Accelerating towards Globalization: Indian Securities Regulation since 1992

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I. Introduction ............................................................................ 105
II. Background ............................................................................ 109
   A. History of Securities in India ........................................... 109
   B. Government Structure of India ....................................... 116
   C. Market Structure .............................................................. 118
III. The Primary Market .............................................................. 121
   A. Issuance of Capital .......................................................... 121
   B. Registration and Prospectus Requirements ..................... 122
   C. Foreign Issues by Domestic Corporations ....................... 125
   D. Exemption from the Capital Issue Act ............................ 128
IV. The Secondary Market .......................................................... 129
   A. Supervision by the Exchanges ....................................... 129
   B. The National Stock Exchange ....................................... 133
   C. Obligations of Broker/Dealers ..................................... 135
   D. Actions by Investors Against Brokers ............................ 141
   E. Foreign Investment .......................................................... 142
   F. Insider Trading ............................................................... 145
   G. Market Manipulation ....................................................... 147
V. Conclusion ............................................................................. 151

I. Introduction

As access to global securities markets has opened, U.S. investors have begun to look to the markets in developing countries in an effort to increase the return on their investments.¹

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¹ See Overview of U.S. Policy Toward South Asia: Hearings on U.S. Policy
India is one of these markets. Due to a combination of several economic conditions, as well as its recent opening to foreign investment, the Indian securities market is considered to have great value.\(^2\) Not only is India home to one of the largest consumer markets in the world, but it is also a country that, like most developing countries, is currently experiencing many significant changes to its infrastructure as well. These conditions work together to create extremely favorable conditions for investors, with opportunities for investments with stable high yield growth.\(^3\)

From its inception in 1947 up through the 1980s, the Republic of India had used an economic model of self reliance.\(^4\) India, like many other nations adopting this model, placed barriers on foreign trade, including a ban on foreign investment.\(^5\) The overriding policy objective for a government utilizing this type of system is to create economic self-reliance, whereby the economy is sustained by the nation's own resources rather than a combination of national products and imports.\(^6\) Starting in the 1990s, India began


\(^3\) The Solow Growth Model predicts that an economy will move towards a steady state unless technical change occurs. See ROBERT M. SOLOW, *GROWTH THEORY: AN EXPOSITION*, at xix-xx (1988). Technical change means a change in the overall system of a nation such as education or infrastructure. See id. Any of these temporary changes are not real long term growth and can cause the economy to become inflationary or deflationary, depending on the situation. See id.

\(^4\) See Darryl D'Monte, *Market Manipulation Comes to India; Exploiting the System*, *The New Leader*, Nov. 30, 1992, at 13 (describing the system of socialism in place in India at its inception). India's first Prime Minister, Jawaharlal Nehru, instituted a system whereby government controlled industry supplied private enterprise with essential raw materials. See id.


\(^6\) See generally RICHARD E. CAVES ET AL., *WORLD TRADE AND PAYMENTS: AN INTRODUCTION* 29 (5th ed. 1990) (explaining that countries seek to be self-sufficient to
changing from a policy of self-reliance to one of globalization. The globalization model recognizes that national economies are intertwined and that barriers to trade stifle national development. In the wake of this economic policy change, the Indian government has instituted new regulations to bring its securities regulation in line with the regulation of more developed nations.

The year 1992 marked a turning point for regulation of securities in India. Several legislative acts enacted prior to 1992 established a foundation for securities regulation. The Capital Issues (Control) Act regulated how a company may issue debt and equity. The Securities Regulation Act of 1956 provided the Central Government the authority to protect investor interest through a system of self-regulation where the exchanges and other self-regulation organizations (SRO's) would oversee securities transactions. However, without a central authority, the SRO's could not create a fair and efficient system of trade. Thus in 1992, the Securities and Exchange Board of India (SEBI) was given the legislative authority to act as the central regulator for the securities industry. The SEBI has been active in efforts to make the legal provisions covering securities transactions effective. For instance, the SEBI has promulgated regulations to cover basic market problems such as insider trading and the unprofessional behavior of broker/dealers.

Another major step taken to improve the financial markets was

\footnotesize{7 See Javalagi & Talluri, supra note 5, at 81-82 (explaining India's change in policy).
8 See generally CAVES ET AL., supra note 6, at 248-49 (discussing the costs incurred by developing countries who choose to restrict trade or protect local industries).
10 See id.
12 See id.
13 See THE GAZETTE OF INDIA Part II § 1 (1992), Securities and Exchange Board of India Act, 1992, Ministry of Law, Justice and Company Affairs, New Delhi, 4 Apr. 1992 [hereinafter SEBI Act].}
the creation of the National Stock Exchange (NSE) in Bombay.\textsuperscript{14} The NSE now serves as a model exchange in India, and through competition, has forced other exchanges to computerize and modernize.\textsuperscript{15} In addition, the high standard for self-discipline within the NSE has helped raise the standards of other exchanges.\textsuperscript{16} In short, the NSE is able to offer investors greater confidence in the market, which in turn allows the savings-investment rate to increase.\textsuperscript{17}

While many positive changes within the regional exchanges were prompted by the competition created by the NSE, the SEBI has also played a critical role. The SEBI closely monitors the regional exchanges, to ensure strict compliance with the adequate capital and margin requirements, before permitting the use of leveraged buying.\textsuperscript{18} For instance, the SEBI allowed the return of the carryforward system to the Bombay Stock Exchange.\textsuperscript{19}

This Article summarizes the basic law important to foreign institutional investors seeking to participate in the Indian market.\textsuperscript{20}

\begin{footnotesize}
\begin{itemize}
  \item[16] See id.
  \item[17] National savings is crucial to increased national growth without inflation. See \textit{SOLOW}, supra note 3, at 13-14 (explaining the effect of the national savings rate on the economy).
  \item[19] See id.
  \item[20] Although other administrative bodies have overlapping jurisdiction, this Article will primarily focus on the operations of the SEBI. For instance, the Company Law Board administers the Monopolies and Restrictive Trade Practices Act, the Chartered Accountants Act of 1949, and the Cost and Work Accountants Act of 1959, which all have an impact to some degree on the securities market. See Robert C. Rosen, \textit{The Myth of Self-Regulation or the Dangers of Securities Without Administration: The Indian Experience}, 2 \textit{J. COMP. CORP. L. & SEC. REG.} 270-71 (1979) (discussing Company Law Board and its enforcement power). Similarly, the MRTP Commission may issue “cease and desist orders” against companies engaging in unfair trade practices. See \textit{SECURITIES AND EXCHANGE BOARD OF INDIA, INVESTOR GRIEVANCES, RIGHTS, AND REMEDIES} 3 (1991) [hereinafter \textit{INVESTOR GRIEVANCES, RIGHTS, AND REMEDIES}]. Furthermore, the Reserve Bank, to encourage stability, may impose certain restrictions on how banks
\end{itemize}
\end{footnotesize}
This Article also discusses the many recent developments that have made the Indian market more efficient and transparent. Part II summarizes the history of securities in India and India’s government structure. An understanding of India’s government and securities history is necessary to comprehend the current market and the process of reform. Part III discusses how the primary market, which involves the creation of securities, is regulated. Part IV discusses the regulation of the secondary market, including the operation of the exchanges, oversight of broker/dealers, restrictions on foreign participation, and problems with market manipulation and insider trading. This Article concludes with a summary of the advances achieved in the Indian securities market over the past years, with a view toward other areas in need of attention before the Indian market becomes more attractive to foreign investment.

II. Background

A. History of Securities in India

The concept of corporations has some foundation in ancient India through the caste system. The kingdom was like a corporation, with the king acting as chief executive officer. The king had the duty to feed his people and to administer the laws justly. Although taxes paid for the king’s personal expenses, they were primarily intended for the benefit of the entire kingdom.

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21 See infra notes 25-145 and accompanying text.
22 See infra notes 146-220 and accompanying text.
23 See infra notes 221-447 and accompanying text.
24 See infra notes 448-67 and accompanying text.
26 See id. at 47-48
27 See id. In fact, many Indian historians believe that the Gupta Empire, the last empire encompassing all of modern day India, fell because its gold supply was depleted...
Even the concept of limited liability was present through the joint family system, whereby the head of the household was in charge of distributing assets amongst its members, and was the only member that could be held liable for the business of the family.28

Securities were introduced into India before 1800 for the purpose of raising capital for the East India Company.29 By the 1830s, securities had expanded to include shares and debt in the cotton presses in Calcutta,30 and the Company Act of 1850 formally recognized the concept of limited liability, a notion which has become the foundation of the modern corporation.31

Not long thereafter, the U.S. Civil War created the first speculative bubble, which served as the driving force behind formation of the Bombay Stock Exchange.32 Because the war cut off cotton supplies from the Confederacy, England had to rely on India for cotton, and the price of cotton rose ten-fold.33 Every Indian, even the most menial of servants, tried to buy shares.34 This “Share Mania” of 1860-65 ended on July 1, 1865, just after the end of the Civil War, and the price of cotton returned to normal levels.35

Although many companies had to be liquidated, this brief period marked the beginning of India’s securities market.36 By 1864, stock quotes for joint stock companies selling tea, jute (rope and linen), and coal were published in the papers.37 In 1875, a Brokers Association was formed in Bombay with 300 members.38

28 See Rosen, supra note 20, at 261, 263-64.
29 See id. at 264.
30 See id.
31 See id.
32 See id.
33 See id.
34 See id.
35 See id.
36 See id.
37 See id. at 264.
38 See id. at 263-64.
In 1877, the Stock and Share Brokers’ Association was formed in order to set standards for brokers in their dealings with the public and to make the occupation a reputable profession.39

After the formation of the Bombay Association in 1877, the textile industry of Ahmedabad, a city just north of Bombay, developed.40 A secondary market formed, and, in 1894, the Ahmedabad Share and Stock Brokers’ Association was created.41 Several years later, in 1920, Madras became the home of the first stock exchange in Southern India.42 Although this Madras exchange failed in three years, scrips in local textile mills continued to be traded.43 In 1933, telephone connections between Madras, Bombay, and Calcutta opened, thereby increasing interest in trading between Northern and Southern India.44 Ultimately, the Madras Stock Exchange formed in 1937 with five members and thirty-seven companies.45

The first World War brought wealth to the members of the Bombay and Calcutta Exchanges.46 The price of a seat on the exchange rose from Rs. 2,900 in 1914 to Rs. 48,000 in 1921.47 Despite this increase in activity, the exchanges had no formal rules governing trade.48 In fact, trading floors were open to the general public, where people conducted their own business.49 Beggars, hawkers, and pickpockets added to the confusion.50 In 1918 and 1919, many brokers manipulated the prices of

39 See id. at 264-65. This association was the precursor to the Bombay Stock Exchange. See id. at 264. The situation was similar in Calcutta. In 1908, the Calcutta Stock Exchange Association, composed of 150 members, was formed. See id.
40 See id. at 265. The capital for this development was supplied by “floating joint stock companies.” See id.
41 See id.
42 See id.
43 See id.
44 See id. at 264.
45 See id.
46 See id.
47 See id.
48 See id. at 265.
49 See id.
50 See id.
heavily traded shares in two companies, Standard Mill and Madhavji Mill. As a result, the market crashed, putting an end to forward trading or the ability to buy stock on margin rather than at the full price. Moreover, the exchange had to sell the seats of fourteen brokers who defaulted.

Public criticism caused the Bombay Legislature to form a committee under Sir Wilfred Atlay, head of the London Stock Exchange, to investigate the Bombay Exchange. Their report revealed that market manipulation lay at the center of the overspeculative nature of the Exchange. This revelation led to the passage of the Securities Contracts Control Act of 1925, which voided all trades failing to comply with rules to be promulgated by the Bombay Stock Exchange.

Unfortunately, this Act had no effect. While the Bombay Exchange produced a set of rules, as mandated by the Act, these rules were never effectively enforced. Furthermore, the Bombay Exchange continued to have its share of crises. In 1933, one of the largest managing companies in India failed, causing the bankruptcies of many smaller textile companies. Once again, forward trading was suspended—this time for seven weeks. Forward trading was again suspended in 1936 because the Bombay Exchange could not halt the manipulation "of several markets by professional jobbers [specialists]." Again, an inquiry committee

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51 See id.
52 See id. at 266.
53 See id.
54 See id.
55 See id.
57 See id.
58 See id.
59 See id.
60 See id. This "crisis period" lasted until 1937. See id.
61 See id. at 266.
62 Id.
was formed, and again, the exchange adopted a set of rules to deal with market manipulation. Like their predecessors, these rules were largely rendered ineffective when the government failed to pass legislation that called for appropriate supervision of the markets.

Although the Second World War brought an increase in the trade of securities, illegal activity by brokers also increased. Restrictions on forward and option trading forced brokers to leave the floors of the exchange and make side deals nearby. For example, in 1945, ninety percent of the transactions in Calcutta were on the "Katai" market instead of the Calcutta Exchange. Nonetheless, the war brought an increase in economic activity and unparalleled prosperity for the exchanges.

After Indian Independence, another committee was formed in 1951 to recommend a role for the new Central Government in supervising the market. This committee's report led to the Securities Contracts (Regulation) Act of 1956 [hereinafter Securities Regulation Act of 1956], which has become the central legislation for securities regulation. The Securities Regulation Act of 1956 was intended to govern the day-to-day trading in the exchanges. The Act also forbade stock options, futures contracts,

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63 See id.
64 See id.
65 See id. at 266.
66 See id.
67 See id.
68 See id. at 265. Greater prosperity resulted in the formation of exchanges in other major cities, such as Lahore (1934), Cawnpore (1940), Hyderabad (1943), Delhi (1947), and Bangalore (1957). See id. Today, India has 23 stock exchanges, not including the recently formed National Stock Exchange, see Sharma, Reliance Affair, supra note 14, at 1, and the Over-The-Counter Exchange of India. See Jenny Ireland, India: Trade Routes, THE BANKER, May 4, 1994, at 62 (describing the OTC Exchange of India). The OTC Exchange of India trades stocks of companies worth less than $1 million. See id. This limit may be raised to $9 million in the near future. See id.
69 See Rosen, supra note 20, at 266.
71 See 1 MAYYA, supra note 56, at 8.
72 See id. at 9.
and other derivatives, and assigned the task of overseeing India’s securities markets to the Ministry of Finance.

Passage of this legislation notwithstanding, stability for the Indian exchanges was to remain a distant dream. The new Indian Republic began to sink into isolation by slowly increasing its restrictions on foreign investors wishing to take part in the Indian markets. The driving force behind the barriers to foreign investors was the socialist ideal of self-reliance. This policy negatively effected the growth of the markets and created an effective barrier to changes in market regulations that would have improved market efficiency and transparency. In addition, although the Ministry of Finance was charged with the duty to regulate the markets, its efforts to do so were largely ineffective; the securities industry continued to be ignored by the government. For the most part, the self-regulatory organizations (SRO’s) were the only organizations enforcing regulations, and thus, individual investors were unprotected.

In recent years, Prime Minister P.V. Narsimharao and his Finance Minister, Mohaman Singh, have been instrumental in implementing many positive changes. In 1988, the Indian Government by resolution created the Securities and Exchange Board of India (SEBI). The SEBI was created to “promote the orderly and healthy growth of the securities market,” and to provide investor protection. The SEBI Act of 1992 made the

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74 See 1 Mayya, supra note 56, at 9.
75 See id.
76 See D’Monte, supra note 4, at 13 (describing the system of socialism in place in India at its inception).
78 See id. at 288-89.
80 See 1 Mayya, supra note 56, at 15.
82 Id.
SEBI a permanent body and gave it the authority to enforce the provisions of the Securities (Contract) Regulation Act of 1956 and the Capital Issues (Control) Act of 1947, and to enact regulations. Furthermore, the SEBI was recently granted the additional power to regulate corporate activities and to fine violators.

Efforts to effectuate change within the Indian markets did not end with the creation of the SEBI. For instance, in 1992 a large securities scam was orchestrated by both local and foreign banks. As a result, the Indian government set up a separate Special Court of Trial Offenses for Transactions in Securities to deal with this scam. In 1995, in the hopes of solving the liquidity crises in the market, legislation was introduced that would establish a depository system. This legislation was finally passed by the Rajya Sabha, the Indian legislature, in July 1996. Furthermore, the carryforward system (badla), which allows brokers to settle securities transactions later by keeping a deposit, was reintroduced to the Bombay Stock Exchange. And most recently, the SEBI has lifted the ban on options and futures trading in an attempt to

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83 See id. at 567.
84 See Richard L. Holman, World Wire, WALL ST. J., Jan. 30, 1995, at A14 (stating that India has increased the powers of the SEBI and lifted the ban on options trading).
85 See Banking Regulation Act of 1949, supra note 20, § 6(d). In 1992, local and foreign banks participated in a market scam that sent tremors through the Indian market. See Suman Dubey, Indian Panel Cites 4 Foreign Banks In Stock Scandal, WALL ST. J., Dec. 22, 1993 at A8 [hereinafter Dubey, Indian Panel Cites 4] (discussing a parliamentary report on the 1992 securities scam). The Bombay Stock Exchange Sensitivity Index (Sensex) rose dramatically, from a pre-scam low of less than 300 points in February 1992, to over 4500 points by mid-April. See id. After the fraud was revealed, Sensex crashed. See id.
86 See 28 THE INDIAN LAW INSTITUTE, supra note 81, at 563 (summarizing the setup for the Special Court of Trial for securities transactions).
88 See Sumit Sharma, India to Streamline Share Sales, Aiding Foreign Investors; WALL ST. J., July 25, 1996, at A8. In March 1997, the first depository corporation, National Securities Depository Ltd., which is designed to act as a clearinghouse for the National Stock Exchange, became operational. See id. at A8.
B. Government Structure of India

The government of India, one of the largest democracies in the world, can be described as quasi-federal. While it is more centralized than the government of the United States, it is less centralized than that of the United Kingdom. The power of the central government extends over the whole republic; whereas, the powers of the state governments are limited territorially. Concurrent powers are shared by the two systems, although the central government trumps the state, and any unenumerated powers reside with the central government. As for securities transactions, regulations passed by the Central Government supersede any state regulation; only stamp duties may be required by states on security scrips.

Similar to most democracies, the government is split into three branches: administrative, legislative, and judicial. The system has established checks and balances between the three branches. The Indian Parliament is a bicameral legislature consisting of the Council of States (Rajya Sabha) and the House of People (Lok Sabha). The Rajya Sabha is a permanent body, though one-third...

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90 See DERIVATIVES IN INDIA: A FRAMEWORK OF ECONOMIC PURPOSE, L.C. Gupta Committee Report (1997), available in Securities and Exchange Board of India (visited Oct. 9, 1997) <http://www.sebi.com/news/news.html>. Keep in mind, however, that the SEBI is not expected to allow exchanges to trade in options and futures unless sufficient standards are set. See id. The National Stock Exchange is ready to offer futures contracts but has not been given the authority to do so by the SEBI. See NSE News (visited Dec. 14, 1996) <http://www.nseindia.com/htdocs/news/sept.96/htm>. One of the reasons for the delay is that the Bombay Stock Exchange wants to prevent futures from being traded because they are an alternative to its badla system. See S. Vaidya Nathan, Will It Be Badla or Futures, BUS. LINE (THE HINDU), May 5, 1997, at 7 (comparing the badla system with futures contracts).

91 See 1 MAYYA, supra note 56, at 2.
92 See id.
93 See id.
94 See id. at 40.
95 See id. at 2.
96 See id.
97 See id. at 3.
of its members retire every second year. The vacancies are filled with candidates elected by state assemblies. All members of the *Lok Sabha* are elected directly by the people every five years. Bills that are passed by both houses become law upon approval by the President.

The President of India is the formal Head of State. He is elected for a five year term by both the Parliament and the State Assemblies. He appoints the Prime Minister, as well as the other ministers, with the consultation of the Prime Minister, the Attorney General, the Judges of the Supreme Court and the High Courts, the Comptroller General, and other administrative officials. The President also has legislative power to promulgate ordinances while the Parliament is not in session, although these presidential ordinances cease either six weeks after assembly of Parliament, or upon parliamentary disapproval.

The judicial system of India is based on the English Common Law, but closely follows U.S. law with regards to civil rights. Unlike most federal systems of government, India has only one judicial system. This system is centered around the Supreme Court of India. The Chief Justice is appointed by the President, who advises him on the appointment of other justices for the

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98 See id.
99 See id. The Council of Ministers, which advises the president, conducts the true administration of the Government. The Council is responsible to the *Lok Sabha* and holds power as long as it has confidence of the *Lok Sabha*. For a complete discussion, see id.
100 See id.
101 See id.
102 See id.
103 See id.
104 See id.
105 See id.
106 See id. The Securities and Exchange Board of India was initially formed in 1988 under such an ordinance. See 28 THE INDIAN LAW INSTITUTE, *supra* note 81, at 563 (summarizing the formation for the Special Court of Trial for securities transactions).
108 See id.
109 See id.
Supreme Court and the State High Courts. The Chief Justice of High Courts appoints the judges of the lower courts. The Supreme Court serves as the court of last appeal from the State High Courts. It has original jurisdiction over disputes between the Central Government and the States and disputes between States, and it can grant habeas corpus, mandamus, prohibition, quo warranto, and certiorari for enforcement of fundamental rights.

In addition to the standard courts, a special court can be set up to deal with specific offenses to prevent the court systems from becoming overburdened. For instance, in order to handle the securities scam of 1992, the President of India passed an ordinance authorizing a special court. The court was extended when Parliament met. For this particular scam, the ordinance authorized the Chief Justice of the High Courts to appoint a custodian of the court and further granted this special court original jurisdiction for prosecutions related to the events that took place in the market manipulation of 1992.

C. Market Structure

Many of India’s securities laws are copied from or based on securities laws of the United Kingdom. Merchant Banker underwriters, as well as other professionals, manage the issue of new capital for a company in an initial public offering. The participation of underwriters at this stage provides an added layer

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110 See id.
111 See id.
112 See id.
113 See id.
114 See id.
115 See 28 The Indian Law Institute, supra note 81, at 563 (summarizing the formation for the Special Court of Trial for securities transactions).
116 See id.
117 See id. at 563-64.
118 See Rosen, supra note 20, at 262 (stating the basis of the Indian laws).
of protection, as the underwriter is required to use due diligence to "independently verify the contents of the prospectus and the views expressed [therein]."\(^{120}\) Perhaps because of the added layer of protection, the SEBI is mandated to register all issues unless explicitly exempt.\(^{121}\) In the event of a misstatement in the prospectus, the Companies Act also gives certain rights of private action.\(^{122}\) The Act also prescribes reporting through an annual report.\(^{123}\)

Once issued and sold, stocks from the initial offering can be traded on the secondary market. The power to regulate the secondary market lies with the SEBI, a power given to it through the Securities Contracts Act of 1956.\(^{124}\) And to ensure that any attempt at regulation is meaningful, the SEBI has several options at its disposal. It may elect to delegate power to self-regulatory organizations (marketplaces for securities which set standards for trade), to control directly the self-regulatory organizations (hereinafter SRO's), or to promulgate regulations and rules.\(^{125}\) When the SEBI elects to establish rules or regulations, they become administrative law unless the Parliament of India overrules them.\(^{126}\)

The exchanges are the primary marketplace for secondary transactions, and they must follow certain provisions of the Securities Regulation Act of 1956 to operate legally.\(^{127}\) They are responsible for disciplining their members in day-to-day transactions and must inform SEBI of any violations that go

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\(^{120}\) Investor Grievances, Rights, and Remedies, supra note 20, at 8.

\(^{121}\) See Capital Issues Act, supra note 9, § 3.

\(^{122}\) See Investor Grievances, Rights, and Remedies, supra note 20, at 8-9.


\(^{124}\) See 28 The Indian Law Institute, supra note 81, at 561 (summarizing the Securities and Exchange Board Act of 1992).

\(^{125}\) See id. A rule is a general provision or guideline for how SEBI will administer the securities trade. See SEBI Act, supra note 13, § 29. A regulation is a more specific version of a rule, and often better defines the rule. See id. at § 30.

\(^{126}\) See id.

\(^{127}\) See Securities Regulation Act of 1956, supra note 11, § 4.
beyond what they are authorized to handle. In the event an exchange does in fact find it necessary to take disciplinary action against a member, they are required to disclose this information to the SEBI.

The regional exchanges operate on a specialist system. The professional jobber, also called a specialist, takes all orders for trade, whether they are orders to sell or to buy, and matches them against each other. The jobber does not trade for direct clients. Clients can enter their trades through a broker, or through a sub-broker who acts as an agent for the broker and will enter the order on the client's behalf.

In contrast, the Over-The-Counter Exchange of India operates on a marketmaker scheme. Unlike the specialist system, marketmakers hold stocks and may trade for clients. Marketmakers are broker/dealers who hold a large supply of an issue and, thus, set the price for issue. Unlike specialists, as long as they disclose their status to their client, marketmakers may act as principals or agents. The newly formed National Stock Exchange introduced a screen-based trading system whereby orders are entered through computers to the specialist's book rather than being taken on the floor. This type of system creates

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128 See id. § 9.
129 See id.
130 See Rosen, supra note 20, at 284 (describing the operation of the regional exchanges).
132 See id.
134 See Rosen, supra note 20, at 284.
135 See Ireland, supra note 68, at 62 (describing the OTC Exchange of India).
136 See HAZEN & RATNER, supra note 131, at 2-4 (discussing net capital rules).
137 See Ireland, supra note 68, at 62.
139 See id. (describing the National Stock Exchange).
a virtual trading floor across the nation, and is being adopted in some of the older exchanges.

Besides SEBI, two other administrative bodies, the Company Law Board and the Monopolies and Restrictive Trade Practices Commission (hereinafter MRTP Commission), have jurisdiction over the securities trade. The Company Law Board deals with shareholder’s rights, including takeover provisions, and standards for information disclosure by companies. The MRTP Commission may issue “cease and desist orders” against companies engaging in unfair trade practices. Furthermore, the Reserve Bank, to encourage stability, may impose certain restrictions on how banks trade in the market. All these bodies tend to coordinate their actions in these jurisdictional overlaps with SEBI.

III. The Primary Market

A. Issuance of Capital

The issuance of capital is defined by the Capital Issues (Control) Act of 1947 as the “issuing or creation of any securities whether cash or otherwise, and includes the capitalisation [sic] of profits or reserves for the purpose of converting partly paid-up shares into fully paid-up shares or increasing the par value of shares already issued.” The statute governs the issue of capital in three instances: 1) the issue of securities by companies, 2) the sale and purchase of securities, and 3) the advertisements.
making public or private offers for subscription or purchase of securities. The regulation of capital issuance holds for not only domestic companies but also foreign corporations issuing within India.

B. Registration and Prospectus Requirements

The Capital Issues Act of 1947 requires any issuance in India to receive the consent of SEBI. This consent will only be granted through registration of the issue, and SEBI may accept, refuse, or qualify registration of securities. If registration is refused, SEBI must provide a written explanation for such refusal upon request by the company. If registration is granted, SEBI may revoke registration if the issuer fails to meet the conditions established by SEBI when effectuating the registration, or if the company violates any provision of the Act or any SEBI regulation.

The Act also prevents advertising an offer unless the government has effectuated the registration. If SEBI has accepted the registration as a private placement, public offerings of that issue are prohibited. No sale or purchase of a security is valid until the registration has been effectuated. SEBI requires a prospectus to be included with the information for registration.

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149 See id. § 4.
150 See id. § 3.
151 See id.
152 See INVESTOR GRIEVANCES, RIGHTS, AND REMEDIES, supra note 20, at 8 (describing the process of evaluation of prospectuses by the SEBI).
153 See Capital Issues Act, supra note 9, § 3.
154 See id. § 3(5).
155 See id. § 3(6). Before such registration is revoked, however, the company has the right to make a showing as to why such an order should not be given. See id.
156 See id. § 4(1). This prohibition includes any offer to the existing shareholders.
157 See id. § 4(3).
158 See id. § 5.
159 See INVESTOR GRIEVANCES, RIGHTS, AND REMEDIES, supra note 20, at 8. This is similar to the common law rule that limited the creation of a subscription only through the issuance of a prospectus. See id. at 9.
and grades each prospectus based on the information contained therein. Among the areas scrutinized by SEBI is the issue price. Previously, SEBI would automatically price the issue at par on a combination of the earnings value, assets value, and the market value, if applicable. However, SEBI has begun to consider proposals to allow the issue to be priced at a premium because of the large difference between the issue price and the initial secondary market price.

The Companies Act of 1956 considers a document a prospectus if the document invites offers or deposits by the public for a capital issue. Directors, promoters, or persons authorizing the prospectus are liable under the Companies Act to investors for material misstatements in the prospectus. However, professionals who take part in the preparation of the prospectus cannot be held liable under this section, and damages are limited to the losses that the investor sustained. Affirmative defenses to claims under this act include withdrawal of consent prior to the distribution of the prospectus, issuance of the prospectus without the person’s knowledge, giving sufficient public notice that consent was withdrawn upon learning of the misstatement, reasonable belief that the statement was true, and reasonable belief that any expert preparation or statement by a public official was a fair representation.

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160 See id. Grade categories are A+, A, B, or C. See id.
161 See id. at 49 (discussing the setting of the issue price by SEBI).
162 See id.
163 See id.
164 See All in a Day’s Scam, The Banker, Sept. 1992, at 54 (stating the loosening of standards for issue price).
165 See INVESTOR GRIEVANCES, RIGHTS, AND REMEDIES, supra note 20, at 7 (quoting Companies Act of 1956, supra note 123, § 2(36)). The requirements of a prospectus are directed by Section 56 of the Companies Act to be set forth under Schedule II under that Act. See id. at 7-8.
166 See id. at 7. An investor can also file a common law claim for deceit in order to seek rescission, see 1 MAYYA, supra note 56, at 24 (discussing the private rights of action available to the investor), but such an action requires reliance by the investor and scienter by the violator. See id.
167 See INVESTOR GRIEVANCES, RIGHTS, AND REMEDIES, supra note 20, at 7.
168 See Companies Act of 1956, supra note 123, § 62(2).
The Companies Act also imposes criminal liability for a person involved in authorizing the issue, including imprisonment of up to two years and/or a fine of up to five thousand rupees (roughly U.S. $167), unless the person has an affirmative defense similar to the ones specified for a section 62 action.\textsuperscript{169} Furthermore, SEBI can proceed with an action for material misstatements or omissions against an underwriter who has not used due diligence in reviewing the prospectus.\textsuperscript{170} SEBI can also impose fines for material omissions or misstatements.\textsuperscript{171}

In addition to the prospectus, a firm often announces the issue subscription through a tombstone advertisement.\textsuperscript{172} The corporation can use a pro forma statement which contains the name and address of the corporation, existing and proposed activities, including the location of the industry, the members of the board of directors, the identity of the managing director or manager, the authorized capital, the subscribed capital, the proposed issue to the public, the dates of opening and closing of the subscription list, and a list of underwriters/bankers/brokers stating that applications for subscription can be obtained from them.\textsuperscript{173} A company using any other form of announcement is in danger that the form may be considered an offer or misleading advertisement.\textsuperscript{174}

A press release or statement in the news must conform with information within the prospectus, or it may be deemed a false inducement to invest,\textsuperscript{175} subjecting individuals to criminal sanctions.\textsuperscript{176} If a person knowingly or recklessly makes any statement, promise or forecast which is false, deceptive or misleading, or by any dishonest concealment of material facts, induces or attempts to

\textsuperscript{169} See INVESTOR GRIEVANCES, RIGHTS, AND REMEDIES, supra note 20, at 9 (describing the underwriter’s duty of due diligence).

\textsuperscript{170} See id.

\textsuperscript{171} See id.

\textsuperscript{172} See id.

\textsuperscript{173} See id.

\textsuperscript{174} See id. at 2 (discussing other statements besides pro forma).

\textsuperscript{175} See id. at 2-3.

\textsuperscript{176} See Companies Act of 1956, supra note 123, § 68.
induce another person to enter into, or to offer to enter into (a) any agreement for, or with a view to, acquiring, disposing of, subscribing for, or underwriting shares or debentures . . . shall be punishable with imprisonment for a term which may extend to five years, or with fine which may extend to ten thousand rupees, or with both.\textsuperscript{177}

The Monopolies & Restrictive Trade Practices (MRTP) Commission treats this activity as an unfair trade practice under Section 36A of the MRTP Act, and can issue a cease-and-desist order.\textsuperscript{178} Similarly, SEBI can take criminal action against the directors, officers, and intermediaries for such behavior.\textsuperscript{179} The underwriter has a duty to ensure that publicity/advertisements meet the SEBI guidelines, and can be sanctioned for not meeting this duty.\textsuperscript{180} Lastly, the stock exchanges can refuse to list the security for failure to meet government guidelines.\textsuperscript{181}

C. Foreign Issues by Domestic Corporations

In order for an Indian corporation to make a foreign issuance, the corporation must get permission from SEBI.\textsuperscript{182} The only type of foreign issuance that has been allowed are depository receipts (DR’s), which are vouchers denoted in the currency of the nation where they are sold.\textsuperscript{183} Depository receipts represent shares that are held by a trustee in India,\textsuperscript{184} and the Indian Government has allowed global DR’s (GDR’s) to be sold only to institutional

\textsuperscript{177} Id. Ten thousand rupees is approximately U.S. $280.
\textsuperscript{178} See INVESTOR GRIEVANCES, RIGHTS, AND REMEDIES, supra note 20, at 3 (discussing various remedies available to a investor under a misleading statement).
\textsuperscript{179} See id.
\textsuperscript{180} See id.
\textsuperscript{181} See id.
\textsuperscript{182} See Capital Issues Act, supra note 9, § 3(1); see also Robert E. Steiner, Report on Asia: A Tsunami of Money Crosses the Pacific, But Some Isn’t Welcome, WALL ST. J., Oct. 18, 1993, at A12.
\textsuperscript{183} See Steiner, A Tsunami of Money, supra note 182, at A12.
\textsuperscript{184} See Indrani Duttagupta & Timothy Mapes, Indian Firms Ready to Return to Global Equity Markets, ASIAN WALL ST. J., Feb. 21, 1996, at 20 (defining GDR’s); see also International Equity, New Members for the GDR Club, EUROMONEY, Nov. 15, 1996, at 90 (noting the practical advantages of using GDR’s in emerging markets).
investors. One rationale for GDR’s is that they allow foreign investors to avoid the settlement problems that occur when buying on the domestic markets. In addition, GDR’s avoid foreign exchange (forex) risk by being denoted in the currency of the market in which they are traded. In order to buy and sell stock in the Indian markets, an institution must receive permission by SEBI, thereby giving foreign investors greater exposure to European markets.

India’s sole investment treaty is with the United Kingdom. Although the treaty states that both nations are to provide the same rights in securities or investment cases to foreigners as they provide to their own nationals, the treaty does not prevent either nation from placing restrictions on the manner and magnitude of foreign investment. The treaty also allows the law of the place where the security transaction takes place to govern any legal problems resulting from the transaction. Analogously, when dealing with other nations besides the United Kingdom, India’s civil procedure will honor a judgment in a foreign country, provided that the judgment deals with securities within the jurisdiction of the other state.

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185 See Stockmarket: Foreign Money Dictates Prices, INDIA BUS. INTELLIGENCE, Mar. 6, 1996, at 6 (noting recent GDR issues); see also New Members for the GDR Club, supra note 184, at 87 (noting GDR trends).
186 See Foreign Money Dictates Prices, supra note 185, at 6 (noting recent GDR issues); Duttasgupta & Mapes, supra note 184, at 1 ("[GDR’s] are popular with foreign investors because they are a means of avoiding the settlement problems associated with trading in Indian and some other markets.")
187 See Duttasgupta & Mapes, supra note 184, at 1; New Members for the GDR Club, supra note 184, at A12.
188 See Steiner, A Tsunami of Money, supra note 182, at A12 (reviewing the various blocks to foreign investment by Asian nations).
189 See New Members for the GDR Club, supra note 184, at 87.
191 See id. art. 4, § 1.
192 See id. art. 4.
193 See id. art. 11, § 1.
194 See NAGENDRA SINGH, COMMERCIAL LAW OF INDIA 92-94 (1976) (stating that there is a presumption that foreign judgments are valid).
Depository receipts may have double regulation, not only by the country where the issue is being traded, but also by the country where the issue originated. In the case of U.S. DR’s (ADR’s), the SEC imposes various conditions. There are two types of ADR’s, sponsored and unsponsored. Unsponsored issues, in which the depository does not actively participate, must file a Form F-6 under the Securities Act of 1933. A foreign issuer could be held liable for misstatements or omissions in the registration statement. The U.S. depository would have no liability, because the Form F-6 is signed by a legal fictional entity as a joint venture between the two, and is therefore exempt under the 1933 Act. In the case of a sponsored issue, a depository may be liable for Section 11 violations. However, since the Indian government imposes a restriction to sell DR’s to only institutional investors, the registration may be exempt as a private placement under Rule 144A of the 1933 Act. An issue entitles the security holder to certain information on request, and also restricts the trade in the issue.

If the issue has a class of equity held by five hundred or more persons and: 1) is traded on a U.S. stock exchange, 2) is quoted by NASDAQ, or 3) the issuer’s assets exceed $1,000,000, then the issuer may be subject to reporting conditions through Form 20-F of the Securities Exchange Act of 1934 (1934 Act). The 1934

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196 See id. at 61.
197 See id. at 60.
198 See id.
199 See id. at 63 (stating that since both the issuer and the depository must sign the registration statement as required by Form F-6, an issuer may be held liable under section 11 of the Securities Act of 1933 for misrepresentation in or omissions from the registration statement).
200 See id.
201 See id. at 63-64.
202 See id. at 64.
203 See id. at 65 (stating that a security holder and potential purchaser have the right to know the basic business and financial data of the issuer).
204 See id.
Act also allows certain exceptions to this reporting requirement.\footnote{See id. Saunders notes that “foreign issuers meeting a 500 shareholder threshold are not required to register the security unless at least 300 of the shareholders are United States residents.” \textit{Id}.} Also, if at the end of the previous fiscal year, the issuer had less than U.S. $5 million in assets and was not quoted on NASDAQ, the issuer is exempt from these registration requirements.\footnote{See id.} Furthermore, the minimum information supplying exemption described in the 1934 Act provides that if the security issuer is willing to supply certain information upon request, the issuer will be exempt from this reporting requirement.\footnote{See id.}

Because of the lack of a depository system in India’s domestic market, Indian securities play a large role in the GDR market.\footnote{See id.} Although Indian GDR’s may be canceled back or converted to domestic issues, they cannot be reissued.\footnote{See id.} Arbitrageurs, who try to make profits based on the price differences in the same security in different markets, often find this inability to trade back and forth between foreign and domestic markets frustrating.\footnote{See New Members for the GDR Club, supra note 184, at 87 (discussing the position of Indian securities in the GDR market).} Indian corporations have issued GDR’s instead of ADR’s primarily because the cost of issuance is cheaper due to the less stringent reporting standards.\footnote{See id. at 88.} Additionally, GDR’s offer greater trading coverage, since they cover the European market and can be sold in the United States as a private placement.\footnote{See id. at 87.} Otherwise, the difference between a GDR issuance and an ADR is considered merely semantic.\footnote{See id.; see also Duttagupta & Mapes, supra note 184, at 20 (discussing the overall advantages of GDR’s in relation to DR’s).}

\textbf{D. Exemption from the Capital Issue Act}

If specified by the Indian Government, an issue of securities

\footnote{See New Members for the GDR Club, supra note 184, at 88.}
may be exempt from the Capital Issue Act for: 1) control of issues, 2) advertisement of offers, or 3) purchase pursuant to Section 6(1). These exemptions are stated in the Capital Exemption Order of 1961. In addition, exemptions are granted to private companies not registered under the MRTP Act, government companies not making a public offering, and banking or insurance companies.

Issues of Rs. 100 lakhs or less may also be exempt if certain conditions under Section 5 of the Exemption Order are met. Most of these conditions are based on the capital structure of the firm, the structure of the issue, and the possibility of listing on an exchange. In the case of a merger or acquisition of nonbanking corporations, capital that is issued is exempt if the issue is approved under Section 396 of the Companies Act. In addition, if approved by the Reserve Bank of India, also known as the Indian Central Bank, a capital issue in a banking amalgamation is exempt.

IV. The Secondary Market

A. Supervision by the Exchanges

Prior to the formation of the Securities and Exchange Board of India, most regulation of the secondary and primary markets was

214 See Capital Issues Act, supra note 9, § 6(1).
215 See 1 MAYYA, supra note 56, at 19-21 (stating the exemptions in the Capital Exemption Order).
216 See id. Issuances by other companies are exempt in certain circumstances. Some examples of circumstances that would warrant an exemption are issuances within twelve months prior and not exceeding Rs. 10 million, issuances involving a stock split or consolidation of shares provided the total value does not change, debentures taken up or loans granted or bonds or promissory notes issued by certain government financial agencies, securities other than debentures made in the ordinary course of business to a banking institution, or debentures in the ordinary course of business to a banking institution or its nominee if the issue and any issues within the previous twelve months does not exceed a certain amount. See id. at 19-20.
217 See id. at 20.
218 See id. at 19-21.
219 See id.
220 See id.
controlled by the self-regulatory organizations. However, due to rampant market manipulations and the need for market efficiency, SEBI was created to act as the government watchdog. Pursuant to the Securities Act of 1956, the SEBI was given complete control over the exchanges. Moreover, under the SEBI Act of 1992, SEBI can be substituted as the regulating governmental authority under previous acts dealing with securities, if the central government feels this substitution is necessary and desirable.

The Securities Act of 1956 also outlines the general conditions that must be met in order to become a member of an exchange. There are only two ways in which to become a member of an exchange: purchase a seat, or have a seat transferred to you upon the death of a member. Any individual seeking membership on an exchange must be at least twenty-one years of age, must have matriculated, and must have completed a two-year apprenticeship with a member of an exchange or banking institution. In addition, they must be solely in the business of securities.

While membership in many exchanges is limited to individuals and partnerships, the National Stock Exchange (NSE) offers memberships to banking institutions and corporations. The NSE also offers separate membership for its debt market and equity market. In order to screen members, the NSE requires applicants

221 See id. (summarizing the existing system of regulation).
222 See 28 THE INDIAN LAW INSTITUTE, supra note 81, at 560 (explaining the creation of the Securities and Exchange Board).
223 See id.
224 See id. at 561.
225 See 1 MAYYA, supra note 56, at 16-18 (overviewing the requirements set in the Securities Contracts (Regulation) Act of 1956). Most exchanges operate through a specialist system, in which a specialist takes orders on the floor and trades for his own account. See Ireland, supra note 68, at 63.
226 See 1 MAYYA, supra note 56, at 16-18. However, unlike most exchanges, the National Stock Exchange does not allow a member to transfer his seat to another individual at any time. See NSE Members (visited Jan. 1996) <http://www.nseindia.com>.
227 See 1 MAYYA, supra note 56, at 16.
228 See id.
229 See Ireland, supra note 68, at 63.
230 See Bist, supra note 15, at 8. However, to operate on the debt market, a member
to take a written exam and undergo an interview. Although the Governing Board of an exchange is in charge of day-to-day supervision of the exchange, this Board supervision is subject to SEBI intervention, if the SEBI finds direct regulation is necessary. This type of intervention has occurred on several occasions. For example, the SEBI attempts to regulate norms for brokers, such as the level of capital adequacy for brokers, and margin requirements through the exchanges.

Without a depository system, a broker must deliver actual certificates to purchasers. This has caused numerous problems. To illustrate, in 1995, Reliance Industries, the highest volume stock in India, had a dispute with the Bombay Stock Exchange (BSE) over issuing duplicate shares. Reliance had issued 26,650 duplicate shares to an investor who claimed to have lost her shares. However, she had already sold the original shares, which were by that time sitting in the Investment Division of the


[233] Capital adequacy is the amount of liquid assets that a broker has separate from his customer trades. See HAZEN & RATNER, supra note 131, at 966. These standards are often set to ensure that a broker can meet his obligations and does not default. See id.; see also Timothy Mapes & Jyoti Pande, Indian Regulatory Board to Allow Resumption of Forward Trading, ASIAN WALL ST. J., Oct. 6, 1995, at 19 (discussing how the initial rates will be set at 3% for individuals and 6% for corporations).

[234] See Bist, supra note 15, at 8 (stating how the Bombay Stock Exchange had failed to make its members follow the capital adequacy norms). Margin requirements are limits on the amount a customer can borrow from a broker to buy stock. See HAZEN & RATNER, supra note 131, at 969-70 (discussing margin requirements). In order to protect against broker default, the exchanges require that, in the event that the customer supersedes the margin requirement amount, a broker either suspend trade for the client or give the customer a margin call asking to meet the margin. See id.

[235] See A Green(ish) Light, ECONOMIST, Dec. 2, 1995, at 83 (explaining the problems with the Indian market). However, the OTC Exchange of India does have a depository. See Ireland, supra note 68, at 63.


[237] See id.
Reliance Conglomerate. Of course, she also sold the duplicates issued to her.\(^{238}\)

Reliance notified the Bombay Exchange of the fraud and the issuance of duplicate shares, which prompted the Bombay Exchange to suspend trading in Reliance for three days.\(^{239}\) Although Reliance threatened to delist their stock from the Exchange and stated that the action was unjustified, the stock continues to trade on the BSE.\(^{240}\) Reliance ultimately took a significant loss as a result of this fraud.\(^{241}\)

A broker who delays in the delivery of shares beyond standards set by the exchange may be held liable for the lost profits of the purchaser.\(^{242}\) The NSE requires a broker to deliver shares within a week, or he may be liable for the highest market price during the entire accounting period.\(^{243}\) This requirement is more stringent than in other exchanges; accordingly, settlement times for stock deliveries in the Indian market generally have been bad.\(^{244}\)

In 1996, the SEBI allowed the Bombay Stock Exchange to reintroduce the carryforward system which had been suspended in 1994.\(^{245}\) A carryforward system allows a trader to buy a security on margin and then settle the account at increasing margins for up to ninety days.\(^{246}\) Thus, a broker can leverage his trading.\(^{247}\) The system was suspended because of the speculative effect it had on the market.\(^{248}\) It was later reintroduced to increase trading volume

\(^{238}\) See id.

\(^{239}\) See id.

\(^{240}\) See id.

\(^{241}\) See id. Another problem that was pointed out by this fracas is the fact that Reliance uses a system of switching, where it will temporarily give shares from its other accounts to meet the delivery requirements of the exchange. See id.

\(^{242}\) See Bist, supra note 15, at 10 (describing the penalties for bad delivery).

\(^{243}\) See id.

\(^{244}\) See id.

\(^{245}\) See Indian Industry Welcomes Return of Forward Trading in Bombay, supra note 18.

\(^{246}\) See id.

\(^{247}\) See id.

\(^{248}\) See id.
during the bear market in 1995. However, the SEBI now requires that exchanges allow forward trading to strictly enforce the capital adequacy norms for brokers, and use only screen-based trading.

B. The National Stock Exchange

One of the main objectives for creating the National Stock Exchange was to have an exchange that was a truly national market, unlike other main markets which were restricted to regional trade. In addition, SEBI encouraged the creation of a new exchange because of problems with the Bombay Stock Exchange (BSE), and because there was a need for a market for debt securities.

The NSE became the second computer-based trading system in India, and has linked regional centers around the nation through the use of very small aperture terminal (VSAT) satellite dishes. The trades go through the regional center to brokers in Bombay.

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249 See id.
250 See id.
252 See Bist, supra note 15, at 8 (discussing the National Stock Exchange). The Bombay Stock Exchange was not strictly enforcing SEBI regulations with its members. For instance, the Bombay Exchange was neither ensuring its members were registered with the SEBI nor enforcing the capital adequacy standards; furthermore, the Bombay Exchange had lengthy settlement times for some stock deliveries. See id.
253 See Bonds: Active Secondary Market Is Badly Needed, INDIA BUS. INTELLIGENCE, Nov. 18, 1994, at 8 (explaining the debt trading before the National Stock Exchange). The lack of a debt securities market caused debt to be highly illiquid and not priced at any standard rate. See id. The NSE first began as a debt market in government bonds and commercial paper, but now trades in equities as well. See NSE Overview (visited Aug. 27, 1997) <http://www.nseindia.com/ht/docs/overview.htm>.
254 OCTEI is also a computerized exchange, but is limited to companies whose assets are less than one million dollars. See Ireland, supra note 68, at 62 (listing computerized exchanges).
255 See Bist, supra note 15, at 8 (discussing the National Stock Exchange).
256 See id. In order to compete with the screen-based system of the NSE, the Bombay Stock Exchange has changed to a computer system of trade as well. See id. As a result of computerization, the BSE market is much more transparent, thus reducing spreads. See id. Spreads occur because the market is composed of immediacy providers and the general public. See KALMAN J. COHEN ET AL., THE MICROSTRUCTURE OF
The system shows whether an order has been entered, and, if so, the price, the time of execution, and the broker's commission. Orders are matched together based on a price and time priority.258 The system enables brokers to trade without disclosing their identity.259

The NSE's strict delivery standards have also caused the BSE to enforce the standards on more frequently traded stocks.260 However, the NSE does not intend to establish a carryforward system.261 The NSE allows members to be either a member of the debt market, the equity market, or both.262 However, the NSE does require different capital requirements for the type of trading sought.263

The National Exchange has implemented a point system for penalties against brokers who default in delivery or settlement.264 For accumulations of between fifty-one to one hundred points, a fine is imposed at various points.265 An accumulation of one hundred points causes the broker to be suspended for five days.266 The Exchange imposes a forty-eight hour rectifying period for a bad delivery.267 Any uncorrected deliveries are auctioned, and the

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SECURITIES MARKETS 93-111 (1986). The immediacy providers are the marketmakers, specialists, and others who can act faster than the market can react. See id. These providers can set their prices at an artificial level because they can act and learn about information before the market. See id. Relevant information is one of the factors to reducing spreads. See id.

257 See Bist, supra note 15, at 8.
259 See id.
260 See Bist, supra note 15, at 8.
261 See id. at 8. See supra note 246 and accompanying text for a definition of the carryforward system.
263 See id.
264 See Bist, supra note 15, at 8 (describing the point system for the NSE members).
265 See id.
266 See id.
267 See id.
broker is not allowed to take part in it. The broker must then redeliver the security from the market.

The National Securities Depository, Ltd. is the first depository for an Indian exchange, and is also a clearinghouse for trades conducted on the National Stock Exchange. Stock certificates are surrendered to the depository registrar. Dematerialization occurs when the registrar destroys the physical certificate and creates an electronic record for the security. This record is treated like an account, stating which depository participant holds the name of the stockholder. Depositories are more efficient, and prevent forgeries.

Since many companies list on multiple exchanges, including the NSE, the high standards of the NSE are filtered down throughout the system. When the NSE formed, its success was uncertain. However, in 1996, the NSE hit record trading volumes that surpassed the highs of the Bombay Stock Exchange. Both exchanges are currently vying with one another for the coveted position as the dominant market of India.

C. Obligations of Broker/Dealers

The Stock Broker [sic] and Sub-Broker Rules of the SEBI Act require that any stockbroker or sub-broker be certified by the

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268 See id.
269 See id.
271 See id.
272 See id.
273 See id.
274 See New Share Depository in India May Not Work for at Least 6 Months, ASIAN WALL ST. J., July 18, 1996, at 12 (discussing the first Indian depository).
275 See Sharma, Reliance Affair, supra note 14, at 1 (showing the influence of the NSE on other exchanges).
276 See id. (discussing the creation of the NSE).
278 See Sharma, Reliance Affair, supra note 14, at 1 (showing the influence of the NSE on other exchanges).
A stockbroker is a member of an exchange; a sub-broker is not a member of an exchange but acts as an agent of the broker, or assists investors in dealing in securities through the broker. A sub-broker can effectuate a securities contract as long as he has been authorized by the broker, and the broker is given a record of such transactions.

A stockbroker applies to the exchange of which he seeks to become a member. Certification is given to a broker if he is a member of an exchange, agrees to follow the rules of that exchange, pays the certification fees, agrees to take adequate steps to address investor grievances, and agrees to keep the Board informed of investor grievances. The Board will consider the broker’s eligibility to be a member of the exchange, the broker’s material resources to handle his duties (e.g., office space or manpower), the broker’s past experience in securities trading, and any disciplinary sanctions against the broker or members of his office. If a broker is refused certification, he has a right to respond to the Board, and ask for reconsideration within thirty days.

A sub-broker, though not a member of an exchange, must comply with similar conditions as a broker and must be given permission by the broker to deal in securities. A sub-broker applies through the exchange of which his broker is a member and must also send a letter of recommendation from the broker with

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279 See SEBI Act, supra note 13, § 12.
280 See Stock Broker Rules, supra note 133, at Rule 2(e).
281 See id.
282 See THE GAZETTE OF INDIA Part II (1992), Securities and Exchange Board of India (Stock Brokers [sic] and Sub-Brokers) Regulations, 1992, under § 30 of the Securities and Exchange Board of India Act, 1992, Securities and Exchange Board of India, New Delhi, 23 Oct. 1992, at Reg. 15(b), sched. II(c) [hereinafter Stock Broker Regulations].
283 See id. at Reg. 3(1).
284 See id. at Reg. 4.
285 See id. at Reg. 5.
286 See id. at Reg. 8(3).
287 See id. at Reg. 11(5).
his application. A sub-broker must be at least twenty-one years of age, have no past convictions of fraud or dishonesty, and must have completed the twelfth standard of schooling. A corporation or partnership can also be a sub-broker if the individual directors or partners of the entity meet these requirements. Like a broker, a sub-broker has a right to respond if his application is refused.

A broker is required to keep accounts, records, and documents for at least five years. Documents that should be kept are registers of transactions, client ledgers, general ledgers, journals, cash books, bank pass books or records of banking transactions, particulars of securities transfer and delivery, contracts with other members of the exchange, notes regarding client contracts, written consents of clients where the broker is a principal, margin deposits, accounts of sub-brokers, and the scope of authority of sub-brokers. The broker is also obligated to send an end of accounting period balance sheet and income statement to SEBI.

If a broker is acting as a principal by transferring securities from his own account rather than from the market, the broker must disclose this to his customers. Furthermore, the Securities Regulation Act also requires that the broker must receive written consent from the customer within three days of the date of the contract. The broker cannot require this consent in order to enter into a contract for a security.

A broker is also required to adhere to a “broker’s code of

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288 See id. at Reg. 11(2).
289 See id. at Reg. 11(5). Completion of the 12th standard is equivalent to a United States high school education. However, the board may relax the educational requirement based on the applicant’s experience. See id. at Reg. 11(5)(c).
290 See id. at Reg. 11(5)(c)(ii).
291 See id. at Reg. 13(3).
292 See id. at Reg. 18.
293 See id. at Reg. 17(1).
294 See id. at Reg. 17(3).
295 See id. at Reg. 7, sched. II(B)(6). Schedule II is the “Code of Conduct for Stock Brokers [sic].” See id.
296 See Securities Regulation Act of 1956, supra note 11, § 15.
297 See id.
conduct.” This code of conduct describes how a broker must conduct his business and the fiduciary duties owed to his clients. The code of conduct encompasses three areas: general, customer, and market (interaction with other dealers) duties. Generally, a broker must have high standards of integrity and must use due diligence. A broker may not manipulate markets or create false markets. Lastly, a broker must comply with all statutory requirements from government and market authorities.

A broker also owes his clients certain fiduciary duties, violation of which may subject the broker to liability to his clients. The broker/dealer must execute orders as he is directed and may not refuse a client simply because the volume of trade is low. The broker must inform the customer of the status of the order and must be prompt in delivery and collection of payment. A broker is required to issue a contract note without delay and has a duty of confidentiality as to client information. Practices of selling stocks in a client account simply to generate commissions are prevented. Similarly, false and misleading quotations or information about a security are not permitted. Brokers also have a duty of fairness to their clients, which includes a prohibition against furnishing “false or misleading advice or information.” When giving investment advice, a broker must know the security that he is recommending and must ensure that

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298 See Stock Broker Regulations, supra note 282, at Reg. 7, sched. II.
299 See id.
300 See id. at Reg. 7, sched. II.
301 See id. at Reg. 7, sched. II(A)(1).
302 See id. at Reg. 7, sched. II(A)(4).
303 See id. at Reg. 7, sched. II(A)(5).
304 See id. at Reg. 7, sched. II(B).
305 See id. at Reg. 7, sched. II(B)(1).
306 See id.
307 See id. at Reg. 7, sched. II(B). However, the board can relax these standards on the merits of the individual.
308 See id. at Reg. 7, sched. II(B)(4)(a). Such practices are commonly known as churning. See HAZEN & RATNER, supra note 136, at 897-98.
310 Id.
the security is suitable to the interests and the assets of the client.\footnote{See id. at Reg. 7, sched. II(B)(7).} The suitability requirement is established when the broker acts with scienter and there is an expectation of reliance.\footnote{See id.} Lastly, a broker should be competent and has a duty of supervision over his employees and office.\footnote{See id. at Reg. 7, sched. II(B)(8).}

When dealing with other brokers, a broker must deliver the terms of a contract.\footnote{See id. at Reg. 7, sched. II(C)(1).} A broker is prohibited from knowingly making an improper delivery and must replace any improper delivery upon learning about it.\footnote{See id. at Reg. 7, sched. II(C)(1).} A duty of cooperation is imposed to protect the interest of other brokers’ clients.\footnote{See id. at Reg. 7, sched. II(C)(2).} The exchanges also determine what is legal advertising and publicity.\footnote{See id. at Reg. 7, sched. II(C)(3).} A broker may not use unfair trade practices to acquire clients.\footnote{See id. at Reg. 7, sched. II(B)(5).} Finally, a broker may not skim from the returns of a security.\footnote{See id. at Reg. 7, sched. II(C)(6).} The duties of a sub-broker are comparable to the duties of a broker, but some duties of agency are added.\footnote{See id. at Reg. 15.}

The Board can appoint an investigative authority or auditor if it believes that a broker is improperly keeping records, if it believes that the Securities Regulation Act is being violated, or if a complaint is made by an investor, broker, or other person.\footnote{See id. at Reg. 19(1)(2).} The Board must give notice to the broker,\footnote{See id. at Reg. 20(1).} unless public interest dictates otherwise.\footnote{See id. at Reg. 20(2).} The broker and his employees must fully cooperate with the authority during the investigation.\footnote{See id. at Reg. 21(4).}
of the authority must be filed promptly,\textsuperscript{325} and the broker has a right to respond before any action is taken against him.\textsuperscript{326}

SEBI can suspend or cancel a broker’s certification under certain conditions.\textsuperscript{327} A suspension can be given for the following: violation of the Securities Regulation Act, violation of the code of conduct, failure to furnish the Board with information about transactions, giving wrong or false information in a broker’s reports to the Board, noncooperation in investigations, failure to resolve customer complaints, market manipulation such as price rigging or cornering, unprofessional or unbusinesslike conduct, financial inadequacy, failure to pay fees, violation of registration conditions, and suspension from an exchange.\textsuperscript{328} If these activities are repeated or constitute a pattern, cancellation may be appropriate.\textsuperscript{329} Certification can also be canceled if a broker violates the insider trading or take-over regulations, is found guilty of fraud, convicted of a criminal offense, or has his registration from an exchange canceled.\textsuperscript{330}

Before SEBI cancels or suspends a broker, the broker must be given notice.\textsuperscript{331} If the broker replies within thirty days\textsuperscript{332} with evidence required to make a defense or if it is required by the Board, SEBI must give the broker an inquiry hearing.\textsuperscript{333} The broker or his representative may be present before the inquiry officer.\textsuperscript{334} The broker is not allowed to have a lawyer present his case, unless SEBI has appointed a prosecuting attorney.\textsuperscript{335} The inquiry officer will then give a written report concerning his

\begin{enumerate}
\item \textit{See id. at Reg. 22.}
\item \textit{See id. at Reg. 23(1).}
\item \textit{See id. at Reg. 25(1).}
\item \textit{See id. at Reg. 26(1).}
\item \textit{See id.}
\item \textit{See id. at Reg. 26(2).}
\item \textit{See id. at Reg. 28(2).}
\item \textit{See id. at Reg. 28(3).}
\item \textit{See id. at Reg. 28(4).}
\item \textit{See id. at Reg. 28(5).}
\item \textit{See id.}
\end{enumerate}
recommendation of penalty. SEBI can change the penalty with cause but must send a report of the cause to the broker. The broker then has a right to reply within twenty-one days, and within thirty days of a reply, SEBI may issue an order. The order must be published in at least two daily newspapers, and can be appealed to the Central Government.

D. Actions by Investors Against Brokers

Usually investor grievances against a broker are taken up by the Investor Grievance Cell of an exchange. An Investor Grievance Cell is an arbitration board that handles complaints against member-brokers or listed companies. For example, the Bombay Stock Exchange has set up the following procedure for arbitration. Both the investor and the broker may nominate any member of the Stock Exchange as an arbitrator, or an investor may ask the Exchange to name an arbitrator. The arbitrators must render their decision within four months from being nominated or an agreed upon extension period. The ruling is binding on all parties and their representatives. The Stock Exchange may take further action by penalizing, suspending, or warning the broker. Furthermore, the investor can file a civil suit instead of the arbitration if there is no arbitration clause in the contract between the investor and the broker. Contracts by sub-brokers should be

336 See id. at Reg. 28(7).
337 See id. at Reg. 29(10).
338 See id. at Reg. 29(2).
339 See id. at Reg. 31.
340 See id. at Reg. 32.
341 See INVESTOR GRIEVANCES, RIGHTS, AND REMEDIES, supra note 20, at 35-36 (explaining Investor Grievance Cells).
342 See id. at 35.
343 See id. at 36 (describing the Bombay Stock Exchange's method of arbitration). The Exchange charges a fee for such recommendations. See id.
344 See id.
345 See id.
346 See id.
347 See id. (stating alternatives to arbitration).
valid through an agency relationship.348

Other actions against broker default include those taken by the Exchange’s Defaulter Committee.349 First the broker’s exchange registration is canceled, and his name is posted as a defaulter on the exchange.350 Second, the committee seizes the security deposits, margin moneys, and securities within his possession.351 The committee will then attempt to collect any assets owed to the defaulter.352 The Committee will then pay off any claims by the Stock Exchange and the Clearing House, followed by exchange members whose claims have been admitted that have outstanding liabilities.353 Lastly, the clients will receive any remaining funds.354 Some exchanges have an Investor Protection Fund that will pay the investor based on his claim up to Rs. 15,000.355 This differs from the United States, where investor insurance is sufficiently funded to provide adequate insurance against broker default.356

E. Foreign Investment

Foreign investment is one of the major areas of economic regulation within a mixed economy. When the Republic of India was formed, it used the socialist economic model that was prevalent in Western Europe. In such a system, private corporations coexist with government corporations who control essential resources such as agriculture, minerals, and utilities.357 The Indian economic model also tried to create national self-sufficiency by preventing foreigners from gaining control of any

348 See id.
349 See id. at 39.
350 See id.
351 See id. (laying out the process for broker default recovery).
352 See id.
353 See id.
354 See id.
355 See id. at 40 (discussing the paltry amount that is insured).
356 See HAZEN & RATNER, supra note 131, at 968.
357 See D’Monte, supra note 4, at 13 (describing the system of socialism in place in India at its inception).
economic sectors.\textsuperscript{358}

India has recently begun the process of moving away from being a closed economic system and moving towards an economic model that is open to world markets.\textsuperscript{359} In 1992, the government opened up the securities market to foreign institutional investors (FII’s).\textsuperscript{360} Before an institution may invest in India, it must receive the consent of the Indian Government.\textsuperscript{361} The process involves filing an application that includes five years of financial records of the corporation, as well as its investment objectives.\textsuperscript{362}

Foreign institutional investors are limited in the scope and manner of investment in the market.\textsuperscript{363} They can invest only thirty percent of their overall securities portfolio in debt securities.\textsuperscript{364} Initially, this thirty percent limit was set for each account the institutional investor held, which caused an inability to set up funds specializing in debt securities.\textsuperscript{365} Only twenty-four percent of issued capital can be held by foreign institutions.\textsuperscript{366} By 1996, twenty-two major companies had hit this ceiling.\textsuperscript{367} This restriction imposes a burden on foreign investment, since only ten percent of listed securities are actively traded by foreign institutions.\textsuperscript{368}

Since foreign investment was permitted in 1992, the market has been directed by these foreign institutions.\textsuperscript{369} One of the

\begin{footnotes}
\textsuperscript{358}See 1 Mayya, supra note 56, at 37.
\textsuperscript{359}See All in a Day’s Scam, supra note 164, at 52.
\textsuperscript{360}See Robert Steiner, India Investors Overcome Bombs and Riots, But Not Bureaucracy, WALL ST. J., May 28, 1993, at C1 (discussing the process of entering the Indian market). However, because India’s purpose for allowing foreign investment is to provide capital for long-term growth, foreign individuals are, for the most part, barred from trade. See id.
\textsuperscript{361}See id.
\textsuperscript{362}See id.
\textsuperscript{363}See Bonds, supra note 253, at 8 (explaining the restrictions on debt trading).
\textsuperscript{364}See id. at 8.
\textsuperscript{365}See id. at 8.
\textsuperscript{366}See id. at 8.
\textsuperscript{367}See Nadkami, supra note 277, at 7.
\textsuperscript{368}See id.
\textsuperscript{369}See Stockmarket: Foreign Money Dictates Prices, supra note 185, at 6.
\end{footnotes}
market indicators has been whether these investors hold on to GDR's, or switch towards domestic issues. One example of the influence of foreign investors occurred in March 1996, when foreign institutional investors stopped trading due to the announcement of the arrests of ten politicians, and the Bombay Stock Exchange Sensitivity Index (Sensex) dropped over one hundred points.

Besides securities trading, SEBI has eased restrictions on ownership of direct investment. Foreign corporations are allowed to increase their ownership to seventy-four percent in already existing subsidiaries. New subsidiaries can be set up as wholly owned by the foreign company.

In terms of tax issues, the tax laws of India can be somewhat complex and confusing. Some of the problems stem from the fact that India did not have an advance ruling system until recently. Further, there is a flat tax rate of twenty percent of all interest and dividend income. The long-term capital gains rate is ten percent. Finally, India has set up tax treaties with many nations, so that a company can credit a portion of taxes paid in India towards taxes in the home country when repatriating funds.

There are two ways that an individual can invest in the Indian stock market. First, the Indian government allows nonresident Indians or citizens of Indian origin to invest. If the investment is

(footnotes)

370 See Khanna, supra note 2, at 15 (quoting Morgan Stanley on switch buying).
371 See Stockmarket: Foreign Money Dictates Prices, supra note 185, at 6 (explaining the influence of FII's).
372 See id.
373 See id.
374 See id.
375 See generally 28 THE INDIAN LAW INSTITUTE, supra note 81, at 363 (summarizing the tax laws of India).
376 See id.
377 See id.
378 See id.
379 See id. at 364.
380 See 1 MAYYA, supra note 56, at 38 (stating the exceptions for non-resident Indians).
in debt securities, there are no restrictions. However, nonresidents may have certain restrictions in equity ownership depending upon whether they will repatriate their funds or not.

The other way to invest in India is to invest in an emerging markets mutual fund that invests in India. These funds generally are closed-ended funds, which means that they invest funds in India raised through equity offerings in the United States, and issue profits through dividends.

F. Insider Trading

Insider trading occurs when a corporate insider trades on information before it is disclosed to the general public. It is generally thought that such trading gives a premium to the insider that comes from the losses of the general public. But because the generic investor tends to be bullish, and the premium causes the information to come to the market sooner, some argue that nothing is wrong with the insider receiving a premium. However, financial markets for the most part depend on the investment of the general public, who expect that it will be done on a level playing field with others in the market. Without this faith in the market, many investors would not invest.

The SEBI Act (Insider Trading) Regulations prohibit "insiders" from dealing in exchange-listed securities on his or another's behalf based on unpublished price sensitive information, communication of such information unless in the ordinary course of business, or counseling others based on that information.

381 See id.
382 See id.
383 See THE INDIA GROWTH FUND INC., 1995 ANNUAL REPORT 1.
385 See id.
386 See id.
387 See id.
388 See Rosen, supra note 20, at 286.
“Dealing in securities” means trading or agreeing to trade either as a principal or agent. Liability is not imposed on tippees, persons who have been given information by the insider.

An “insider” is a person connected to a corporation, and is reasonably expected to have access to, has received, or has previously had access to unpublished price sensitive information. A “connected person” can include directors, officers, employees, or “professionals” who may be reasonably expected to have access to such information. The “professionals” included under this definition include stock exchange members, self-regulatory organization (SRO) members, and bankers. The “information” is any unpublished information that relates to the company that if published would materially affect the market.

SEBI may delegate an investigative authority if it receives a complaint of insider trading by investors, intermediaries, or others. SEBI may also investigate an insider based on supposition arising out of its own knowledge or information. The insider must be given notice of the investigation, unless public interest dictates that no notice should be given. The insider is then required to give reasonable access to relevant records with him or others, such as his stockbroker. The authority can interview partners, employees, or members of the insider, and these persons are required to give full assistance to the

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390 See id. § 2(d).
391 See id. § 2(c).
392 See id. § 2(e).
393 See id. § 2(c)(i).
394 See id. § 2(c)(ii).
395 See id. § 2(h)(ii).
396 See id. § 2(h)(v).
397 See id. § 2(h)(iii).
398 See id. § 2(k).
399 See id. § 5(2)(a).
400 See id. § 5(1).
401 See id. § 6(1).
402 See id. § 6(2).
403 See id. § 7(1).
Unlike broker violations, the authority is required to give a report to SEBI within a month. The report can also be generated through a qualified auditor, provided that the auditor has the same access to information as would the authority.

Before taking any action, SEBI must give the insider a statement of its findings and an opportunity to respond. The Board can then proceed with criminal prosecution after receipt of the response. Other actions the Board can take include injunctions against dealing with securities, prohibition of disposal of securities, and the restraint of communication or counsel to deal in securities. An insider may appeal to the Central Government if the Board sanctions him.

G. Market Manipulation

There is no explicit definition of market manipulation in the Securities Act of 1956. SEBI monitors such activities through the broker regulations and standards set by the exchanges. The biggest securities scam in Indian history occurred in 1992, just before SEBI was granted permanent status. A presidential ordinance governed SEBI, making it simply a policy making body, so the Ministry of Finance was in charge of oversight of the

404 See id. § 7(3).
405 See id. § 8.
406 See id. § 10.
407 See id. § 9(1).
408 See id. § 11.
409 See id. § 11(a).
410 See id. § 11(b).
411 See id. § 11(c).
412 See id. § 12.
413 See 1 MAYYA, supra note 56, at 24 (discussing the lack of explicit definition of market manipulation).
414 See Stock Broker Regulations, supra note 282, at Reg. 7 (requiring a stockbroker certified under Regulation 7 to follow the code of conduct established in schedule II).
The securities scam involved forty-four individuals, including Harshad Mehta, who filed the largest income tax return in India, and some of the main banks in India, including foreign banks such as PLC Standard Chartered, ANZ Grindlays, Bank of America, and Citibank. This manipulation caused the Sensex to rise from under 3,000 points in February to over 4,500 points in mid-April, and subsequently crash after the scam was revealed. The manipulation is said to have involved over U.S. $1.4 billion in securities, and caused the Bombay Stock Exchange to be closed for nearly five weeks. The government of India has set up the Special Court of Trial to hear and decide the violations that occurred during this scam.

The root of the scandal was violations of the Reserve Bank guidelines, which had a twenty-five percent reserves requirement at the time. A reserves requirement is the amount of funds that a bank must keep with the central bank of a nation to prevent the bank from overextending itself in giving loans. In addition to the reserves, the Reserve Bank also requires that the banks meet a Standard Liquidity Ratio (SLR) of 38.5%, which must be held in

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416 See Dubey, Indian Panel Cites 4, supra note 85, at A8 (summarizing the findings of a parliamentary committee's report).
418 See Dubey, A Financial Scandal, supra note 415, at A13 (describing the results of an investigation into the 1992 scandal).
419 See Dubey, Indian Panel Cites 4, supra note 85, at A8.
420 See id.
421 See id.
422 See Dubey, Scandal Delays Issues, supra note 417 (explaining the scandal's effects on the Indian stock market).
423 See 28 THE INDIAN LAW INSTITUTE, supra note 81, at 563 (summarizing the establishment of the Special Court of Trial for securities transactions).
425 See Bonds, supra note 253, at 8 (explaining the banking guidelines of the Reserve Bank of India).
426 See id.
government bonds or other liquid, low-yield securities. The banks violated this provision of the guidelines by trading with these SLR funds.

Standard Chartered created false or dummy records of securities to contravene these banking guidelines and used funds for securities speculation. These funds were lent, in some cases, for "mere promises to deliver securities" or bank receipts issued for nonexistent securities. Through its corporate cash deployment service scheme, the bank would lend funds to traders using false receipts. The bank would then get a gentleman's promise to be paid back at interest rates above the specified Reserve Bank guidelines. When the bank sustained losses on its trades, Hiten P. Dalal, one of the brokers implicated in the scandal, would bail the bank out. This gave Mr. Dalal "virtual control of the bank's treasury department and enabled him to gain access to billions of rupees of the bank's funds." Standard Chartered officials involved in this scam stated that they acted without the approval or knowledge of senior management.

Grindlays Bank created a "special relationship" with Harshad Mehta, one of the brokers charged with complicity, which "enabled him to route his securities transactions through Grindlays and enjoy unauthorized overdraft facilities." The funds diverted into Mr. Mehta's account included checks from the National Housing Bank, a Reserve Bank subsidiary created for housing development. Citibank and Bank of America were similarly

427 See id.
428 See id.
429 See Dubey, Missing Funds at $1.23 Billion, supra note 424, at B6 (describing the practices of the foreign banks in the scandal).
430 Id.
431 See id.
432 See id.
433 See id.
434 Id.
435 See id.
436 Id.
437 See id.
charged with making unauthorized bank funds available for trade
into the market.\textsuperscript{438}

In 1993, a joint parliamentary report was published about the
scandal recommending actions to be taken against the four
banks.\textsuperscript{439} Parliament found that the banks were “deeply involved
in the irregularities in securities transaction,” and that all failed to
follow procedure of internal control.\textsuperscript{440} The report stipulated that
the banks were likely guaranteed a certain return for usage of the
funds, created by diverting funds from other customer accounts
held by Mehta, Dalal, and other brokers.\textsuperscript{441} Parliament further
suggested fining the banks and preventing them from repatriating
funds gained from the scam.\textsuperscript{442} The parliamentary report found that
transactions similar to those conducted by Mr. Mehta and other
brokers had occurred since 1986.\textsuperscript{443}

Grindlays Bank is currently in arbitration with the Housing
Bank regarding its role in the scandal,\textsuperscript{444} while Citibank stated in
its 1993 annual report that it expects to be fined by the Indian
government when the litigation ends.\textsuperscript{445} Citibank also paid a U.S.$64 million pretax charge in 1993 for closing down its portfolio
management division for Indian investors.\textsuperscript{446} Furthermore, in
1994, John Dingell, Chairman of the U.S. House Energy and
Commerce Committee, asked the SEC and the Federal Reserve to
investigate whether Citicorp had violated any United States

\textsuperscript{438} See id.

\textsuperscript{439} See Dubey, Indian Panel Cites 4, supra note 85, at A8 (describing a

\textsuperscript{440} Id.

\textsuperscript{441} See id.

\textsuperscript{442} See Suman Dubey, India Panel Calls for Penalties in Stock Scandal:
Investigators' Draft Report Urges Special Scrutiny, Audits of Foreign Banks, WALL ST.
J., Apr. 16, 1993, at A9 (stating the recommendations of the parliamentary report on the
1992 scandal).

\textsuperscript{443} See id.

\textsuperscript{444} See id.

\textsuperscript{445} See Citicorp Expects Fine by Indian Regulators Over Scandal in 1992, WALL
ST. J., Feb. 3, 1994, at B12 (discussing the penalties Citicorp faces for its role in the
1992 Indian stock market scandal).

\textsuperscript{446} See id.
V. Conclusion

Current conditions within the Indian government and securities market have allowed many investment firms to conclude that India is a high value market. Recent changes within the exchanges themselves, the development of the Indian infrastructure, and a large middle class are all factors that make Indian securities attractive. The Indian government has opened the market up to foreign institutional investors, which has predictably led to more institutions applying to trade on the Indian market. Furthermore, the regional exchanges in India have begun to make serious attempts to increase their efficiency by seeking advice from developed nations. Also, since portions of existing Indian regulations parallel regulations in developed nations, the market tends to be attractive to foreign investors.

At the same time, the Indian market is leading the way by adding features that are innovative even in foreign markets, such as inflation-indexed government bonds and screen-based trading. India also is poised to be the first country to regulate credit rating agencies directly. Greater change is expected as the

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448 See Khanna, supra note 2, at 15 (citing Morgan Stanley's view of the Indian market).

449 See Steiner, Bombs and Riots, supra note 360, at C1.

450 The OTCEI, for example, has consulted with members of NASDAQ. See Sharma, Reliance Affair, supra note 14, at 5 (stating that OTCEI has been getting training and technical assistance from NASDAQ officials).

451 See India May Issue Inflation Bonds, ASIAN WALL ST. J., Aug. 15, 1996, at 12 (announcing that the Indian government is seriously considering the issuance of inflation bonds to insulate fixed-income groups from inflation).

452 See Ireland, supra note 68, at 62.

453 See SEBI Drafts Eligibility, Disclosure Norms for Credit Rating Agencies, BUS. STANDARD, June 10, 1997, at 7 (announcing that SEBI will regulate credit rating agencies). The credit rating agencies rate "debt instruments issued by promoters to raise money." Id. SEBI has drafted guidelines for the process of this rating. See id.
result of a parliamentary panel’s review of and recommendations for the Indian regulations. These recommendations include expanding the definition of a security and merging the Securities Contract and Regulations Act with the SEBI Act. This high valuation and continuing change in regulation makes it likely that India will be a major global market in the future.

That being said, while many changes have occurred in recent years, the Indian market has yet to mature. Although the SEBI has the power to enforce the Indian laws concerning securities, their power is substantially undermined by the large number of appeals available to parties who are dissatisfied with an SEBI order, particularly in the primary market. In fact, the SEBI itself has admitted its inability to prevent a particular merchant banker from underwriting even though they failed to meet their underwriting commitments.

Another hurdle yet to be crossed is poor market liquidity. In 1995, the annual trading volume was only eight percent of the market capitalization. Recognizing that poor market liquidity is partly the result of a much-needed depository system, the Indian Government promulgated a Depositories Ordinance in 1995. While actual implementation of this Ordinance was delayed in

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454 See Dhanuka Panel for Widening the Definition of Securities, BUS. STANDARD, July 21, 1997, at 9 (explaining some of the recommendations of the parliamentary panel reviewing the current acts).

455 See id.

456 See Stockmarket: The Monetary Brakes Are Still On, supra note 87, at 8 (citing the problems still faced by SEBI). For example, in 1996, the SEBI suspended SBI Capital Markets, the largest merchant banker in India, for failing to prevent the issuance of misleading advertisements for MS Shoe. See id. SBI Capital “promised to appeal right up to the Supreme Court if necessary.” Id. This type of suit in the United States would be frivolous, because the enforcement power of the S.E.C. is well-established. See id.

457 See id.

458 See id.

459 See id. This is quite a poor showing when compared to the liquidity of other Asian markets. Taiwan has a volume of up to 194%, and South Korea has a volume at 59%. See id.

460 See A Green(ish) Light, supra note 235, at 83 (discussing the lack of a depository system).
Parliament until the following year, the National Securities Depository, Ltd. registered as the first depository in India in 1996. Establishment of this depository is hopefully a move in the right direction.

1992 marked a dramatic change in how India views foreign investment, and it may well be the wise investor who does not overlook the potential of the Indian market. Although the ability of foreign institutions to trade remains highly restricted, foreign institutional investors may now trade in the secondary market, and foreign direct investment is permitted by foreign investors interested in long term investment. Even though Indian regulators set limits on the extent of foreign trading that occurs, and the Indian Government has prohibited domestic corporations from creating foreign issues, India is slowly opening the door to foreign investment, and laying the foundation to become a major global market in the years to come.

[463] See Steiner, Tsunami of Money, supra note 182, at A12 (reviewing the various blocks to foreign investment by Asian nations).
[464] See Steiner, Bombs and Riots, supra note 360, at C1 (discussing the process of entering the Indian market).
[466] See id.
[467] See Capital Issues Act, supra note 9, § 3(1).