and Exchange Board of India (SEBI) and it modifies the rules and regulations from time to time as per the need of the market. These Acts came into existence to prevent unfair trade practices, insider trading and for registration and regulation of all market intermediaries.

Securities and Exchange Board of India (SEBI) Act, 1992

The legislation that governed the Indian securities market till early 1992 was Capital Issues (Control) Act, 1947. In 1991 reforms and liberalization, process began in the Indian securities market. One of the important parts of these reforms was the repeal of Capital Issues (Control) Act, 1947 by Securities and Exchange Board of India (SEBI) Act, 1992. While presenting the Budget for the year 1987-88, the then Prime Minister and Minister of Financesaid *"For a healthy growth of capital market, investor's rights must be fully protected. Trading malpractices must be prevented. Government has decided to set up a separate board for the regulation and orderly functioning of stock exchange and the securities industry."* Hence, in 1988, SEBI was constituted under a resolution of Government of India. On January 30, 1992, the government for giving statutory powers to SEBI passed an ordinance. On April 4, 1992, this Act received the approval of the Parliament as an Act no.15. Hence, SEBI Act came into existence and it discussed all the powers related with securities market operations. On April 12, 1992, Securities and Exchange Board of India (SEBI) got enacted in accordance with the provisions of SEBI Act, 1992. In the speech for year 1992-93, Dr. Manmohan Singh, the then Finance Minister said *"Financial sector reform also includes reform of the capital markets, which will increasingly play a vital role in mobilizing and allocating resources from public. Several initiatives announced in my Budget speech last year since been implemented. The Securities and Exchange Board of India (SEBI), has now been established on a statutory basis. As we gain experience, additional powers will be given to SEBI to strengthen its capability."* In the year 1995, Government of India gave additional powers to SEBI, through an amendment in the Securities and Exchange Board of India Act, 1992.

According to section 3 of SEBI Act, 1992, ***"SEBI is a body corporate having perpetual succession and a common seal with power to acquire, hold and dispose of property, both movable and immovable and to contract, sue and be sued in its own name".*** Every stock exchange comprises of certain rules relating to listing, trading and margining of securities and hence SEBI was formed, with the objective to regulate and promote healthy and orderly development of the Indian Securities Market and to protect investor's interest.

SEBI regulates all the stock exchanges in India. SEBI has its head office at Mumbai and it is under the control of Ministry of Finance. SEBI board consists of one Chairman,one member from amongst the officials of the Reserve Bank of India, two members from the officials of the Ministries of the central government dealing with Finance & Law, and five other membersof whom at least three shall be the whole-time members.

The Chairman has power to direct the affairs of the board and he/she may also use all powers of the board. The central government, who also sets their conditions of service, terms of office and tenure, appoints these members, except the officials of RBI. Central government may also remove any member from board under certain circumstances. The working of the board is divided into four departments, which are headed by an executive director. These departments are primary market department, issue management and intermediaries department, secondary market department and institutional department. Other than these departments, there are two more departments; namely legal and investigation department. SEBI also has a non-statutory advisory committee, which is constituted from the investors, market players and renowned persons associated with the

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Indian Securities Market. It is mandatory for SEBI to submit a yearly report to the central government comprising true and full account of the activities, policies and programs. The Comptroller and Auditor General of India audit these reports.

The Preamble of the Securities and Exchange Board of India explains the basic functions of the SEBI as ***"…to protect the interests of investors in securities and to promote the development of, and to regulate the securities market and for matters connected therewith or incidental thereto."***

SEBI plays an important role in the development and regulation of the Indian securities market. The board provides license to dealers, brokers and other intermediaries to deal in the securities market and it also audits their and stock exchanges performance to ensure fair and safe dealing in the market. SEBI even controls the takeovers, merger and acquisition of companies. SEBI formulates norms, guidelines, rules and policies to control fraudulent activities in securities market. It also keeps on modifying these norms, guidelines, rules and policies to protect the interest of investors.

The Story of Major Scams

In spite of the presence of SEBI, the investors' confidence was beaten down by repeated scams. There were basically two major scams which changed the face of Indian securities market. In 1992, an Indian stockbroker 'Harshad Mehta' was in the headline for BSE security scam. Harshad Mehta belonged from a lower middle-class Gujarati Jain family. He studied in Holy Cross Higher Secondary School, Raipur and was Bachelor in Commerce. He started his working life as an employee of the New India Assurance Company but quit his job, as he got interested towards stock market. He started investing in stock market with his brother Ashwin Mehta and managed to get BSE brokers card. In the year 1990, Harshad Mehta was a well-known name in the Indian stock market for buying shares heavily. Due to his huge buying, by the latter half of 1991, Mehta was called as the 'Big Bull' in the market.

Mehta took advantages of loopholes in banking system and created situations for dramatic rise in SENSEX. For this, he used two small banks that were the Bank of Karad (BOK) and the Metropolitan Co-operative Bank (MCB) to issue fake bank receipts (BRs). As fake BRs were issued, they were passed on to other banks and Mehta use to get money as banks was assuming that they are lending against government securities. He used this money to make rise in stock prices and when there was rise in stock prices, he use to sell shares for profit and return the money due to bank.

On April 23, 1992 journalist 'SuchetaDalal' exposed Mehta's scam. Once the scam exposed, many banks were left holding BRs with no value. The immediate impact of this scam resulted in stay on liberalization, holding banks suffered loss, bank receipts were removed by Reserve Bank of India (RBI), bribery case was charged against P. V. NarsimhaRao and chairman of the Vijaya Bank committed suicide. Mehta was charged with 72 criminal offenses and more than 600 civil action suits were filed against him. Mehta was arrested by CBI and was banned from dealing in the stock market. Mehtadied in 2001, due to heart attack under criminal custody. Interestingly, by the time Mehta died, he was convicted in only one of the many cases filed against him.

In the late nineties, when stock market was in rough phase, the second big bull 'Ketan Parekh' came forward. He was a stockbroker in BSE and was well aware about the powers of online trading. Parekh belonged from a brokers' family and hence created his own trading ring. From 1999 till 2001, this big bull that was trained by Harshad Mehta made huge amount of money by rigging the market by wrong means. He used to be involved in the circular trading to jack up share prices for the benefit of promoters and himself. Promoters through their investment companies provided him funds to jack up share prices. During his peak period, he used to drive a pack of ten stocks known as K-10 stocks. These K-10 stocks included Global Tele Systems, Zee Telefilms, Hindustan Steelworks Construction Limited (HFCL), Silverline, Satyam Computers, Aftek Infosys, DSQ Software, Ranbaxy, Pentamedia Graphics and Vishual Soft. Smelling planned price rigging, the Ministry of Finance ordered SEBI to do an investigation. News of higher exposure of private banks and co-operative banks to stock markets came out and looking at RBI started investigating. In 2008, Ketan Parekh was convicted in stock market manipulation. Since 2001, Parekh is barred to trade in the stock market and won't be allowed till 2017. He was convicted for being involved in Engineering and Technology stocks scam in Indian stock market. After his conviction in 2008

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followed by his ban in 2001, Parekh has been living a very quiet life. In June 2009, the SEBI had banned twenty-six entities for acting as fronts for Parekh to undertake share trading. This scam resulted in reduction in trading cycle from T+7 to T+2, ban on badla system and operates could not carry forward trade in its primitive form.

Both stories were quite similar, only the star cast changed. In the scam of 1992 it was 'Harshad Mehta' and in 2001 it was 'Ketan Parekh' both were big bulls. Ketan Parekh use to make big investment in media companies but he always wanted to be away from publicity whereasHarshad Mehta was media savvy and he made heavy investment in Associated Cement Companies (ACC). Ketan Parekh was from traders background family whereasHarshad Mehta has no such background. The main activity of these two people in the stock market was to purchase stocks at rock bottom prices and then push it up and sell them. In their scam, they involved promoters of companies, certain close cronies and banks. In the Harshad Mehta scam, the controversy was related to bank receipts, while it was pay order in the Ketan Parekh scam. Many were involved in rigging the market, but these two people were among few to be punished. The scam exposed the loopholes in trading system of BSE. Further, SEBI introduced new rules and guidelines to cover the drawbacks of the market.

REVIEW OF LITERATURE

A brief review of selective relevant studies relating to SEBI was done to express the opinion of different researcher. The study conducted by Pandya (1992)on SEBI observes that the SEBI's efforts in the direction of investor protection are wide-ranging and unlimited.Gupta (1996) assessed the regulatory efficiency of the SEBI and found that the stock markets were suffering from price-rigging and even the guidelines planned to protect the investors' interests were not serving the purpose.Sharma (2009)in her research evaluated the working of SEBI by using simple descriptive statistics, ratios and growth rates, correlation, regression, sharpe ratio and probability techniques to find out the results. She found that after establishment of SEBI, there has been growth in the primary market. She also mentioned that secondary market and FIIs have shown tremendous growth after establishment of SEBI. Finally, she concluded that income was the key determinant of investment decision of investors and investors with the experience up to five years were more aware of investors programs compare to the other groups.The study of Sabarinathan (2010) reviews various regulations propagated by SEBI. According to his study SEBI has achieved considerable progress in terms of its oversight on the securities market both in quantitative and qualitative terms. The cost of transaction and the risk of settlement have been minimized and Indian stock market is one of the safest and low cost securities market.

OBJECTIVE OF THE STUDY

Being descriptive in nature, the present study examines the cases taken up by SEBI and the achievement made by SEBI in completing these cases.

JUSTIFICATION OF THE STUDY

In the past two decades many reforms, frauds and other activities have affected the performance of stock market. Therefore, it becomes essential to unfold different issues that surmount the Indian securities market and to study the way SEBI has been performing to safeguard the interest of investors. Generally, investors are fearful in approaching market, as they do not know much about securities and are afraid of scams and frauds. The present study focuses on the cases taken up by SEBI and the number of cases they have completed and hence, this study would be helpful to investors because it will boost the confidence of investors towards the stock market. Also, in the given review of literature,many researchers have examined growth and state of SEBI but there are no studies focusing on investigations conducted by SEBI for redressal of investor's grievances and hence a strong need is felt to study the current concept.

RESEARCH METHODOLOGY

The present study covers a period of 22 years i.e. from 1993-94 to 2014-15 and it is based on secondary data gathered from Annual Report of SEBI and Handbook of Statistics on Indian Securities Market.The method of percentage change has been used as it pinpoints the change occurred in the figure in comparison to the

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preceding year. The paper includes table and graph. The data has been classified and tabulated using MS-EXCEL.

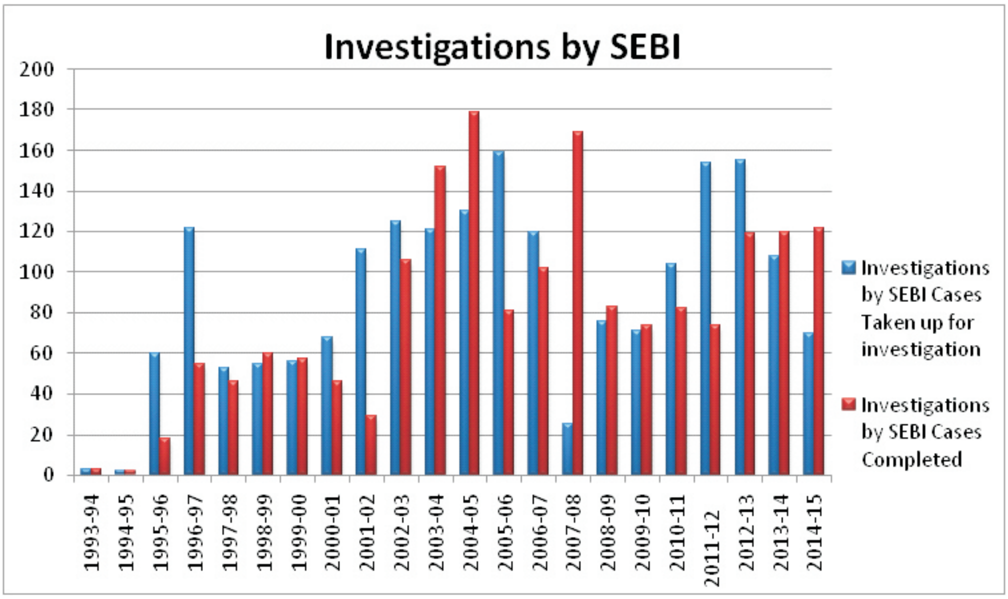
INVESTIGATIONS BY SEBI

Market manipulation on the stock exchanges through fraudulent practices leads to loss of investor confidence. Therefore, by having effective monitoring, SEBI keeps on investigating. Given table shows the investigations conducted by SEBI from the financial year 1993-94 to 2014-15. In financial year 1993-94, SEBI started investigation on cases of price rigging, insider trading and price manipulation. In 1993, there was large trading made by M/s. Jaiprakash industries. Hence, SEBI conducted an investigation and found that there was short selling in the scrip by a large extent and they found stock exchange guilty due to lack of proper monitoring and control. Until 1994-95, not much was seen to be badly inflicting the market and as such, the number of investigations remained in single digit. However, the number of investigations increased in 1995-96 and 1996-97. This was the time when companies started disappearing after raising money from the market and share prices also dropped down and investors lost their money in the Indian securities market. In the year 1998-99, investigations completed were 60 as against 55 cases taken up showing success rate of 109.09 %.

Table 3.3 Investigations by SEBI

Year	Cases Taken up for investigation	Cases Completed	Success Rate (%)
1993-94	3	3	100.00
1994-95	2	2	100.00
1995-96	60	18	30.00
1996-97	122	55	45.08
1997-98	53	46	86.79
1998-99	55	60	109.09
1999-00	56	57	101.79
2000-01	68	46	67.65
2001-02	111	29	26.13
2002-03	125	106	84.80
2003-04	121	152	125.62
2004-05	130	179	137.69
2005-06	159	81	50.94
2006-07	120	102	85.00
2007-08	25	169	676.00
2008-09	76	83	109.21
2009-10	71	74	104.23
2010-11	104	82	78.85
2011-12	154	74	48.05
2012-13	155	119	76.77
2013-14	108	120	111.11
2014-15	70	122	174.29
Total	**1948**	**1779**	

Source: Various issues of Handbook of Statistics on the Indian Securities Market.



Source: Given Table

In 2003-04, 2004-05 and 2007-08, investigations completed were 152, 179 and 169 against the cases taken up for investigations that were 121, 130 and 25. The success rate for 2003-04, 2004-05, and 2007-08 were 125.62%, 137.69% and 676%. This showed that during these years performance of SEBI improved. Whereas during the2010-11, 2011-12 and 2012-13, the speed with which these investigations were being completed was not satisfying. These years accounted for 82, 74 and 119 cases completion where as the cases taken up was 104, 154 and 155. The success rates for these years were 78.85% in 2010-11, 48.05% in 2011-12 and 76.77% in 2012-13. The total figure of investigations started during this period from 1993-94 to 2014-15 was 1948 and investigations completed were 1779, indicating a shortfall of 169 cases, which are yet to be completed. The number cases taken up by SEBI in financial year 2014-15 was 70 but during the same period the number of number f cases completed increased to 122 by giving success rate of 174.29.

The way a head

A stock exchange, through its miscellaneous economic services, serves the nation in numerous ways but it should be kept in consideration that a stock exchange can execute efficiently only under the normal conditions and not under speculative market condition. Under this condition it may adversely affect the entire nation. Thus to overcome this type of conditions SEBI has made more influential and had issued various guidelines for various market players. All these development enhanced the confidence of general investors and they actively take part in the trades at thestock exchange.

Reforms in the Indian securities market, particularly establishment of SEBI has resulted in improved efficiency and safety of issue. Twenty-five years ago when SEBI was set up, the Indian securities market was in the hand of few rich peoples. There were very few issues and instrument dealt were primitive and practices opaque. A complete transformation in the infrastructure of Indian securities market and its regulation has made the market more transparent and efficient one. Further, dematerialization, rolling out red carpets for FIIs and big bang IPO reforms has increased the activities of Indian Securities Market. All these changes can be attributed to the guidelines issued, investor education, disclosures, surveys, dealing with investors' complaints and public interest advertisement done by SEBI.

Although scams committed by rogue traders such as 'Harshad Mehta' and 'Ketan Parekh' also showed the loopholes in the regulation system and hence to avoid this kind of scams, SEBI has been updating its norms and guidelines to empower and protect investors. Although, there were various regulators regulating the Indian securities market but SEBI has set the standard in regulating the system.

Overall, the strengthening of the regulatory system has made the Indian securities market, a better option for investing in. More recently, SEBI initiated an innovative model of resource persons (RPs) tospread financial education across the country bytargeting various groups such as school children,college students, middle incomegroups, executives, homemakers,retired people and self-help groups.SEBI certified resource persons organize workshops for these target segments on variousaspects like savings, investments, financial planning,banking, insurance and retirement planning.

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