

Capital Market: Structure and Emerging Trends

Part-2

1.5 Securities and Exchange Board of India (SEBI)

Securities and Exchange Board of India (SEBI) was established in 1988. Primary role at that time was to observe the market but SEBI had no power to control anything. It was a non-statutory body. To give it powers, Union Government of India passed SEBI Act 1992. On 12 April 1992 SEBI became an autonomous body with statutory powers. Currently, there are 4 financial regulators in India, including SEBI.

Why was SEBI formed?

At the end of the 1970s and during 1980s, capital markets were emerging as the new sensation among the individuals of India. Many malpractices started taking place such as unofficial self-styled merchant bankers, unofficial private placements, rigging of prices, non-adherence of provisions of the Companies Act, violation of rules and regulations of stock exchanges, delay in delivery of shares, price rigging, etc.

Due to these malpractices, people started losing confidence in the stock market. The government felt a sudden need to set up an authority to regulate the working and reduce these malpractices. As a result, the Government came up with the establishment of SEBI.

Role of SEBI

SEBI acts as a watchdog for all the capital market participants and its main purpose is to provide such an environment for the financial market enthusiasts that facilitate efficient and smooth working of the securities market.

To make this happen, it ensures that the three main participants of the financial market are taken care of, i.e. issuers of securities, investor, and financial intermediaries.

Issuers of securities

These are entities in the corporate field that raise funds from various sources in the market. SEBI makes sure that they get a healthy and transparent environment for their needs.

Investor

Investors are the ones who keep the markets active. SEBI is responsible for maintaining an environment that is free from malpractices to restore the confidence of general public who invest their hard earned money in the markets.

Financial Intermediaries

These are the people who act as middlemen between the issuers and investors. They make the financial transactions smooth and safe.

Organizational Structure of SEBI

There are main 9 (nine) members on the SEBI Board:

1. One chairman appointed by Government of India.
2. Two members are officers from Union Finance Ministry.
3. One member from Reserve Bank of India (RBI).
4. Five members are appointed by Union Government of India. Out of these five, three are whole-time members.

Objectives of SEBI

1. To provide a transparent and healthy platform for corporate to raise funds from the financial market.
2. To create and enforce bye-laws for corporate and financial intermediaries.
3. To protect the rights of investors and ensure the safety of their investment.
4. To listen and provide system for investor grievances.
5. To promote and develop the financial markets.

SEBI Functions

SEBI's Preamble describes in detail the functions and powers of the board. Its Preamble states that SEBI must "protect the interests of investors in securities and to promote the development of, and to regulate the securities market and for matters connected there with or incidental there to."

Its functions can be divided in three parts:

1. Protective functions

SEBI performs the following functions to provide a safe and transparent environment for investors, who keep the financial market alive. These protective functions are –

- a. **Prevent price rigging:** One of the most important objectives behind the establishment of SEBI was to stop manipulated huge fluctuations in the financial market. Fluctuations are actually the basis to trade and earn money in the financial market for traders/investors. In-fact by studying historical fluctuations, several theories have emerged to predict the trend. These theories are collectively called as Technical Analysis (TA) and today very popular among traders. Usually, these fluctuations are natural but sometimes sudden fluctuations are fixed already by a group of the corporates leading to a huge loss for investors/traders. These fixed fluctuations are called price rigging/price fixing/collusion. SEBI keeps strict surveillance to prevent such price riggings. Introduction of circuits is one of them. A circuit is defined as a threshold with respect to previous day closing. If a security price goes beyond this defined circuit (threshold), a circuit breaker comes into action and trading on that security is halted for some time or the whole day.
- b. **Prohibit insider trading:** This can be seen as a part to prevent price rigging. A company's stock price fluctuation is highly affected by any public news/announcement about that company. Obviously, any forthcoming public news/announcement is already accessible by some persons in the company. What if they take advantage of this coming news/announcement by buy-sell company's security beforehand. This is called insider trading. To prevent insider trading, SEBI has barred trusts of listed companies and employee welfare schemes from purchasing their own shares from the secondary markets. SEBI also asks listed companies to disclose all their existing employee benefit schemes involving the stock purchase and align them in accordance with its ESOS and ESPS guidelines within a given timeframe.
- c. **Financial education for Investors:** SEBI conducts various online and offline seminars through various mediums to educate the traders and investors. This education starts from basics of financial market and covers money management as well.
- d. **SEBI Guidelines:** There are several other unfair practices which can be used by the corporate and others to manipulate security markets. SEBI makes sure that these are prevented beforehand by enforcing its bye-law guidelines.

2. Developmental functions

Developmental functions refer to the SEBI initiatives which bring fresh breathe and innovations in Indian financial market. Developmental functions include:

1. Introduction of electronic platform for financial market
2. DEMAT form of securities
3. Introduction of Discount brokerage
4. Training for financial intermediaries
5. Buy-sell mutual funds directly from AMC through a broker
6. Underwriting is optional to reduce the cost of issue.
7. IPO is permitted through exchange

3. Regulatory functions

Regulatory functions refer to enforcement of SEBI bye-laws to financial intermediaries and corporate. This ensures that stock market will run smoothly with transparency. This function includes –

1. SEBI has designed guidelines and code of conduct that are enforced to financial intermediaries and corporate.
2. SEBI registers all the intermediaries, share transfer agents, trustees and all those who are associated with the stock exchange in any manner.
3. SEBI registers and regulates the functioning of mutual funds.
4. SEBI regulates takeover of companies.
5. Conduct inquiries and audit of exchanges.