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FEAR ISN’T THE KEY: ON REGULATION OF SECURITIES MARKETS

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Capital Market & SEBI

India’s stock markets are booming, with the BSE Sensex touching new highs. The regulation of securities markets has evolved over the last two and a half decades since the setting up of the Securities and Exchange Board of India, but it is still a work in progress. Front-running, insider trading, shady accounting practices that are tantamount to window-dressing firms’ performance, and other shenanigans to manipulate share prices continue. A panel headed by T.K. Viswanathan, a former Lok Sabha Secretary General, has now submitted recommendations to curb illegal practices in the markets and ensure fair conduct among investors. A key recommendation is that the stock market watchdog be granted the power to act directly against “perpetrators of financial statements fraud”. In essence, this means SEBI can act not only against listed entities under its extant powers but also against those who aid or abet financial fraud — including accountants and auditors. The panel has suggested that SEBI, rather than the Central government, be given the power to grant immunity to whistle-blowers who help uncover illegal activities. It has mooted new ideas to address market manipulation, from better scrutiny of price-sensitive information to the creation of processes to expedite investigation into cases. It goes to the extent of recommending that SEBI be given powers to tap phone calls.

Greater executive powers, it is being suggested, can help the regulator take swifter action against offenders instead of relying on government bodies such as the Ministry of Corporate Affairs. Ostensibly, this could also free SEBI from various manifestations of political influence. Since SEBI is better placed to understand the complex nuances that financial market fraud entails, compared to other investigative agencies or even those in charge of implementing the Companies Act, it may also be better placed to enforce the law. A strong regulator serves as a good deterrent to truants in the market, but banking on fear too much could also scare away genuine investors. SEBI is widely considered to be one of the more efficient regulators, but it is not faultless. Last year, its order to impose restrictions on the trading of shares of 331 companies suspected of laundering money was seen as a hasty move taken under pressure from the government without a formal investigation. Given that SEBI is now considering a cap on trading by retail investors based on their assessed ‘net worth’, the committee’s suggestion that it may consider any trading by players beyond their known ‘financial resources’ as fraud could lead to undue harassment of investors. Granting more teeth to enable the market regulator to fulfil its primary role of protecting investors is fine. But it is equally critical to empower it with the right tools so that a sledgehammer is not deployed to crack a nut.

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