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REGULATORY ARBITRAGE IN INDIAN SECURITIES MARKETS: SYSTEMIC ANALYSIS OF DETECTION AND ENFORCEMENT GAPS THROUGH MULTI-ENTITY FRAUD CASES

AUTHORED BY - KENAN GEO JOLLY

Abstract

India's securities markets have evolved technologically and institutionally since the enactment of the Securities and Exchange Board of India Act, yet sophisticated multi-entity frauds continue to exploit structural gaps within the regulatory architecture. This dissertation conceptualizes these recurring failures not as isolated governance breakdowns, but as instances of regulatory arbitrage, the deliberate structuring of transactions, ownership networks, and trading strategies to remain formally compliant while functionally evading regulatory intent. Through a comparative analysis of five landmark cases: Ketan Parekh (circular trading), IL&FS (subsidiary opacity), Yes Bank–Rana Kapoor (disclosure evasion), Adani Group (offshore beneficial ownership structuring), and Jane Street (algorithmic index manipulation), the study identifies recurring detection and enforcement gaps within SEBI's surveillance systems, beneficial ownership disclosure framework, inter-agency coordination mechanisms, and appellate deterrence structure.

Using doctrinal analysis and a FILAC-based case methodology, benchmarked against regulatory models of the U.S. Securities and Exchange Commission and the European Securities and Markets Authority, the research demonstrates that India's entity-based and disclosure-centric framework is misaligned with the velocity, complexity, and cross-border layering of contemporary financial misconduct. The study introduces the concept of the "Detection Immunity Window" to explain prolonged enforcement lag and proposes targeted architectural reforms: modernization of surveillance infrastructure through real-time audit trails, integrated ultimate beneficial ownership mapping across agencies, reduction of disclosure thresholds, enhanced algorithmic oversight, strengthened inter-regulatory intelligence-sharing frameworks, and recalibration of appellate review standards to restore deterrence.

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By reframing regulatory arbitrage as a systemic vulnerability rather than episodic misconduct, this dissertation contributes to securities law scholarship and offers an implementable roadmap for strengthening institutional capacity, enhancing market integrity, and aligning India's capital market regulation with global best practices.

Introduction

The Indian stock market is one of the growing financial systems in the world. It has changed a lot since the government opened it up in the 1990s. The Securities and Exchange Board of India or SEBI was set up to make sure the market is fair and transparent. SEBI was created by the SEBI Act of 1992. Over the years SEBI has put in place rules and systems to watch the market and prevent fraud.However with these rules and systems there have been many big financial scandals in India. These include the Ketan Parekh stock market scam, the Satyam fraud, the IL&FS collapse, the Yes Bank debacle and the Adani-Hindenburg controversy. These scandals show that there are still gaps in the system that allow fraud to happen.

The main problem is that people are finding ways to exploit the system. They are using loopholes in the rules and differences between regulatory bodies to avoid getting caught. In India this is a problem because there are many different regulatory bodies that do not always work well together. This creates opportunities for fraudsters to hide their activities. The way fraudsters operate is also very clever. They use schemes that involve many different people and companies.

They use algorithms and other techniques to manipulate the market and avoid detection. With the use of advanced technology, such as the Integrated Market Surveillance Systems and Data Warehousing and Business Intelligence Systems SEBI often finds out about fraud after it has happened.This research project looks at how fraudsters are able to exploit the system in India. It examines big cases of fraud and how they were able to happen. The project uses different methods to analyze the problem including looking at the law comparing India to other countries and studying specific cases.

The goal of the project is to identify the weaknesses in the system and suggest ways to improve it. It looks at how SEBIs surveillance systems are working and how well different regulatory bodies are working together. It also compares India's system to those in countries, such as the United States and Europe.The main idea of the project is that the problems in the stock market

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are not just because of a few bad people but because of the way the system is designed. To fix the problems we need to make changes to the system not just small tweaks. We need to use technology make the rules clearer and change the way regulatory bodies work together.

Ultimately the project hopes to contribute to the discussion about how to regulate markets. It wants to help people understand how the system can be improved to prevent fraud and make the market safer for everyone. By looking at the cases of fraud, in India it shows that we need to make sure the rules and regulations are strong enough to catch fraudsters and prevent them from exploiting the system. The Indian stock market, the Securities and Exchange Board of India and the Indian government all have a role to play in making the market safer and more transparent.

Background of the Study

Over the thirty years India's securities market has changed a lot. It used to be a market where brokers had a lot of power and everything was done on the floor. Now it is one of the electronic capital markets in the world with advanced technology and investors from all over the globe. The Securities and Exchange Board of India or SEBI was set up to oversee the market and protect investors.

SEBI was created to make sure the market is fair and safe for investors. Many changes were made to the market like electronic settlement systems and dematerialization to make it more transparent and safe. These changes were made after some scandals, like the Harshad Mehta securities scam showed that the market was not safe.With all these changes the market is still not perfect. The regulators are still trying to keep up with the market. India is now a part of the global financial market and this has made things more complicated. There are many foreign investors and companies are using structures to avoid rules. This has made it harder for regulators to do their job.One big problem is something called arbitrage. This is when people find ways to exploit the rules and avoid getting caught. They do this by using structures and taking advantage of gaps in the rules. This is different from fraud, which is when someone breaks the law on purpose. Regulatory arbitrage is like finding a loophole in the law.

There have been big scandals in India's securities market. The Ketan Parekh scam, the IL&FS crisis and the Yes Bank-Rana Kapoor matter are a few examples. These scandals show that the regulators are still not doing enough to stop people from exploiting the rules.With new laws

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and technology the same problems keep happening. This suggests that the problem is not just with the regulators but with the way the market is set up. The scholars who study India's securities market usually look at each scandal as an event.. This does not explain why the same problems keep happening.The problem is that the regulators are not keeping up with the market. The market is getting more complex. The regulators are not able to keep track of everything. There are a reasons for this. One reason is that the regulators rely much on disclosure thresholds. This means that they only look at companies that meet criteria and they do not look at the bigger picture.

Another reason is that the regulators focus on companies rather than looking at the whole network of companies. This makes it hard for them to see what is really going on. There are also gaps between regulatory agencies, which makes it hard for them to work together.The regulators are also not able to keep up with the technology. The market is using algorithms to trade and the regulators are not able to keep track of everything. This creates a "detection immunity window" which's a period of time when people can exploit the rules without getting caught.

Other countries are doing a job of regulating their markets. The US Securities and Exchange Commission has set up a system to track all trades in time and the European Securities and Markets Authority has set up rules to make sure that all trades are reported.India's capital market is very important to the country's economy. It helps to bring in investment and promote financial inclusion.. If the regulators are not able to do their job it could undermine investor confidence and make the market unstable.

This study is looking at the intersection of securities law, design and financial regulation theory. It is trying to understand why the same problems keep happening in India's securities market and how to fix them. The study is looking at the scandals that have happened in the market and how the regulators have responded.

The goal of the study is to identify the weaknesses in the framework and propose some solutions. It is hoping to contribute to the discussion, about how to regulate emerging markets and build strong institutions.

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Statement of the Problem

India's securities markets have changed a lot since the Securities and Exchange Board of India Act was made and the Securities and Exchange Board of India (SEBI) was set up. Overtime SEBI has been given power to enforce rules, including the power to stop fraudulent and unfair trade practices, insider trading and to make sure companies list and disclose information correctly. SEBI can also impose fines. Ban people from the market.

Even with these changes big problems in the market keep happening. At first these problems were simple, like price rigging or insider trading. Now they are more complicated. Involve many companies, funds from other countries and complex computer systems.

These strategies follow the rules. They do not do what the rules are meant to do. This is called arbitrage, which means finding ways to get around the rules.

Most of the time people talk about cases of bad corporate governance, insider trading or companies not disclosing information. Studies have shown that many cases are not solved or they take a time to solve or the penalties are reduced. Some people have said that the rules about insider trading are not clear and they do not cover everyone they should. They also said that there are not ways for people to fix problems and the penalties are not strong enough. Even though some of these problems have been fixed the fact that there are still problems shows that there are deeper issues.

So the main question this study is trying to answer is not just why securities violations happen. Why they keep happening even after the rules are changed. Specifically:
Why do the same kinds of problems keep happening after the rules are changed?
Why do regulators usually act after a big problem has happened, of before?
Why is it hard to detect and punish companies that have structures?
Does Indias regulatory system encourage companies to follow the rules in a way that's not really meaningful?
The fact that there are delays and companies manipulate information and different agencies do not work well together and penalties are reduced on appeal shows that there are big gaps, in the system. These gaps create a "detection immunity window". A time when companies can get away with things because regulators are not watching enough.
So the main question this study is trying to answer is:

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Does the Indian securities regulatory system have weaknesses that allow companies to get around the rules, which hurts the integrity of the market and protects investors?

The study wants to look at the picture and see if the rules are aligned with the way the market is changing.

Scope of the Study

This study looks at what happens when people try to find loopholes in the rules of the securities market. The Indian securities market is controlled by the Securities and Exchange Board of India which is also called SEBI. We want to see if there are any gaps in the system that people can exploit.

At the heart of this study we are trying to understand the laws and rules that govern the securities market. We are looking at the laws like the Securities and Exchange Board of India Act and other rules, such as the ones that prevent fraudulent trade practices and insider trading. We also want to know if these laws are strong enough to stop people from doing things in the market.

To do this we are looking at some cases where people have tried to exploit the system.

These cases involve things like trading, insider trading and manipulating the rules to hide who really owns a company. We are not just looking at these cases as one-off incidents. As examples of how the system can be exploited.

We also want to see how well SEBI is doing its job. We are looking at how SEBI watches the market how it investigates problems. How it punishes people who break the rules. We want to know if SEBI is reacting to problems after they happen or if it is trying to prevent them from happening in the place.

We are also comparing the system to other countries, like the United States and Europe. We want to see what they are doing differently. If there are any lessons we can learn from them.

This study starts from when SEBI was set up in 1992 and goes up to the day. We want to see how the rules and laws have changed over time and if people are still finding ways to exploit the system.

Overall we think that people trying to find loopholes in the rules is a problem that needs to be addressed. We want to understand how the system works and how we can make it stronger. We are looking at things, like how the lawsre written how well SEBI is watching the market and how different parts of the system work together.

We are looking at the laws and rules that govern the securities market

We are examining cases where people have tried to exploit the system

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We are evaluating how well SEBI is doing its job

We are comparing the system to other countries

We want to understand how the system works and how we can make it stronger The Indian securities market and SEBI are the focus of this study. The Indian securities market is a system and SEBI has a big role to play in regulating it. We want to see how the Indian securities market and SEBI can work together to prevent people from exploiting the system. The Indian securities market and SEBI are important because they help to protect investors and maintain the integrity of the market.

Limitations of the Study

While this study tries to give an analysis it has some limitations that come with studying rules and using non-numerical data.

First the research mainly uses information that's available to the public. This includes SEBI orders, court judgments, laws, academic studies and published data on enforcement. It does not have access to algorithms, investigative methods or private communications. So the analysis of how well enforcement works based on what can be observed rather than internal data.

Second the case studies looked at in this research are high-profile cases that had a big impact on the market. These cases are useful for finding weaknesses in the system. They might not represent smaller or unreported cases of regulatory issues. This means the findings might only show patterns in enforcement cases rather than all types of market problems.

Third this study does not use numbers and statistics to analyze trends. It does not try to measure how well regulations deter people from breaking the rules. Does it calculate how much money investors lose in each case. The approach is based on understanding rules and interpreting data. This gives insight but limits the ability to make general statements that can be proven with statistics.

Fourth while the study does compare some things it does not compare systems across many countries. Differences in institutions, economies and laws between India and other countries might limit how applicable certain regulatory tools are. So comparisons are used carefully and mainly for ideas.

Fifth the study only looks at rules for the securities market. Does not examine related areas like banking, insurance, taxes or anti-money laundering except where they directly relate to securities. This means it does not cover all vulnerabilities in the system beyond just the capital markets.

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Sixth the changing world of financial technology is a limitation. New developments in AI trading, decentralized finance and blockchain securities might create kinds of regulatory issues that are not covered in this study. So the conclusions are based on the market and enforcement mechanisms.

Finally the research does not say that regulatory issues are only due to failures or institutional weaknesses. It recognizes that market innovations often happen faster than regulations can keep up with globally. The limitation is in assessing how well regulatory design keeps up with market changes not in evaluating the intent, behind regulations.

Literature Review

Citation: Sanjith S, Foreign Portfolio Investment and Its Impact of Regulatory Arbitrage in Indian Capital Markets, 7 Indian J.L. & Legal Res. 5236 (2025).

This research paper provides a comprehensive analysis of the systemic vulnerabilities within the Indian capital markets that facilitate regulatory arbitrage, specifically focusing on the exploitation of Foreign Portfolio Investment (FPI) frameworks. The author explores how the SEBI (Foreign Portfolio Investors) Regulations, 2019, while designed to categorize and monitor capital inflows, inadvertently created "enforcement gaps" through tiered investor classifications. By examining the structural differences between Category I and Category II FPIs, the study illustrates how unregulated funds and corporate bodies can leverage jurisdictions with limited disclosure norms to mask their Ultimate Beneficial Ownership (UBO). A significant portion of the analysis is dedicated to the role of Offshore Derivative Instruments (ODIs), which act as conduits for jurisdictional arbitrage by allowing foreign entities to gain market exposure while bypassing the stringent "look-through" mechanisms typically required for direct domestic investments.

The paper utilizes the Adani-Hindenburg Research Report as a critical case study to demonstrate the practical application of these multi-entity fraud mechanisms. It argues that by routing funds through tax havens like Mauritius and the British Virgin Islands, insiders can circumvent Minimum Public Shareholding (MPS) requirements and engage in "round-tripping," effectively manipulating stock prices under the guise of being "public shareholders". The research notes that while SEBI has introduced proactive measures in

2024 and 2025,such as mandating granular disclosures for FPIs with concentrated holdings, the detection of fraud remains hindered by complex shell structures and a lack of multilateral

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cooperation. To address these systemic gaps, the author recommends a shift toward a jurisdiction-agnostic UBO verification system and the renegotiation of bilateral treaties like the Double Taxation Avoidance Agreement (DTAA) to ensure that regulatory oversight keeps pace with global financial engineering.

Citation: Rakshit Sharma, Tech Startups and Regulatory Arbitrage in India: A Socio-Legal Study of Compliance Avoidance and Social Costs, 3 White Black Legal L.J. 1 (2025).

This research explores the phenomenon of regulatory arbitrage within India's tech startup ecosystem, examining how companies in the fintech, edtech, and gig economy sectors exploit legal grey areas to scale rapidly while bypassing compliance. The author argues that regulatory arbitrage,the strategic exploitation of jurisdictional gaps and loopholes,is often framed as "entrepreneurial agility" but in reality, creates severe legal and social externalities. The paper highlights systemic gaps in the Companies Act, 2013, and SEBI norms, noting that startups frequently fall between the jurisdictional cracks of fragmented regulatory bodies like the RBI and SEBI. By examining sectoral case studies, such as gig platforms classifying workers as "independent contractors" to evade labor protections or fintechs operating without NBFC registration, the study underscores a pattern of "structured legal avoidance" that challenges corporate accountability.

Beyond legal analysis, the study employs a socio-legal approach to evaluate the significant "social costs" of these enforcement gaps, such as the lack of social security for gig workers and predatory lending practices in the unregulated fintech space. The author highlights that while the Digital Personal Data Protection Act, 2023 is a step toward closing these gaps, enforcement remains reactive rather than anticipatory, allowing innovation to outpace legal oversight. To mitigate these systemic risks, the paper advocates for "responsive regulation" and the use of regulatory sandboxes, which provide a controlled environment for innovation without sacrificing consumer protection or market integrity. Ultimately, the research calls for a unified, adaptive regulatory framework that balances technological growth with democratic legal norms and social responsibility.

Smitha, C., & Chendroyaperumal, C. (2011). Violation of SEBI ACT and Rules in India: A Study on 'Other than Collective Investment Scheme'. Saveetha Engineering College.

The historical landscape of the Indian market is characterized by a recurring cycle of financial misconduct, where new scams emerge every few years despite the continuous expansion of

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SEBI's statutory powers. Research indicates that India remains an "informationally weak market," allowing swindlers to exploit procedural and legal loopholes faster than regulations can be updated. This creates a "detection immunity window" where sophisticated participants use multi-entity structures to engage in price rigging and unfair trade practices,the most frequently violated provisions of the SEBI Act,enabling significant illicit gains before any regulatory intervention occurs.

Modern financial crimes, such as the IL&FS collapse, highlight how "subsidiary opacity" and "jurisdictional redundancies" facilitate regulatory arbitrage. Fraudsters deliberately structure transactions across different legal entities to exploit the lack of coordination between agencies like SEBI, the RBI, and the SFIO. Furthermore, technical gaps in insider trading regulations make it nearly impossible to prove connections within complex webs of entities, allowing participants to remain just below disclosure thresholds, such as the 1% FPI limit, to evade the "insider" or "promoter" labels while maintaining control.

Even when misconduct is detected, the enforcement framework often struggles with an "appellate safety valve" that dilutes the deterrent effect of penalties. Large-scale offenders frequently utilize lengthy appeals to the Securities Appellate Tribunal (SAT) to stay or reduce fines, often benefiting from the "proportionality doctrine" which views SEBI's penalties as too harsh. Comparative studies with the US SEC suggest that while Indian laws are pervasively modeled after global standards, the primary arbitrage gap lies in SEBI's lagging technological infrastructure and the need for greater judicial-regulatory cooperation to handle the complexities of modern algorithmic trading Singh, J. & Pandey, S. (2025). Corporate Governance Failures and White-Collar Crime: Evaluating India's Enforcement Framework. International Journal for Multidisciplinary Research (IJFMR), Vol. 7, Iss. 3.

This research examines the structural breakdown between corporate governance and legal enforcement in India, specifically analyzing how systemic weaknesses allow white-collar crimes like the IL&FS collapse to persist. The authors argue that while SEBI and the Companies Act of 2013 provide a robust statutory foundation, the actual enforcement of these laws is frequently paralyzed by "jurisdictional redundancies." This lack of coordination between key agencies,such as the SFIO, ED, and MCA,creates administrative silos that sophisticated fraudsters exploit to remain undetected until the financial damage has already become systemic.

The study identifies a critical "accountability gap" among directors, auditors, and management,

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where internal checks and balances fail to prevent misconduct. This relates directly to the concept of regulatory arbitrage discussed in your dissertation, as it highlights how multi-entity frauds are intentionally structured to fall into the "blind spots" of overlapping regulators. By operating across different regulatory jurisdictions, entities can
obscure their financial trails, effectively utilizing the government's own fragmented oversight as a shield against rapid detection and prosecution.

Ultimately, the paper concludes that India's current regulatory stance is "reactive" rather than "preventive," often intervening only after a total collapse has occurred. To close these enforcement gaps, the research suggests moving toward international standards, such as the implementation of Deferred Prosecution Agreements and technology-driven compliance. This aligns with your dissertation's proposal for a modernized surveillance architecture, suggesting that without integrated intelligence sharing and proactive oversight, the Indian market will remain vulnerable to the deliberate exploitation of its enforcement limitations.

Lesley, T. (2022). Insider Trading and its Regulatory Framework in India. Indian Journal of Integrated Research in Law, Vol. II, Iss. VI.
This research evaluates the efficacy of the Indian legislative framework in curbing insider trading, primarily focusing on the evolution from the 1992 regulations to the more "pragmatic" SEBI (Prohibition of Insider Trading) Regulations of 2015. The author defines insider trading as the illegal practice of utilizing unpublished price-sensitive information (UPSI) for personal gain, which fundamentally jeopardizes capital market integrity and creates an unfair playing field for retail investors. The study highlights that while the 2015
regulations have broadened the scope of "connected persons" and introduced automated system-driven disclosures, significant systemic hurdles remain.
The paper identifies several critical "lacunae" that facilitate regulatory arbitrage, most notably SEBI's difficulty in proving cases "beyond reasonable doubt" due to a persistent lack of evidence. A major investigative gap is noted in the misuse of modern communication channels, such as WhatsApp, where SEBI often struggles to establish the

link between a connected person and the leak of financial data. Furthermore, the research points to a severe resource disparity; for instance, the US SEC employs roughly 15 times more staff in corporate finance sectors than SEBI, resulting in a "paltry" enforcement workforce in India that lacks the infrastructure to adequately detect and analyze sophisticated trading patterns.

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To address these vulnerabilities, the author advocates for a shift in the "onus of proof" onto the defendant once a prima facie case is established, which would reduce enforcement costs and act as a stronger deterrent. The study also emphasizes the "problem of territoriality," noting that India lacks extra-territorial reach to effectively prosecute insiders trading on foreign exchanges, often leaving the regulator dependent on slow-moving bilateral MOUs. By comparing the Indian regime to the more "aggressive" misappropriation theories used in the US, the paper concludes that systemic reforms in investigative manpower and legal standards are essential to close the immunity windows exploited by sophisticated market participants.

This research presents a comparative analysis of the regulatory architectures of the United States and India, focusing on the efficacy of the SEC and SEBI in maintaining market integrity. The author identifies that while Indian securities laws are pervasive and modeled after global standards, the primary gap lies in "enforcement capability" and a lagging technology infrastructure compared to the more mature U.S. market. This disparity provides a fertile ground for regulatory arbitrage, as market participants exploit the "surveillance blindness" and the slower pace of regulatory action in India to engage in misconduct that might be preemptively blocked by the U.S. SEC's superior computerized databases and real-time monitoring systems.

The study highlights critical differences in disclosure requirements and the regulation of market participants, noting that the U.S. framework requires extensive electronic filings and detailed information on any security holder owning more than 10% of equity shares. In contrast, while SEBI has reinforced its oversight through various amendments, it continues to face issues in enforcement that result in occasional "breakdowns in investor trust". This relates directly to the concept of "disclosure threshold exploitation" discussed in your dissertation, where the lack of stringent, technology-driven oversight allows entities to hide beneficial ownership or bypass public float norms,as seen in the Adani-Hindenburg controversy,by exploiting the differences between Indian and international disclosure standards.

Ultimately, the paper concludes that strengthening SEBI’s investigative powers and technological synergy is essential for aligning India with global best practices. The author argues that greater judicial-regulatory cooperation is necessary to prosecute market misbehavior effectively and prevent "big swindlers" from using the legal system to delay or

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dilute penalties. These findings validate your dissertation's proposal for systemic reform, suggesting that closing the "detection immunity window" in India requires moving beyond reactive legislation toward a proactive, technologically-integrated enforcement model similar to the one established in the United States.

Reddy, Vinay and N, Prakash (1998) "The Sebi (Insider Trading) Regulation, 1992: A Critique," National Law School Journal: Vol. 10: Iss. 1, Article 10.
This foundational critique evaluates the original SEBI (Insider Trading) Regulations of 1992, arguing that the framework's narrow definitions and lack of clarity facilitate the very practices it seeks to prevent. The authors highlight that the definition of an "insider" is overly restrictive because it relies on a specific list of "connected persons," which excludes critical actors like legal advisors, auditors, and even relatives of directors. This structural limitation allows secondary insiders to escape liability despite having access to price- sensitive information, directly supporting your dissertation's thesis on how "disclosure threshold exploitation" and narrow statutory definitions create windows for regulatory arbitrage.

The research further identifies significant enforcement gaps regarding the scope of "dealings" and the nature of "unpublished price-sensitive information." By defining price-sensitive information through an exhaustive list rather than statutory illustrations, the regulation limits judicial flexibility in addressing novel manipulation tactics. Additionally, the paper points out that the 1992 framework fails to address transnational insider trading or provide civil remedies such as disgorgement of profits, leaving affected investors without clear means of recovery. This lack of a comprehensive deterrent mechanism reinforces the "appellate safety valve" concept, as the absence of precise definitions and defenses leads to inconsistent legal outcomes.

Ultimately, the authors recommend that SEBI adopt more expansive definitions similar to the English model to close these "glaring loopholes." They advocate for more precise language regarding when information becomes public and the introduction of civil remedies to make the regulations more "investor-friendly." These early warnings about systemic vulnerabilities in the regulatory architecture explain why multi-entity frauds have persisted; without precise definitions and proactive enforcement mechanisms, the market remains susceptible to participants who deliberately structure their activities to bypass outdated legal categories.

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Sharma, Rakshit. (2025). Tech Startups and Regulatory Arbitrage in India: A Socio-Legal Study of Compliance Avoidance and Social Costs. White Black Legal Law Journal, Vol. 3, Iss. 1.

This study explores how India's tech startup ecosystem, spanning fintech, edtech, and the gig economy, systematically utilizes regulatory arbitrage to bypass legal obligations and reduce compliance costs. The author defines this practice as the strategic exploitation of jurisdictional gaps and legal "grey areas" to achieve rapid scale, often at the expense of corporate accountability and consumer safety. While typically framed as entrepreneurial agility, the research argues that such compliance avoidance generates significant social externalities, including the erosion of public trust and the exploitation of vulnerable groups.

The research highlights specific sectoral tactics, such as gig economy platforms classifying workers as "independent contractors" to evade labor laws, and fintech startups offering credit-like products through partnerships to bypass stringent RBI non-banking financial company (NBFC) regulations. These practices allow firms to avoid mandatory social security benefits, minimum wage requirements, and strict financial oversight. The paper draws a direct parallel to the systemic "surveillance blindness" discussed in your dissertation, noting that while laws like the Companies Act and SEBI norms exist, their enforcement remains fragmented and reactive in the face of disruptive business models.

Ultimately, the study advocates for a shift toward "adaptive regulatory frameworks" and "responsive regulation" that can evolve alongside technological innovation. By integrating theoretical lenses like legal pluralism and social justice, the author emphasizes that sustainable innovation must align with democratic legal norms and ethical responsibility. This aligns with your dissertation’s call for architectural reform, suggesting that closing the gaps in the Indian market requires not just more rules, but a fundamental redesign of how regulatory institutions like SEBI and the RBI monitor and respond to multi-entity arbitrage.

Patel, Mitali and Sabne, Mayura. (2026). The Future of Financial Regulation: Domestic Laws and Regulations in India. Indian Journal of Law and Legal Research, Vol. VII, Iss. II.

This research evaluates the evolving landscape of financial regulation by contrasting international standards with Indian domestic laws, specifically focusing on how globalization and emerging technologies necessitate a more flexible regulatory approach.

The authors identify "regulatory arbitrage" as a core challenge, noting that the vast and dynamic

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nature of the market often results in SEBI facing difficulties in responding timely to irregularities. This finding supports your dissertation's focus on the "detection immunity window," suggesting that the delay between a market violation and regulatory intervention is a systemic weakness that sophisticated entities exploit to maximize illicit gains before enforcement actions are triggered.

The paper outlines several critical limitations within SEBI's current framework that facilitate arbitrage opportunities. It notes that SEBI's jurisdiction is primarily confined to domestic markets, making international enforcement against cross-border financial crimes,such as the offshore fund parking seen in the Adani-Hindenburg case,extremely difficult.

Furthermore, the study points out that the complexity of SEBI regulations can discourage small businesses while failing to stop malpractices in a large, scattered market where many violations simply go unnoticed. These enforcement gaps are compounded by concerns regarding regulatory autonomy and the influence of government appointments, which can potentially hinder aggressive oversight.

Ultimately, the authors argue for the integration of technology-driven solutions and the adoption of emerging standards like ESG and fintech-specific rules to protect market integrity. By promoting concepts like e-trading and dematerialization, SEBI has modernized the market, but the research emphasizes that without a "technology-friendly" and cooperative regulatory system, it will remain impossible to impose rules effectively over a market as complex as India's. This aligns with your dissertation's proposal for architectural reform, reinforcing the idea that closing detection gaps requires a shift from reactive, scattered enforcement toward a proactive, technologically integrated surveillance model.

Bhattacharjee, Shuchishrabha and Akshaya, AM. (2024). Regulatory Arbitrage in Financial Market: Causes, Consequences and Solutions. Indian Journal of Integrated Research in Law, Vol. IV, Iss. V.

This research provides a comprehensive analysis of regulatory arbitrage, defining it as the practice of exploiting differences in laws across jurisdictions to avoid taxes or bypass regulatory compliance. The authors argue that while this practice is often framed as a quest for efficiency, it significantly compromises market integrity and poses systemic risks to financial stability. By examining the mechanisms behind arbitrage, the paper identifies "jurisdiction shopping" and legal gaps,often created by rapid technological developments

and the rise of fintech,as primary drivers that allow market participants to evade traditional

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oversight.

The study highlights that regulatory arbitrage creates an uneven playing field, where sophisticated entities utilize complex legal structures to stay ahead of regulators, a theme that mirrors the "surveillance blindness" and "subsidiary opacity" explored in your dissertation. It notes that the fallout from such practices includes increased systemic hazards and the potential for financial crises, which necessitates a shift toward more flexible and adaptive regulatory strategies. The research underscores that the evolution of these practices is not merely a technological challenge but a fundamental threat to public confidence in financial institutions.

To address these vulnerabilities, the authors emphasize the need for international collaboration and responsive regulatory frameworks that can support innovation without sacrificing stability. They conclude that maintaining a stable financial system requires a careful balance between encouraging economic activity and upholding strict, proactive oversight. This aligns with your dissertation's call for systemic reform, reinforcing the idea that closing enforcement gaps requires ongoing study and a coordinated effort among legislators and regulators to keep pace with global financial shifts.

Sharma, Rakshit. (2025). Regulatory Arbitrage in Indian Securities Markets:
Systemic Analysis of Detection and Enforcement Gaps through Multi-Entity Fraud Cases.

This dissertation is about " arbitrage". Regulatory arbitrage is when people do frauds on purpose to take advantage of gaps in the way SEBI watches and enforces things. The dissertation looks at five cases: Ketan Parekh, IL&FS, Yes Bank, Adani and Jane Street. It finds that there are patterns that keep happening like "surveillance blindness" and "subsidiary opacity" that let people do things with multiple companies.

These frauds are designed to stay hidden until it's too late. They stay in a "detection immunity window" where they can make a lot of money before SEBI does anything. The
dissertation points out problems with the system like how people took advantage of a rule in the Adani case and how Jane Street used complicated algorithms to manipulate things.

It also talks about how the Securities Appellate Tribunal reduces penalties, which can make it so that SEBIs actions do not stop people from doing bad things. There are gaps between agencies like SEBI, RBI and the MCA that let fraudsters do what they want. They can operate in the " spots" of the system in India.

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The dissertation says we need to make some changes. It looks at what other countries, like the US and EU do and suggests that SEBI should do things like use technology to watch for algorithmic trading and make companies disclose who really owns them. It also says that agencies should work together to share information. This will help make sure that people who invest their money are protected from people who try to cheat them. Regulatory arbitrage will be. Sebi will be stronger.

CHAPTER 3.

Regulatory Arbitrage: Conceptualization

The anatomy of regulatory arbitrage

Arbitrage is when companies plan their financial activities to take advantage of differences in laws and rules. They do this to save money on compliance avoid taxes or get around rules they do not like. Of breaking the law they operate in "grey areas" or move across different countries to avoid being caught.In the securities market this means making complex deals with many entities to avoid detection by the Securities and Exchange Board of India (SEBI). This gives them a "detection immunity window" where they can make a lot of money before SEBI can catch on.

Big market players use methods to exploit these weaknesses. One way is "silo arbitrage" where they spread activities across legal entities to avoid being detected by different agencies like SEBI, the Reserve Bank of India (RBI) and the Ministry of Corporate Affairs (MCA).For example a financial crisis in one entity can be hidden through transactions with subsidiaries that are not directly regulated by the regulator. This lack of sharing information between agencies allows risks to build up without being detected.Entities also engage in threshold and definitional arbitrage to avoid transparency requirements. They keep shareholding levels below certain triggers to conceal ownership and exercise control.

The rise of the economy has made it easier to do regulatory arbitrage through technology and algorithms. Tech startups classify workers as " contractors" to avoid labor protections. Fintech firms partner with banks to offer products without strict regulations.In high-frequency trading sophisticated actors use algorithms to manipulate market order flows at speeds that traditional surveillance systems cannot monitor. This creates a challenge for regulators as the complexity of the digital trail often exceeds their resources.

The Architecture of Evasion: Mechanisms and Manifestations of Regulatory Arbitrage in India

entities use regulatory arbitrage to minimize compliance costs avoid taxation or bypass

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undesirable oversight. In the securities market this means making complex deals with many entities to evade SEBIs detection during critical phases. This gives them a "detection immunity window" to secure gains before SEBI can identify the anomaly or initiate enforcement action. Sophisticated market participants use mechanisms to exploit these structural limitations with "silo arbitrage" being a primary method.

For instance the IL&FS crisis showed how "subsidiary opacity" can conceal distress through undisclosed related-party transactions. This lack of time inter-agency intelligence sharing allows systemic risks to accumulate undetected.Entities engage in threshold and definitional arbitrage to bypass transparency requirements and maintain control. They keep shareholding levels below specific reporting triggers to conceal beneficial ownership as seen in the Adani-Hindenburg controversy.

The rise of the economy has expanded opportunities for regulatory arbitrage through technological and algorithmic arbitrage. Large financial players and tech-driven startups navigate gaps by classifying activities in ways that avoid strict institutional labels.In high-frequency trading sophisticated actors utilize complexity to manipulate market order flows at speeds that traditional surveillance systems cannot monitor. These practices create a onus of proof" challenge for regulators as the complexity of the digital trail often exceeds the investigative resources and technological infrastructure currently available, to Indian enforcement agencies.

The Grey Zone: The Non-Illegal Nature and Systemic Economic Costs of Arbitrage Regulatory arbitrage is an controversial thing in the financial system. It is not against the
law by definition. This is different from fraud or embezzlement which are clearly against the law. Regulatory arbitrage is like an art, where people use legal ways to follow the law but still undermine its purpose. They do this by using allowed types of companies, offshore
places and specific rules for disclosure. This means they can avoid getting in trouble with the law. However this does not mean that regulatory arbitrage does not have effects on the economy and the market.

The main bad effect of arbitrage is that it creates a lot of systemic risk. This happens when big companies like IL&FS use ways to move debt and liabilities around without being clear about it. They do this by using unlisted companies, which makes it hard for people to see the true state of the company. Because these actions are technically legal the risk builds up without anyone noticing. When the company eventually collapses, like in the 2018 liquidity crisis it

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affects not that company but the whole market. It makes it harder for other companies to borrow money. The government has to step in to help. This means that companies can make profits. The public has to bear the risks if they fail.

Regulatory arbitrage also hurts the market and investor confidence. In India companies can use loopholes to control companies without being clear about it. They do this by using structures and special notes. When regular investors find out that the market is being manipulated they lose trust. Take their money out. This makes the market more volatile. It is harder for companies to raise money. It also means that big companies can use their power to get ahead than competing fairly.

Finally regulatory arbitrage creates a playing field. Big companies can afford to hire lawyers and experts to find loopholes, which gives them an unfair advantage. This means that small companies, which have to follow the rules are at a disadvantage. Over time this leads to a situation where companies are more focused on finding loopholes than on being efficient. This hurts the economy. Makes it harder for new companies to start and grow.

SEBI's Regulatory Architecture: Institutional Drawbacks and Enforcement Limitations The reason why regulatory arbitrage is so successful in India is because of the weaknesses in the system. The Securities and Exchange Board of India (SEBI) has a time keeping up with the complicated ways that companies use to manipulate the market. SEBIs systems for monitoring the market are not good enough to catch all the things that companies do. This means that the market is vulnerable to manipulation and it is hard to catch the people who do it.

One of the problems is that the rules for disclosing who owns a company are not strong enough. Companies can use loopholes to hide who really owns them which makes it hard for SEBI to see what is going on. SEBI also does not have resources to investigate and enforce the rules. For example the US SEC has more staff than SEBI, which means that SEBI is not able to handle all the complex financial data that it needs to.

The way that SEBI enforces the rules is also not effective. There are many different agencies involved and they do not work well together. This creates gaps in the system that companies can exploit. SEBI also tends to react to problems after they have happened than trying to prevent them. This means that companies can get away with manipulating the market and it is hard to catch them.

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Finally the way that SEBIs decisions are reviewed is not effective. The Securities Appellate Tribunal (SAT) often reduces the penalties that SEBI imposes which means that companies do not take the rules seriously. They see the penalties as a cost of doing business rather than a serious punishment. This means that SEBI needs to be more aggressive, in enforcing the rules and it needs to work with the courts to make sure that companies are held accountable.

Systemic Economic Externalities: Impact on Market Competition and Foreign Capital

The practice of regulatory arbitrage exerts a profound and distorting influence on the broader economy by creating a bifurcated market environment that penalizes transparent entities while rewarding those with the resources to navigate legal grey areas. At the domestic level, this creates a significant "uneven playing field" where large, sophisticated corporations and tech-driven startups utilize their capital to hire legal architects who can bypass compliance costs through "silo arbitrage" or "jurisdiction shopping". In contrast, small and medium enterprises (SMEs) are often discouraged from entering the formal market because they must bear the full weight of complex SEBI regulations without the institutional capacity to exploit similar loopholes. This misallocation of resources leads to a "race to the bottom" where financial success is determined not by operational efficiency or innovation, but by the sophistication of a firm’s compliance-avoidance strategy, ultimately stifling genuine competition and economic productivity.

Beyond internal competition, regulatory arbitrage introduces severe "social externalities" and systemic risks that threaten national financial stability. When large entities like IL&FS utilize "subsidiary opacity" to conceal financial distress across unlisted entities, they effectively privatize their profits while socializing the risks of their eventual failure. Because these maneuvers often operate within a "detection immunity window," systemic hazards accumulate in regulatory blind spots until they trigger a contagion effect that freezes credit markets and necessitates state-led interventions. This creates a long-term economic downside where the state is forced into a cycle of "reactive legislation," imposing

increasingly stringent rules post-scandal that add a heavy "compliance tax" on legitimate businesses, further slowing the nation's overall growth.

The impact on foreign investors is equally damaging, as systematic arbitrage undermines the "market integrity" necessary to attract long-term global capital. When international participants observe sophisticated domestic entities exploiting disclosure thresholds,such as the 1% Foreign Portfolio Investor (FPI) rule,to conceal beneficial ownership, they perceive the Indian market

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as "informationally weak" and prone to manipulation. This erosion of trust leads to a higher "risk premium" on Indian equity, as foreign institutional investors (FIIs) demand greater returns to compensate for the potential of hidden regulatory vulnerabilities or "surveillance blindness". Furthermore, the difficulty of international enforcement against cross-border financial crimes, exemplified by offshore funds in the Adani case,can lead to reputational damage on the global stage, potentially lowering India's standing in international governance indices and causing capital flight toward more transparent jurisdictions.

Ultimately, the persistent use of arbitrage by large entities weakens the fundamental "social contract" between the state, the market, and its participants. By allowing a "deterrence deficit" to grow, where appellate review frequently dilutes SEBI's penalties, the system inadvertently signals to global and domestic players that rules are negotiable for those with sufficient legal reach. This environment disproportionately harms unsophisticated retail investors who lack the means to detect or protect themselves from multi-entity schemes, thereby violating broader social justice goals and undermining public confidence in democratic legal norms. Sustainable economic development requires a shift away from these fragmented oversight models toward an "adaptive regulatory framework" that can protect all market players from the predatory costs of strategic non-compliance.

Case Selection Rationale

The selection of cases for this dissertation is strategically designed to illustrate the chronological and technical evolution of regulatory arbitrage in the Indian securities market. Each case represents a distinct mechanism, ranging from traditional circular trading to sophisticated offshore parking and algorithmic manipulation, that has successfully exploited structural vulnerabilities in SEBI's surveillance and enforcement architecture.

Ketan Parekh Scam (1999-2001): Circular Trading and Surveillance Blindness

The Ketan Parekh case is selected as a foundational example of circular trading and entity aggregation utilized to manipulate market prices. By orchestrating transactions across a network of over 90 entities to artificially inflate stock values, the scam exposed critical failures in SEBI's real-time surveillance systems at the time. It serves as a historical benchmark for the "detection immunity window," demonstrating how multi-entity structures can facilitate substantial illicit gains over several years before the regulator can effectively intervene.

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IL&FS Financial Crisis (2018): Subsidiary Opacity and Coordination Gaps

The IL&FS crisis is included to analyze the risks associated with subsidiary opacity and the strategic use of complex corporate webs to conceal financial distress. With more than 340 subsidiaries engaged in unreported related-party transactions, the case illustrates how "silo arbitrage" can be used to evade consolidated oversight. Most significantly, it highlights the persistent inter-agency coordination failure between SEBI, the RBI, and the MCA, which allowed systemic risks to accumulate in regulatory "blind spots" for over three years.

Yes Bank-Rana Kapoor Case (2018-2023): Disclosure Evasion and Appellate Protection

This case is chosen to examine disclosure evasion and the impact of the appellate review process on the deterrence efficacy of Indian regulations. Through the issuance of personal guarantees for unlisted entities without board disclosure and the misselling of AT-1 bonds to retail investors, the case demonstrates how insiders exploit statutory gaps. Furthermore, it highlights the role of the Securities Appellate Tribunal (SAT) in potentially diluting enforcement through the "proportionality doctrine," which can significantly reduce penalties and undermine SEBI's authority.

Jane Street Market Manipulation (2025): Algorithmic Complexity and Modern Arbitrage

The Jane Street case is selected to represent the modern frontier of algorithmic manipulation and the shift toward technological arbitrage. By allegedly manipulating the Bank Nifty index through complex strategic index arbitrage, the case illustrates how sophisticated actors can exploit retail order flow at speeds that exceed traditional surveillance capabilities. This case underscores the "technological lag" within SEBI's current architecture (IMSS/DWBIS), where the complexity of digital order flows creates new opportunities for evasion.

Adani Group Controversy (2023): Offshore Parking and Threshold Exploitation

The Adani controversy is essential for its focus on offshore parking and the strategic exploitation of the 1% FPI disclosure threshold. This case demonstrates how offshore funds in jurisdictions like Mauritius and Cyprus can be leveraged to maintain "de facto" control while staying just below public reporting triggers. It highlights the "surveillance blindness" SEBI faces when dealing with beneficial ownership in complex global architectures, particularly when attempts are made to bypass minimum public float requirements.

CHAPTER 4

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SEBI's Regulatory Architecture:

Drawbacks, Limitations, and Systemic Vulnerabilities

SEBI

The Securities and Exchange Board of India (SEBI) stands at the intersection of India's aspirations for a deep, efficient capital market and the stubborn persistence of sophisticated financial fraud. Established by the SEBI Act, 1992, in the aftermath of the Harshad Mehta securities scandal, SEBI was conceived as an autonomous watchdog with quasi-legislative, quasi-judicial, and executive functions. Over three decades, it has unquestionably modernised India's markets, introducing dematerialisation, electronic trading, mandatory disclosure norms, and a sprawling regulatory apparatus that now governs over 10,000 listed entities, more than 70 million demat accounts, and daily equity market turnover exceeding ₹1 lakh crore.

Yet the five landmark fraud cases examined in this dissertation , Ketan Parekh, IL&FS, Yes Bank-Rana Kapoor, Jane Street, and Adani Group , share an uncomfortable common thread: each succeeded in exploiting identifiable, structural weaknesses in SEBI's regulatory architecture for extended periods. This is not a coincidence of unrelated bad actors; it is a systemic pattern. Sophisticated fraudsters do not merely break rules , they study the surveillance architecture and architect their schemes around its known blind spots. This deliberate exploitation is what this dissertation terms regulatory arbitrage.

This chapter undertakes a granular examination of SEBI's institutional design, operational mechanisms, and procedural architecture, and then subjects each element to comparative scrutiny against the US Securities and Exchange Commission (SEC) and the European Securities and Markets Authority (ESMA). The analysis proceeds in six parts: SEBI's institutional structure and statutory mandate; its surveillance and detection architecture; its disclosure and beneficial ownership framework; its inter-agency coordination mechanisms; its investigative and enforcement pipeline; and finally, its appellate review structure and deterrence calculus.

Institutional Structure, Statutory Mandate, and Design Philosophy

Constitutional and Legislative Foundation

SEBI derives its authority from the Securities and Exchange Board of India Act, 1992, which empowers it to regulate the securities market, protect investor interests, and promote the development of the market. The SEBI Act grants the Board quasi-legislative powers (issuing regulations, circulars, guidelines), quasi-judicial powers (adjudicating violations, passing orders), and executive powers (conducting searches, seizing documents, and investigating).

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Parliament has progressively augmented SEBI's powers through amendments , the Securities Laws (Amendment) Act 2014 was particularly significant, introducing provisions for call data record access, disgorgement of unlawful gains, and attachment of assets.

Structurally, SEBI is governed by a Board comprising a Chairman appointed by the Central Government, two full-time members from the Ministry of Finance, one from the Reserve Bank of India, and five other members. This composition immediately reveals a foundational tension: SEBI is formally autonomous, yet its top leadership is government-appointed and the Ministry of Finance occupies two Board seats. The US SEC, by contrast, is governed by five Commissioners appointed by the President and confirmed by the Senate, with no more than three from the same political party , a structural protection against executive capture that SEBI conspicuously lacks.

The Tripartite Function Problem

SEBI simultaneously acts as legislator (issuing LODR Regulations, PFUTP Regulations, Takeover Code), prosecutor (initiating adjudication proceedings), and judge (passing orders through its Whole Time Members). This concentration of functions has been critiqued by the Financial Sector Legislative Reforms Commission (FSLRC) and academic scholars as fundamentally compromising procedural fairness. When SEBI frames the regulations, investigates violations, and then adjudicates guilt, the due process concerns are structural rather than incidental.

The critical comparative insight is that the US SEC separates its enforcement and adjudicative functions more rigorously. The SEC's Division of Enforcement files cases either in federal district courts (external adjudication) or before Administrative Law Judges (ALJs) who are formally independent within the SEC structure and subject to Article III review. ESMA, operating as a pan-European supervisory authority, enforces against regulated entities while leaving final judicial determination to national courts. SEBI's Adjudicating Officers and Whole Time Members, who both investigate and decide cases, operate without equivalent structural separation, creating institutional confirmation bias, a tendency to credit the findings of one's own investigation division.

Resourcing and Capacity Asymmetry

SEBI's resource constraints relative to its mandate constitute a structural vulnerability that fraudsters implicitly exploit. As of 2024, SEBI employs approximately 900 officers for a market encompassing over 10,000 listed companies, 1,300+ mutual funds, 15,000+ registered

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intermediaries, and daily transactions worth lakhs of crores. The US SEC, regulating a market of comparable or only moderately larger complexity, employs over 4,500 staff. ESMA, coordinating 27 national competent authorities, has a combined regulatory workforce of several thousand. The per-regulated-entity staffing ratio at SEBI is a fraction of its Western counterparts.

This is not merely a headcount problem , it is a capability problem. SEBI has struggled to attract and retain professionals with expertise in quantitative finance, algorithmic trading, derivatives pricing, and complex structured products. When the Jane Street manipulation allegedly involved sophisticated algorithmic strategies exploiting index rebalancing arbitrage, SEBI's investigative team faced the challenge of reconstructing complex order-flow strategies that required understanding of delta hedging, gamma exposure management, and execution algorithms. The institutional knowledge gap between the regulated and the regulator is a persistent feature of India's securities enforcement landscape.

Surveillance Architecture: Mechanisms, Blind Spots, and Systemic Failure

SEBI's Integrated Market Surveillance System (IMSS)

SEBI's primary market surveillance tool is the Integrated Market Surveillance System (IMSS), operated in conjunction with stock exchanges, principally NSE and BSE, that maintain their own real-time surveillance systems. The surveillance architecture is layered: exchanges conduct first-line surveillance using automated alert systems, and refer suspicious activity to SEBI for second-level investigation. SEBI's Investigations Department then processes these referrals, supplemented by its own IMSS analysis and the Department of Economic Analysis and Policy (DEAP) for data analytics.

The IMSS generates alerts based on price movement patterns, volume anomalies, and concentration of trades. When price moves exceed pre-defined thresholds, typically a percentage deviation from moving averages or peer indices, the system flags the scrip for human review. This price-based detection model has a fundamental architectural flaw: it detects the consequence of manipulation (price distortion) rather than its cause (coordinated trading). By the time the price signal is anomalous enough to trigger alerts, the manipulation has typically been executing for days or weeks.

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The Fragmented Exchange-SEBI Pipeline

A critical and underappreciated structural flaw is the dependence on stock exchanges as first-line surveillance actors. NSE and BSE are for-profit, demutualised exchanges with commercial interests in maintaining high trading volumes and listing fees. The co-location scandal (2015-2019), where NSE's own systems were alleged to have provided preferential market access to certain algorithmic traders, demonstrated that exchanges are not disinterested surveillance partners. SEBI's dependence on exchange referrals for initiating most investigations means that patterns detectable only at the exchange level , such as the Ketan Parekh entities' coordinated intra-day circular trades , may not reach SEBI promptly if exchange surveillance incentives are misaligned.

The US SEC addressed this structural dependence by creating the Consolidated Audit Trail (CAT) , a comprehensive, centralised repository that captures every order, modification, cancellation, and trade across all national securities exchanges and FINRA member broker-dealers. CAT is maintained by FINRA under SEC oversight and is independent of any individual exchange's commercial interests. As of 2024, CAT processes over 100 billion market events daily, providing SEC examiners with a complete, queryable record of every market participant's order lifecycle , enabling pattern recognition across entities and time horizons that SEBI's fragmented, exchange-dependent system cannot replicate.

DWBIS: The Offshore Surveillance Gap

SEBI introduced the Data Warehousing and Business Intelligence System (DWBIS) to aggregate and analyse large-scale market data. While DWBIS represents a meaningful technological upgrade, it operates on domestically sourced data , trade records from Indian exchanges, depository records from NSDL and CDSL, and company filings from the MCA database. The critical surveillance gap is offshore.

The Adani-Hindenburg controversy illustrates this gap with forensic precision. Hindenburg Research's January 2023 report alleged that entities incorporated in Mauritius, Cyprus, and Cayman Islands , holding Indian securities through the Participatory Notes (P-Notes) and Foreign Portfolio Investor (FPI) route , were beneficially owned or controlled by Adani promoter-linked persons. If true, this would constitute a violation of minimum public shareholding norms and create undisclosed promoter concentration. SEBI's surveillance systems could observe the FPI's trading behaviour in Indian markets but could not independently verify beneficial ownership through the offshore corporate structures without requesting assistance from foreign regulators , a slow, treaty-dependent process.

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The EU's Market Abuse Regulation (MAR 596/2014) combined with the EU's Anti-Money Laundering Directive's Ultimate Beneficial Ownership registers requires disclosure of beneficial ownership down to natural persons holding more than 25% of any corporate entity. More importantly, under the European Market Infrastructure Regulation (EMIR), all derivatives transactions must be reported to designated trade repositories accessible to ESMA and national competent authorities in near-real-time. This dual transparency , in entity ownership and transaction reporting , systematically eliminates the offshore opacity that Indian regulations permit.

Algorithmic and High-Frequency Trading: The Complexity Frontier

The Jane Street matter (2025) represents the emergence of a new category of regulatory arbitrage: algorithmic complexity as a shield against detection. Jane Street allegedly employed strategies involving large-scale options positions in Bank Nifty index constituents, coordinated with cash market activity, to create artificial index levels that benefited their derivatives book. This form of manipulation , sometimes characterised as marking the close or index arbitrage manipulation , requires understanding of options gamma, index calculation mechanics, and the order flow dynamics of electronic markets.

SEBI's IMSS was designed primarily to detect older manipulation patterns: circular trading, pump-and-dump, and front-running. These involve relatively direct price-causation chains amenable to statistical pattern recognition. Algorithmic manipulation strategies involve multi-leg, multi-product strategies where the manipulative intent is embedded in the interaction between positions across the derivatives and cash segments , a pattern that may not trigger any single-product alert, and that requires cross-product, cross-segment analysis to reconstruct. SEBI does not currently have a publicly documented algorithmic surveillance methodology comparable to the SEC's Market Analysis and Research System (MARS) or ESMA's transaction-level reporting under MiFID II.

MiFID II, which came into force in 2018, requires investment firms in the EU to report transaction details , including algorithm identification fields , for every order submitted to any trading venue. Each algorithmic strategy must be tagged and disclosed, and any 'direct electronic access' (DEA) client must be identifiable. This creates a complete algorithmic audit trail that regulators can query retroactively. India's algo-trading framework, governed

by SEBI's 2012 circular on algorithmic trading and subsequent modifications, requires exchanges to perform order-level risk checks and mandates broker-level audit trails, but does

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not require the systematic, regulator-accessible transaction reporting that MiFID II establishes.

Disclosure and Beneficial Ownership Framework: Structural Loopholes

The FPI Disclosure Threshold: A Structural Arbitrage Entry Point

SEBI's Foreign Portfolio Investor (FPI) framework requires disclosure of granular beneficial ownership information only when an FPI's holding in a single company exceeds 50% of its corpus, or when the FPI holds more than 10% of the equity of a listed Indian company.

Below these thresholds, FPIs are required to disclose only broad category-level information, their registered jurisdiction, category (institutional, individual, etc.), and overall corpus size. Crucially, the beneficial ownership disclosure requirement , identifying the ultimate natural persons behind the FPI , is triggered only at the 1% aggregate FPI threshold for a listed company.

The Hindenburg report alleged that certain Mauritius-based FPIs held significant Adani group stock through P-Notes, with the underlying beneficial ownership concealed by a chain of opaque offshore structures. The regulatory arbitrage is mathematically precise: by ensuring that each individual FPI vehicle held positions carefully calibrated below the individual disclosure threshold, while the aggregate promoter-linked economic interest was allegedly far higher, the scheme could operate within the letter of SEBI's disclosure rules while violating their spirit.

The US SEC's Schedule 13D/13G beneficial ownership disclosure framework requires any person or group that acquires beneficial ownership of more than 5% of any class of equity securities of a Section 12 registered company to file a detailed disclosure within 10 days. Crucially, the SEC's rules define 'beneficial ownership' broadly to include persons who directly or indirectly, through any contract, arrangement, understanding, relationship, or otherwise, have or share: (i) voting power, or (ii) investment power. This functional definition, combined with the group filing concept under Section 13(d)(3), collapses the offshore shell strategy , a consortium of technically separate vehicles acting in concert is treated as a single beneficial owner for threshold calculation purposes.

Related-Party Transaction Disclosure: The IL&FS Architecture

The IL&FS financial crisis demonstrated a complementary disclosure failure: the inability of consolidated disclosure requirements to capture financial flows through a 340-entity subsidiary web. The SEBI LODR Regulations 2015 require listed companies to disclose 'material' related-party transactions (RPTs) to stock exchanges and seek shareholder approval. However, the

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definition of materiality has historically been set at 10% of annual consolidated turnover, a threshold high enough that individual intra-group transactions at the subsidiary level, though cumulatively vast, could evade the disclosure trigger.

More fundamentally, LODR disclosure requirements apply primarily to the listed holding company. The subsidiaries of IL&FS, through which allegedly inflated related-party transactions were routed to mask liquidity stress, were not individually listed, and their RPT disclosures in their standalone accounts were subject to Companies Act requirements rather than SEBI's more rigorous capital market disclosure regime. The regulatory gap between SEBI's jurisdiction (listed entities) and MCA's jurisdiction (all companies) created an opacity zone that the IL&FS management allegedly exploited.

SEBI has since reduced the materiality threshold and tightened RPT approval requirements through the 2021 LODR amendments, but the fundamental jurisdictional gap between SEBI and MCA remains. The EU's Transparency Directive and MAR require consolidated group disclosure that extends substantive obligations to material subsidiaries , a holistic approach that India's bifurcated SEBI/MCA framework structurally cannot replicate without legislative intervention.

Insider Trading Disclosure: Timing and Aggregation Gaps

SEBI's Prohibition of Insider Trading Regulations 2015 (PIT Regulations) require designated persons to maintain trading window closures around unpublished price-sensitive information (UPSI) events and to pre-clear trades above threshold sizes. However, the pre-clearance mechanism is company-administered, the compliance officer of the listed company (who is an employee of the same company) approves or denies trade requests by other designated persons. This creates a structural conflict of interest absent from the US system, where broker-dealers must maintain independent supervisory procedures and SEC examination scrutinises insider trading controls at the broker level.

The Rana Kapoor situation at Yes Bank illustrates how related-party and disclosure frameworks interact. Kapoor's issuance of personal guarantees for ₹950 crore to entities linked to Yes Bank borrowers , without board disclosure , implicated both RPT disclosure norms and insider trading concerns (his knowledge of the bank's deteriorating asset quality was UPSI). The complex interplay of LODR disclosure obligations, PIT Regulations, and RBI fit-

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and-proper norms for bank directors created jurisdictional confusion about which regulator had primary detection responsibility and enforcement jurisdiction.

Inter-Agency Coordination Failures: The Jurisdictional Labyrinth

The Three-Regulator Problem in Indian Finance

India's financial regulation is divided among three primary regulators , SEBI (capital markets), RBI (banking and monetary), and IRDAI (insurance) , alongside the Ministry of Corporate Affairs (MCA) for company law, the Enforcement Directorate (ED) for money laundering under FEMA/PMLA, the Central Bureau of Investigation (CBI) for criminal investigation, and the Income Tax Department for tax evasion. The Financial Stability and Development Council (FSDC), chaired by the Finance Minister, exists as a coordination body but has no independent operational authority.

This fragmentation creates what this dissertation terms the 'coordination immunity window' , the period during which a multi-entity fraud operates across regulatory boundaries, exploiting the assumption by each regulator that another agency has primary oversight responsibility. The IL&FS crisis is the paradigmatic example: SEBI's mandate covered the listed holding company and its bond issuances; RBI's mandate covered the systemically important NBFC subsidiaries; MCA's remit covered all 340+ group companies under the Companies Act. The actual liquidity fraud , the rolling over of short-term commercial paper to fund long-term illiquid infrastructure assets , operated precisely in the interstices of these three mandates.

SEBI-RBI Coordination: Structural Friction

The SEBI-RBI relationship is characterised by structural tensions rooted in institutional culture and regulatory philosophy. RBI is India's oldest and most powerful financial regulator, with a mandate encompassing monetary policy, banking supervision, foreign exchange, and payment systems. SEBI is comparatively newer and more narrowly mandated. When the Yes Bank situation emerged, involving both capital market misconduct (AT-1 bond misselling to retail investors, related-party guarantee disclosure failures) and banking supervisory failures (deteriorating asset quality masked by governance failures), the two regulators operated largely through their separate investigative and enforcement channels.

RBI exercised its banking supervisory powers to impose a moratorium, reconstitute Yes Bank's board, and orchestrate a rescue through SBI-led capital infusion. SEBI investigated the capital market disclosure violations. Neither regulator had a protocol for jointly presenting evidence,

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coordinating investigation timelines, or developing a unified case theory that would have enabled a more comprehensive fraud reconstruction. The result: SEBI's ₹3 crore penalties addressed only the capital market violations, while the broader scheme of related-party diversion, which implicated bank lending decisions as much as capital market disclosure, remained inadequately addressed in aggregate enforcement terms.

The US approach to cross-regulator coordination is institutionalised through the President's Working Group on Financial Markets and, more operationally, through the Financial Crimes Enforcement Network (FinCEN), which serves as the intelligence hub connecting SEC, CFTC, bank examiners (OCC, FDIC, Federal Reserve), and law enforcement (DOJ, FBI). The SEC's formal Memoranda of Understanding (MOUs) with banking regulators establish specific information-sharing protocols and case-referral procedures. Critically, the DOJ's securities fraud prosecutors are embedded in US Attorney's Offices with formal coordination protocols with the SEC's Enforcement Division, enabling simultaneous civil and criminal actions with shared evidentiary bases. India's CBI-SEBI coordination has no comparable institutionalised protocol, and has historically been ad hoc and reactive.

The FEMA-SEBI-ED Triangle and Offshore Flows

When Indian capital market fraud involves offshore entities , as in the Adani offshore fund allegations and the Ketan Parekh circular trading network that involved Mauritius-based entities , SEBI's investigation necessarily intersects with FEMA enforcement (RBI's mandate) and anti-money laundering enforcement (ED's mandate under PMLA). The investigative trail for offshore entity ownership requires FEMA compounding investigation records from RBI, ED's PMLA attachment orders and financial intelligence, and SEBI's own LODR/PFUTP analysis.

These three agencies operate under separate statutory mandates, with different evidentiary standards, different powers of summons, and different document sharing protocols. A suspected front entity in Mauritius requires a request through India's mutual legal assistance treaty (MLAT) with Mauritius, coordinated through the Ministry of External Affairs , a process that can take years. SEBI's own 2024 status report to the Supreme Court acknowledged that its Adani investigation had been pending for 24 show cause notices over two years, with offshore entity verification being a cited constraint.

The EU's regulatory architecture addresses this through the ESMA-EBA-EIOPA Joint

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Committee, which coordinates cross-sectoral supervision and shares granular data across financial sectors in near-real-time. The EU AML Authority (AMLA), established under the 2024 AML package, will centralise beneficial ownership verification and coordinate with national financial intelligence units (FIUs) across 27 member states. India's Financial Intelligence Unit (FIU-IND) exists as an interface with Egmont Group networks but lacks the data-sharing infrastructure to provide SEBI with rapid, actionable offshore beneficial ownership intelligence.

The Investigative and Enforcement Pipeline: Delay, Dilution, and Deterrence Failure

SEBI's Investigative Process: Anatomy of Delay

SEBI's enforcement pipeline follows a sequential, multi-stage process that, while designed to ensure procedural fairness, structurally enables the detection immunity windows that sophisticated fraudsters exploit. The typical investigation lifecycle proceeds through: (1) market surveillance alert or complaint receipt; (2) preliminary examination; (3) formal investigation order; (4) investigation by SEBI's Investigations Department; (5) show cause notice (SCN) issuance; (6) personal hearing; (7) adjudication order or Whole Time Member (WTM) order; (8) appeal to the Securities Appellate Tribunal (SAT); and potentially (9) appeal to the Supreme Court.

The Ketan Parekh case illustrates the consequence of this pipeline's latency. Circular trading across 90+ entities inflated multiple stocks during 1999-2001; SEBI's investigation order was issued in 2001, but the final enforcement orders came in 2007 , six years after the scheme's peak operation. Maximum penalties imposed were ₹1.05 lakh , a derisory sum relative to profits that SEBI's own orders estimated at hundreds of crores. By the time enforcement concluded, the statute of limitations, asset dissipation, and offshore transfer had rendered recovery essentially impossible.

The structural source of investigative delay is twofold. First, SEBI's Investigation Department is chronically understaffed relative to caseload, with complex multi-entity cases requiring forensic reconstruction of trading networks across thousands of entities over multi-year periods. Second, SEBI lacks compulsory testimony powers equivalent to the SEC's Section 21(a) investigative subpoena, which allows the SEC to compel witness

testimony under oath with the full backing of federal court contempt jurisdiction. SEBI can issue summons under Section 11C of the SEBI Act, but enforcement of summons compliance through courts is slow, and witnesses who provide false information face limited, rarely-

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invoked penalties.

Penalty Quantum: The Deterrence Calculus Problem

SEBI's maximum civil penalties under the SEBI Act were enhanced by the 2014 amendments to ₹25 crore per violation or three times the illicit profit (whichever is higher). While this represents a significant statutory improvement from earlier caps of ₹5 crore, the actual penalty quantum imposed in practice frequently falls far short of the statutory ceiling. Adjudicating Officers and WTMs apply a proportionality analysis that considers factors including the nature of violation, investor harm caused, and the accused's financial position , and have historically imposed penalties substantially below maximum levels in contested proceedings.

The deterrence calculus for a sophisticated financial fraudster involves comparing: (a) the expected illicit profit from the fraud, discounted by the probability of detection; against (b) the expected penalty, discounted by the probability of successful appellate reduction.

When detection probability is low (years-long investigation lag), successful appellate reduction is high (SAT's proportionality doctrine, discussed below), and the penalty ultimately imposed is a fraction of illicit profits, the expected cost of fraud is often a small percentage of its expected return. This is the fundamental deterrence failure at the heart of SEBI's enforcement architecture.

The US SEC's enforcement toolkit addresses this through multiple complementary mechanisms. First, the SEC can pursue disgorgement of illicit profits as a civil equitable remedy (now codified in the 2020 NDAA following SEC v. Liu), which ensures that fraudsters cannot retain gains even when penalty caps would otherwise allow it. Second, parallel DOJ criminal prosecution , with prison sentences , transforms the deterrence calculus entirely: no rational actor accepts prison risk for financial gain in the way they might accept financial penalties. Third, the SEC's Whistleblower Program (Section 21F of the Securities Exchange Act) provides whistleblowers 10-30% of sanctions exceeding $1 million, generating over $1.3 billion in awards and facilitating detection of frauds that surveillance systems alone would not catch.

The Yes Bank SAT Stay: A Case Study in Appellate Deterrence Erosion

The Yes Bank-Rana Kapoor enforcement action provides a textbook illustration of how appellate relief erodes enforcement deterrence. SEBI's Adjudicating Officer imposed aggregate penalties exceeding ₹3 crore on Rana Kapoor for disclosure violations relating to his personal

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guarantees and AT-1 bond misselling. On appeal to SAT, the Tribunal granted a stay on the penalties pending hearing, conditioning the stay on deposit of only ₹50 lakh , effectively reducing the immediate financial consequence of SEBI's penalty by 94% pending a multi-year appellate process.

This pattern recurs systematically. SAT's jurisprudence has developed a 'proportionality doctrine' , derived from administrative law principles , under which it scrutinises SEBI penalties for proportionality to the specific harm caused and the accused's financial capacity. While proportionality review has legitimate administrative law foundations, its application to financial market penalties creates a structural problem: the penalty quantum needed for deterrence (high enough to outweigh expected illicit profits for a well-resourced fraudster) will often fail a proportionality test calibrated to 'harm caused' in a narrow sense that ignores market integrity externalities and systemic deterrence value.

The US court system, handling SEC civil enforcement actions in federal district courts, applies a different standard: courts defer substantially to agency penalty determinations and focus their review on whether the penalty is within statutory limits and supported by the record , not whether it is 'proportionate' to a narrow conception of direct harm. This doctrinal difference has significant practical consequences for the sustained deterrence capacity of securities enforcement.

The Securities Appellate Tribunal: Guardian of Due Process or Enforcement Obstacle?

SAT's Constitutional Position and Mandate

The Securities Appellate Tribunal (SAT) was established under Sections 15K-15P of the SEBI Act as the dedicated appellate body for SEBI enforcement orders. SAT comprises a Presiding Officer (with the status of a High Court judge) and two other members, and its

decisions are directly appealable to the Supreme Court. SAT's creation was a genuine due process improvement , SEBI's combination of investigative and adjudicative functions in its WTM orders required an independent appellate check, and SAT provides that external scrutiny. However, SAT's design has produced several systemic effects adverse to enforcement deterrence. First, SAT's appellate review is broad , it can examine both questions of law and fact, essentially re-conducting the merits analysis. This is different from the more deferential 'abuse of discretion' standard that US federal courts apply to SEC ALJ decisions and that courts typically apply to agency factual findings under the 'substantial evidence'

test. SAT's de novo fact-finding capacity means that SEBI's investigation, even if meticulous,

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must survive a full re-examination , incentivising well-resourced accused to pursue SAT appeals as delay mechanisms regardless of underlying merits.

The Stay Problem: Systematic Enforcement Nullification

SAT's liberal stay jurisprudence , granting interim stays on penalty orders pending appeal upon deposit of a fraction of the penalty , has the effect of systematically nullifying SEBI's immediate enforcement impact. When a sophisticated accused can appeal a ₹25 crore penalty to SAT, secure a stay for deposit of ₹2-3 crore pending a 2-3 year appellate process, and then potentially have the penalty reduced on the merits, the effective present-value cost of the enforcement action may be only 10-15% of the nominal penalty.

SEBI has sought to address this through the Securities Laws (Amendment) Act 2014, which introduced Section 15JB providing for disgorgement of unlawful gains in addition to penalty. However, SAT has stayed disgorgement orders in several cases pending appeals, diluting this mechanism as well. The Supreme Court, in SEBI v. Sahara India Real Estate Corporation (2012), emphasised SEBI's investor protection mandate and granted SEBI significant enforcement powers , but the Court's docket constraints mean that Supreme Court enforcement of SEBI orders is inherently slow.

Structural Reform Directions: Learnings from Comparative Jurisprudence

The UK Financial Conduct Authority (FCA) offers a useful intermediate model. FCA enforcement decisions that include financial penalties above £10 million are automatically referred to the Upper Tribunal (Financial and Tax), with the Upper Tribunal applying a 'de novo' merits review. However, FCA procedures for 'decision notices' include robust internal review through a Regulatory Decisions Committee (RDC) , independent of FCA enforcement , which provides internal due process before external appeal. The result is a process where external appellate review is genuinely independent but is preceded by rigorous internal review, reducing the rate of successful external appeals on procedural grounds.

A reform model for SEBI might involve: (1) establishing a genuinely independent adjudication panel within SEBI , with members appointed through a transparent, merit-based process independent of the SEBI Chairman , to separate the investigative and adjudicative functions; (2) constraining SAT stays on enforcement orders to require deposit of a minimum percentage (e.g., 50%) of the penalty pending appeal; and (3) enacting a statutory presumption of correctness for SEBI's factual findings, limiting SAT review of facts to the 'perversity' standard

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and focusing appellate scrutiny on legal questions.

Technology and Data Architecture: The Modernisation Imperative

The Legacy System Constraint

SEBI's surveillance and enforcement technology architecture reflects the historical sequencing of Indian capital market development , systems built in the 1990s-2000s for cash equity market oversight, progressively patched to accommodate derivatives, then algorithmic trading, and now high-frequency and cross-product strategies. The IMSS, DWBIS, and exchange surveillance systems were not designed with cross-product, cross-

market, algorithmic manipulation in mind. Retrofitting legacy architecture to handle these use cases is demonstrably harder than building purpose-fit systems.

The Jane Street intervention required SEBI to conduct physical raids seizing 100+ computers from 80+ locations , a dramatically resource-intensive investigation model compared to what a comprehensive electronic transaction audit trail would enable. If SEBI had MiFID II-equivalent algorithm-tagged transaction reporting for every order placed on NSE and BSE, the complete trading record for Jane Street's strategies would be available for electronic querying within minutes of a complaint, rather than requiring physical asset seizure and forensic reconstruction.

Artificial Intelligence and Machine Learning: Unrealised Potential

SEBI has acknowledged the potential of AI/ML for market surveillance in its discussion papers and annual reports, and has engaged with technology vendors on pilot programs.

However, the institutional barriers to deploying effective AI-based surveillance are not merely technical , they are structural. Effective ML-based manipulation detection requires:

(a) comprehensive, high-quality training data (which requires the kind of transaction-level reporting India currently lacks); (b) significant domain expertise in financial mathematics and market microstructure to design and validate detection models; (c) ongoing model maintenance and adversarial updating as fraudsters adapt; and (d) a clear legal framework for using algorithmic alert outputs as evidence in enforcement proceedings.

The SEC's Division of Economic and Risk Analysis (DERA) employs over 150 economists, data scientists, and quantitative analysts who build and maintain surveillance models, conduct economic analysis of enforcement cases, and provide expert witness testimony.

SEBI's DEAP, while capable, operates with a fraction of this capacity and without the depth of

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quantitative expertise that complex algorithmic case reconstruction requires. This is not merely a budgetary gap, it reflects a structural difference in how India and the US conceptualise the role of quantitative expertise in securities regulation.

Synthesis: Regulatory Arbitrage as a System Property

The analysis in this chapter reveals that India's regulatory arbitrage vulnerabilities are not isolated defects amendable through targeted legislative patches. They constitute a systemic architecture problem , the aggregate product of institutional design choices made over decades that collectively produce predictable blind spots, exploitable by sophisticated actors with the resources to study and map SEBI's detection capabilities.

Five structural properties generate the regulatory arbitrage landscape described in the preceding sections. First, SEBI's surveillance architecture is consequence-oriented (detecting price distortion after manipulation) rather than cause-oriented (detecting manipulative order patterns during execution). Second, SEBI's disclosure framework is threshold-driven rather than substance-driven, enabling entities to calibrate their structures precisely below disclosure triggers. Third, inter-agency coordination is treaty-dependent and informal for offshore investigations, creating investigation timelines that exceed the operational lifespan of fraud schemes. Fourth, SEBI's enforcement pipeline latency , from detection to final order , routinely spans 3-7 years, enabling asset dissipation and profits retention pending final adjudication. Fifth, appellate review structures systematically reduce the expected cost of enforcement, eroding the deterrence premium that aggressive enforcement is intended to create.

This five-property architecture creates a permissive environment for regulatory arbitrage that individual enforcement actions, however vigorous, cannot systematically address. What is required is architectural reform: a fundamental redesign of the surveillance, disclosure, coordination, and enforcement systems rather than amendment within the existing framework. Chapter 5 examines the specific mechanisms from SEC and ESMA frameworks that would address each identified limitation, and Chapter 6 proposes a targeted Indian implementation roadmap.

CHAPTER 5

International Comparative Analysis and SEBI's Regulatory Failures Across Five Landmark Cases

Introduction: The Comparative Framework

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The preceding chapters have established both the theoretical architecture of regulatory arbitrage and the systemic limitations of SEBI's institutional design. This chapter applies that analytical framework to the five landmark cases at the core of this dissertation, Ketan Parekh, IL&FS, Yes Bank-Rana Kapoor, Jane Street, and Adani Group, examining each case in granular detail, identifying the specific regulatory failures that enabled it, and benchmarking those failures against how equivalent conduct would have been detected, prosecuted, and deterred under the US SEC and EU ESMA frameworks.

The structure for each case follows a consistent analytical method: first, a detailed reconstruction of the fraud's mechanism and execution; second, a precise mapping of which SEBI framework limitations created the conditions for the fraud to operate; and third, a comparative analysis of how the US and EU regulatory architectures would have responded differently. This case-by-case approach is not merely an exercise in institutional comparison, it is the evidential foundation for the reform proposals in Chapter 6, demonstrating that the identified limitations are not theoretical but have concrete, documented consequences in each of India's most consequential market fraud cases.

Case I: The Ketan Parekh Scam (1999–2001)

The Fraud: Mechanism and Execution

The Ketan Parekh scam represents the most elaborate circular trading network in Indian securities market history, and in many respects it remains the archetypal case study of how entity proliferation can defeat surveillance systems built around individual account monitoring. Ketan Parekh, a Chartered Accountant by training and a stockbroker by practice , operated through a network of over ninety entities, including broker firms, investment companies, and shell vehicles, to orchestrate coordinated price inflation across a select group of stocks that became known as the 'K-10' scrips: Himachal Futuristic Communications, Global Tele-Systems, Zee Telefilms, Pentasoft Technologies, and others, predominantly technology, media, and telecommunications companies riding the global dotcom enthusiasm of the late 1990s.

Parekh's method was architecturally sophisticated for its era. The scheme operated in three operationally distinct phases. In the accumulation phase beginning in 1998-1999, Parekh entities quietly built positions in low-liquidity technology stocks using bank finance, crucially, funds borrowed from cooperative banks including Madhavpura Mercantile Cooperative Bank, which extended credit against securities collateral in flagrant violation of RBI's credit norms. The cooperative bank channel was deliberately chosen because cooperative banks fell outside RBI's direct supervisory jurisdiction at the time, falling instead under state registrar supervision, a jurisdictional gap that Parekh mapped and exploited.

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In the inflation phase, the network of entities executed circular trades , simultaneously buying and selling the same securities among related accounts , to generate artificial volume and price momentum. The critical design insight was that each individual entity appeared as an independent market participant. Entity A would buy from Entity B; Entity B would buy from Entity C; Entity C would buy from Entity A , each transaction appearing, in isolation, as a legitimate arm's length trade. SEBI's surveillance systems of the era monitored individual scrip price movements and individual account activity, but lacked the entity aggregation capability to observe that the same beneficial controller was on both sides of every 'trade.'

The Adani connection in this case is particularly instructive for the dissertation's broader themes. SEBI's subsequent investigation found that fourteen Adani private companies transferred approximately ₹3.4 billion to Ketan Parekh-linked entities between February and August 2000. Adani Exports' stock price was inflated from approximately ₹570 to ₹1,111 during this period, a 95% appreciation with no corresponding fundamental business improvement. The mechanism was bidirectional: Parekh entities received funds from Adani companies, used them to inflate Adani stock, and the inflated stock served as collateral for further bank borrowings that funded further inflation across the K-10 basket.

The distribution phase , selling inflated shares to retail investors and institutional funds attracted by the price momentum , coincided with the global dotcom crash of March 2000. As global technology valuations collapsed, the artificial price support that Parekh's circular network was providing became financially unsustainable. The network unwound catastrophically, with Madhavpura Mercantile Bank facing a ₹800 crore exposure against collateral whose value had evaporated, and retail investors left with near-worthless securities purchased at peak artificial prices. The aggregate estimated loss to investors exceeded ₹40,000 crore.

SEBI's formal investigation order was issued in 2001. The final enforcement orders , passed in 2007 , imposed penalties on Parekh of ₹1.05 lakh and a market ban. The investigation took six years; the penalty was a fraction of a percentage of estimated illicit profits.

SEBI Framework Limitations

The Ketan Parekh case exposed four fundamental SEBI framework limitations with forensic clarity. The first and most consequential was the absence of entity aggregation in surveillance. SEBI's IMSS monitored price and volume at the scrip level and activity at the individual account level , but had no mechanism for attributing multiple accounts to a single beneficial controller and examining their collective trading pattern. A network of ninety

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entities, each appearing independently, was functionally invisible to a surveillance architecture designed around individual account monitoring. This is not an implementation failure , it is an architectural design failure.

The second limitation was the cooperative bank regulatory gap. Parekh's entire financing architecture depended on borrowing from cooperative banks that were outside RBI's direct supervisory purview. The SEBI Act gave SEBI no jurisdiction over bank lending practices; RBI's jurisdiction over cooperative banks was fragmented between its oversight of banking operations and state government oversight of cooperative societies. The scheme exploited this jurisdictional gap with precision , the funding pipeline that sustained the inflation operated entirely in a regulatory no-man's land.

The third limitation was SEBI's lack of real-time cross-market data. Parekh's circular trades were executed during market hours, creating intraday price and volume patterns that would have been detectable with real-time cross-entity surveillance. However, SEBI's data access in this period was largely end-of-day batch data, by the time suspicious patterns were assembled for review, the trading day had ended and the evidence was historical rather than actionable.

The fourth limitation , relevant to deterrence rather than detection , was the six-year investigation timeline and the nominal penalty that resulted. The combination of detection delay and penalty inadequacy meant that the scheme's expected enforcement cost, viewed prospectively, was negligible relative to its expected return. This is the deterrence failure in its purest form.

US SEC and EU ESMA Comparative Analysis

Under the US framework, the Consolidated Audit Trail would have attributed all ninety Parekh entities' trading to their common beneficial owner from the first trade , making the circular pattern visible as a network phenomenon in real-time. The SEC's EDGAR beneficial ownership disclosure system would have required Parekh's aggregate position in each K-10 stock to be disclosed under Schedule 13D once it crossed 5%, regardless of how many vehicles held the position. And the SEC's pattern-of-racketeering provisions under RICO, available to DOJ in parallel criminal prosecution, would have enabled asset seizure at the investigation stage, not after a six-year civil enforcement process.

Under EU frameworks, MiFID II's algorithm and order tagging, combined with MAR's explicit prohibition on artificial volume creation through coordinated trading, would have provided the direct legal hook. More practically, the EU's suspicious transaction reporting (STR) obligation

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, requiring brokers and investment firms to report suspicious trading patterns to national competent authorities within 24 hours , would have generated regulatory alerts from the multiple brokers executing Parekh's circular trades far earlier than SEBI's own surveillance systems.

Case II: The IL&FS Financial Crisis (2018)

The Fraud: Mechanism and Execution

The Infrastructure Leasing and Financial Services (IL&FS) crisis represents a qualitatively different fraud typology from Ketan Parekh's market manipulation, it is a governance and disclosure fraud executed through corporate structural complexity, and it produced the most severe near-systemic financial shock that India's capital markets have experienced in the post-liberalisation era. When IL&FS's first default on commercial paper obligations occurred in June 2018, followed by cascading defaults across its entities through September 2018, the Indian commercial paper market effectively froze, non-banking financial company (NBFC) stocks collapsed, and the Reserve Bank of India was compelled to intervene in a manner not seen since the 2008 global financial crisis.

IL&FS had been incorporated in 1987 as a public-private partnership vehicle for infrastructure financing, with shareholders including LIC, ORIX Corporation of Japan, Abu Dhabi Investment Authority, and various Indian public sector financial institutions. By 2018, the IL&FS group comprised over 340 subsidiaries and associate companies , a corporate structure of staggering complexity that had grown organically over three decades of project financing across roads, bridges, ports, and energy infrastructure. IL&FS's total debt stood at approximately ₹91,000 crore at the time of crisis.

The fraud mechanism was not a single criminal act but an extended pattern of misrepresentation that operated across several interlocking dimensions. The first was maturity transformation concealment: IL&FS's infrastructure projects typically had 20-25 year revenue generation profiles, but were being funded through short-term commercial paper with 90-180 day maturities that needed continuous rollover. This fundamental asset-liability mismatch was structurally unsustainable , any disruption in the commercial paper market's willingness to roll IL&FS paper would trigger default cascades. The management was aware of this structural vulnerability from at least 2014, according to the SFIO investigation report, but the commercial paper issuances continued with credit ratings of AAA and AA+ maintained through what the SFIO found to be a process of misrepresenting cash flows and concealing subsidiary-level distress.

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The second dimension was the subsidiary opacity mechanism. IL&FS's 340+ entities were organised in multiple holding layers, with the listed holding company (IL&FS Limited) at the apex and operating subsidiaries several layers removed. Related-party transactions between subsidiaries, including circular fund flows designed to make cash-strapped entities appear liquid were executed at the subsidiary level and disclosed, where disclosed at all, only in standalone subsidiary accounts that no analyst or regulator was practically capable of consolidating across 340 entities. The SFIO found that certain senior management members had caused funds to be transferred between subsidiaries in patterns that concealed the group's true liquidity position from the consolidated accounts.

The third dimension was the capture of governance mechanisms. IL&FS's board included nominees from LIC, ORIX, HDFC, SBI, and other institutional shareholders, nominally sophisticated and independent. Yet the board failed to detect or disclose the liquidity crisis as it developed. IL&FS's statutory auditor, BSR and Associates (a KPMG affiliate), issued unqualified audit opinions on financial statements that the SFIO subsequently found to be materially misleading. The rating agencies , CARE Ratings, ICRA, and India Ratings , maintained investment-grade ratings on IL&FS commercial paper until days before the first default, despite access to financial information that, on the SFIO's analysis, should have revealed the liquidity stress years earlier.

SEBI Framework Limitations

The IL&FS crisis exposed the fundamental limitation of SEBI's jurisdiction-as-gateway approach to financial regulation. SEBI's oversight extended to IL&FS Limited as a listed entity and to its debt securities listed on stock exchanges , but not to the unlisted operating subsidiaries that were the actual locus of the liquidity crisis. The 340+ subsidiary structure meant that the fraud operated below SEBI's jurisdictional horizon: SEBI could observe the consolidated accounts of the listed holding company (which concealed the subsidiary-level distress) but had no direct access to the subsidiary cash flows, intra-group transactions, and maturity profiles that would have revealed the structural problem.

The materiality threshold problem was equally significant. SEBI's LODR Regulations required disclosure of related-party transactions above 10% of consolidated annual turnover. In a group of IL&FS's size, individual intra-group transactions, even those that cumulatively constituted hundreds of crores of circular fund flows, fell below this threshold. The disclosure framework, by design, filtered out precisely the granular transactional information that would have revealed the subsidiary-level manipulation.

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The three-regulator problem was nowhere more consequential than in IL&FS. SEBI had jurisdiction over the listed entity and its debt securities. RBI had jurisdiction over IL&FS Financial Services, the group's NBFC subsidiary, which was a systemically important financial institution. MCA had jurisdiction over all 340+ entities as registered companies under the Companies Act. None of these three regulators had visibility into the complete group cash flow dynamics , and no coordination mechanism existed to assemble the three perspectives into a unified group-level risk assessment. The SFIO investigation, initiated only after the crisis had broken, took over a year to reconstruct what a real-time coordinated surveillance mechanism should have been detecting continuously.

The credit rating agency failure intersects with a specific SEBI regulatory gap: SEBI regulates credit rating agencies under the SEBI (Credit Rating Agencies) Regulations, 1999, but the enforcement history of those regulations against rating agencies that issue negligent or conflicted ratings is essentially blank. No credit rating agency has faced meaningful enforcement action from SEBI for failure of the ratings process, a regulatory forbearance that has no equivalent in the SEC's enforcement record, which includes multiple enforcement actions against rating agencies arising from the 2008 financial crisis.

US SEC and EU ESMA Comparative Analysis

The US SEC's approach to conglomerate disclosure under Regulation S-K would have required IL&FS to provide segment-level financial information for each material business segment, with disclosure of all material related-party transactions regardless of which level of the group structure they occurred at. The SEC's focus on substance over form in related-party transaction disclosure , enforced through Rule 10b-5's broad prohibition on material misstatements , would have made the subsidiary-level fund flow manipulation legally problematic at the moment of the misleading consolidated disclosure, not only after a
post-crisis SFIO investigation.

The EU's systemic risk framework is perhaps more directly applicable. Under the EU's Financial Conglomerates Directive (FICOD), an entity like IL&FS , operating across banking, insurance, and capital market activities through its subsidiary structure , would be
designated a 'financial conglomerate' subject to supplementary supervision at the group level by a 'coordinator' regulator. This group-level supervisor would have had direct access to consolidated group cash flows, intra-group transaction data, and group-level capital and liquidity adequacy assessments. The absence of any equivalent group-level supervision

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framework in India is the single most direct regulatory gap exposed by IL&FS.

Case III: Yes Bank and Rana Kapoor (2018–2023)

The Fraud: Mechanism and Execution

The Yes Bank-Rana Kapoor case is analytically rich because it combines three distinct fraud typologies , governance concealment, related-party transaction fraud, and capital market misselling , and because it implicates the regulatory boundary between SEBI's capital market jurisdiction and RBI's banking supervision mandate in ways that created mutual regulatory blind spots enabling the overall scheme to persist for years.

Rana Kapoor co-founded Yes Bank in 2004 and served as its Managing Director and CEO until January 2019, when the RBI declined to extend his tenure following its own assessment of governance concerns. During the period from approximately 2016 to 2018, Yes Bank's disclosed loan book presented an NPL (Non-Performing Loan) ratio that the RBI's own Asset Quality Review subsequently found to be materially understated , Yes Bank was evergreening stressed loans by extending new credit to borrowers who were using it to service interest on existing facilities, deferring NPA classification while accumulating real credit risk.

The Rana Kapoor personal enrichment mechanism was the following: certain large Yes Bank borrowers who were experiencing financial stress , including DHFL (Dewan Housing Finance Corporation Limited) and IL&FS entities , received credit facilities from Yes Bank. In exchange, companies controlled by Rana Kapoor, his family members, or connected entities received economic benefits from these borrowers. DOIT Urban Ventures, a Kapoor family company, received a ₹600 crore unsecured loan from DHFL, allegedly structured as a quid pro quo for Yes Bank's continued lending to DHFL despite its deteriorating financial condition. DoIT's receipt of DHFL funds , while Yes Bank simultaneously extended ₹3,983 crore in credit to DHFL , constituted a related-party transaction of the most direct kind: the MD was personally benefiting from the bank's lending decisions.

The guarantee concealment dimension involved Kapoor issuing personal guarantees on behalf of Morgan Credits , a private company connected to his family , worth approximately ₹950 crore, in transactions that involved Yes Bank borrowers or entities connected to them. These guarantees were never disclosed to Yes Bank's board, its shareholders, or to SEBI as required under LODR Regulations. They represented a direct financial interest of the MD in transactions affecting Yes Bank's credit decisions , the precise scenario that LODR's related-party disclosure requirements are designed to capture.

The AT-1 bond misselling dimension affected a different class of victims , retail investors. Yes

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Bank issued Additional Tier-1 (AT-1) bonds, which are Basel III-compliant regulatory capital instruments with a critical structural feature: they can be written down to zero or converted to equity at the discretion of the regulator if the bank reaches a point of non-viability. This feature makes AT-1 bonds substantially different from ordinary fixed-income securities and appropriate only for sophisticated investors who understand the contingent write-down risk. Yes Bank's relationship managers allegedly sold these instruments to retail fixed deposit customers as 'FD-like' instruments with a slightly higher yield , misrepresenting their fundamental risk characteristics to investors entirely unequipped to assess the write-down risk. When the RBI-orchestrated Yes Bank reconstruction in March 2020 wrote down ₹8,415 crore of AT-1 bonds to zero as part of the rescue package, approximately 1,300 retail investors who had purchased the bonds faced total loss of their invested capital.

SEBI Framework Limitations

The Yes Bank case exposed the limitations of SEBI's disclosure enforcement framework at multiple levels. The LODR Regulations required disclosure of material related-party transactions and events that could affect the listed entity's securities. Rana Kapoor's personal guarantee issuance , directly connecting him financially to Yes Bank borrowers and creating an undisclosed conflict of interest in the bank's lending decisions , was precisely the kind of material related-party transaction that LODR intended to capture. Yet it remained undisclosed for years. The enforcement failure here was not one of inadequate regulation but of detection: SEBI had no mechanism to discover that a guarantee had been issued other than voluntary compliance by the managing director himself or a whistleblower complaint , neither of which materialised until after the crisis had broken.

The compliance architecture problem is structural. Yes Bank's Compliance Officer was an employee of Yes Bank, reporting ultimately to Rana Kapoor. The expectation that this Compliance Officer would identify, document, and publicly disclose her chairman's personal financial arrangements with the bank's borrowers is architecturally unrealistic , the employment relationship created an insurmountable conflict of interest in precisely the disclosure scenario where independence was most needed.

The SEBI-RBI coordination failure was equally consequential. RBI's Asset Quality Review of Yes Bank in 2017-18 revealed massive NPA understatement , information that was directly relevant to the capital market disclosure obligations of a listed bank. If RBI had shared its AQR findings with SEBI under a formal information-sharing protocol, SEBI could have initiated a disclosure investigation and compelled Yes Bank to disclose the true state of its loan

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book to capital market investors years before the moratorium. No such protocol existed.

The SAT deterrence failure , discussed in detail in Chapter 4 , is most concretely illustrated by the Yes Bank enforcement outcome. SEBI's ₹3 crore penalty was stayed on deposit of

₹50 lakh pending a multi-year SAT appeal. The message transmitted to the market , that a managing director who concealed material related-party transactions while heading a major listed bank faces an effective immediate financial consequence of ₹50 lakh , is the antithesis of meaningful deterrence.

The AT-1 bond misselling sits at an uncomfortable regulatory boundary. SEBI regulates public issuances of securities and mandates disclosure norms for listed instruments; RBI regulates bank capital instruments including AT-1 bonds under its prudential framework. The misselling of AT-1 bonds to retail investors was primarily a sales conduct violation , falling within the jurisdiction of the banking regulator as a consumer protection matter , yet RBI's supervisory framework was not designed to scrutinise individual retail sales interactions at the relationship manager level. SEBI's investor protection mandate was directly implicated, but SEBI's enforcement powers over bank capital instrument issuances are circumscribed by RBI's primary jurisdiction over bank regulatory capital.

US SEC and EU ESMA Comparative Analysis

Under US securities law, Rana Kapoor's undisclosed guarantee issuances would have constituted a violation of Item 404 of SEC Regulation S-K, which requires disclosure of all transactions in which a director or executive officer has a direct or indirect material interest, above a $120,000 threshold. This disclosure obligation is enforced not merely through SEC investigation but through private plaintiff litigation , any Yes Bank shareholder who purchased shares while the guarantee was undisclosed could bring a securities fraud class action under Rule 10b-5, creating a private enforcement mechanism entirely independent of the regulatory enforcement pipeline. India has no equivalent private securities fraud class action mechanism.

The EU's MiFID II product governance and suitability requirements directly address the AT-1 misselling scenario. Under MiFID II, AT-1 bonds must be classified as complex products; investment firms selling them to retail clients must conduct a suitability assessment and demonstrate that the product is appropriate for the specific client's knowledge, experience, financial situation, and investment objectives. Selling an AT-1 bond as an 'FD

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equivalent' to a retail fixed deposit customer would constitute a per se suitability violation under MiFID II, trigerring immediate regulator action and potential customer redress. SEBI's suitability framework for securities distribution is significantly less granular , particularly for products that straddle the capital market and banking regulatory boundary.

Case IV: Adani Group Controversy (2023)

The Fraud: Mechanism and Execution

The Adani Group controversy , triggered by Hindenburg Research's January 2023 short-seller report , represents the most high-profile and most legally contested of the five cases, with SEBI's investigation ongoing, multiple Supreme Court interventions, and the case's ultimate factual resolution still pending at the time of this dissertation's preparation. The analytical value of the case for this dissertation lies not in adjudicating Hindenburg's specific allegations , which Adani has comprehensively denied , but in the structural regulatory issues that the controversy has unambiguously revealed, regardless of the ultimate merits.

Hindenburg's central allegations involved two distinct but related mechanisms. The first was that offshore entities incorporated in Mauritius, Cyprus, and Cayman Islands , which held significant Adani group shares through the FPI route , were beneficially owned or controlled by persons connected to the Adani promoter group. If true, this would mean that shares nominally counted as publicly held 'free float' were in economic substance promoter-controlled shares, and the Adani group's actual public float was below the

minimum 25% required by SEBI's minimum public shareholding (MPS) norms. The allegation was that the promoter's true economic interest in Adani group companies was not the disclosed approximately 72-75% but potentially as high as 90%+ when the offshore vehicles were attributed to the promoter group.

The second mechanism alleged was stock price manipulation through these offshore vehicles , that the promoter-connected FPIs engaged in trading patterns designed to support Adani group stock prices rather than investment-return-seeking behaviour. This allegation, if true, would constitute both a disclosure violation (the FPIs were not disclosing promoter connection) and a market manipulation violation (coordinated buying to support prices).

The structural vehicle for both mechanisms was the Participatory Note (P-Note). An FPI registered with SEBI can issue P-Notes , derivative instruments referencing Indian

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securities , to end investors who are not directly registered with Indian regulators. The end investor in a P-Note has economic exposure to Indian securities (including dividends, capital appreciation, and voting economics in some structures) but appears in Indian regulatory records only as an unnamed beneficiary of an FPI's position. SEBI knows that FPI X holds 5 lakh shares of Adani Enterprises; SEBI does not know, from its own records, who the ultimate beneficiary of those shares is.

The regulatory challenge this created was precise: Hindenburg alleged that the UBOs of certain Mauritius FPIs holding Adani shares were persons connected to the Adani family. SEBI's investigation, to verify or refute this, needed to obtain beneficial ownership information from Mauritius's Financial Services Commission , a treaty-based, inter-regulator request process. SEBI's August 2024 affidavit to the Supreme Court

acknowledged that its investigation had issued 24 show cause notices and that verification of offshore entity beneficial ownership had been a constraint on investigation completion. Two years after the Hindenburg report, SEBI's investigation remained incomplete.

SEBI Framework Limitations

The Adani case is the sharpest illustration of what this dissertation terms 'disclosure threshold arbitrage.' SEBI's FPI regulations, as they existed at the time, required granular beneficial ownership disclosure only when an FPI's holding in a single Indian company

exceeded 50% of the FPI's corpus, or when the FPI held more than 10% of the equity of the listed company. Below these thresholds, FPIs were required to provide only broad category-level information. The 1% aggregate shareholding threshold for triggering enhanced FPI disclosure , applicable when the FPI is identified as part of a 'high risk' category , left substantial room for calibrated position-taking below the threshold.

The SEBI investigation timeline problem , two-plus years and still pending , is directly attributable to the absence of a pre-existing beneficial ownership database and the

dependence on MLAT and inter-regulator request processes for offshore verification. If India had a Beneficial Ownership Intelligence Database that required all FPIs to register

their UBOs down to natural persons as a condition of initial SEBI registration, the beneficial ownership question in the Adani investigation would have been answerable from existing records within days , not months or years of treaty-based investigation. The entire investigation delay, to a significant extent, represents the cost of not having invested in a pre-registration beneficial ownership framework.

The P-Note opacity problem deserves specific treatment. SEBI has progressively tightened P-

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Note disclosure requirements through circulars in 2017 and subsequent amendments, requiring FPIs to report their P-Note issuances with beneficial ownership information quarterly. However, the quarterly reporting frequency, combined with the absence of real-time verification capability, means that P-Note beneficial ownership data is always historical. An FPI can issue P-Notes to a beneficial owner today, trade on the market tomorrow, and SEBI will learn of the beneficial owner's identity only in the quarterly report filed weeks later.

US SEC and EU ESMA Comparative Analysis

The US framework addresses the offshore beneficial ownership problem through two complementary mechanisms. First, the SEC's Section 13D/13G regime requires disclosure of 5%+ beneficial ownership regardless of whether the holding is through direct shares, P-Note equivalents, or offshore structures , and the 'group' concept under Section 13(d)(3) means that multiple offshore vehicles with coordinated economic interests are treated as a single beneficial owner for threshold calculation. Second, the Corporate Transparency Act (CTA) of 2020, administered by FinCEN, requires all US-formed or US-registered entities to disclose their UBOs to a centrally maintained database , and non-US entities that are registered to do business in the US or hold US securities face analogous disclosure obligations. The SEC has access to FinCEN's beneficial ownership database, enabling cross-reference verification without the MLAT process that constrains SEBI.

The EU's approach is equally instructive: ESMA's UBO registers under the Anti-Money Laundering Directive require disclosure down to natural persons holding more than 25% of any EU-incorporated entity. For market access purposes, non-EU entities seeking to hold EU securities through EU-regulated investment structures must comply with equivalent beneficial ownership disclosure as a condition of access. India's GIFT City framework is progressively incorporating international financial centre norms , but SEBI's onshore FPI framework has not yet adopted equivalent access-conditional UBO disclosure.

Case V: Jane Street Market Manipulation (2025)

The Fraud: Mechanism and Execution

The Jane Street case represents the most technically sophisticated of the five cases and the most consequential for understanding the emerging frontier of algorithmic market manipulation in India's derivatives markets. Jane Street Group , a US-headquartered global quantitative trading firm with operations in Indian markets , was subjected to SEBI raids in June 2025, with over 100 computers seized from more than 80 locations across major

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Indian financial centres. SEBI issued an interim ex-parte order banning Jane Street from Indian markets pending investigation, alleging market manipulation in the Bank Nifty index options segment.

Jane Street is among the world's largest market makers in exchange-traded options , its business model globally involves providing liquidity across equity, fixed income, and currency derivatives, profiting from bid-ask spreads and sophisticated arbitrage strategies.

Its Indian operations focused significantly on Bank Nifty index options , the world's most actively traded single-contract options series by volume, with daily notional turnover exceeding hundreds of thousands of crores of rupees. The Indian retail participation in Bank Nifty options is exceptionally high , a structural feature of Indian derivatives markets that distinguishes them from more institutionally dominated derivatives markets globally, and that creates specific market microstructure vulnerabilities.

The alleged manipulation mechanism , reconstructed from SEBI's interim order and subsequent reporting , involved Jane Street accumulating large directional or gamma-exposed positions in Bank Nifty options, then systematically influencing the Bank Nifty index level at critical calculation points through coordinated cash market activity in the constituent banking stocks. The Bank Nifty index is calculated in real-time as a weighted average of twelve banking sector stocks. Large, coordinated buying or selling of these constituent stocks near market close , when options settlement prices are determined , can influence the index level in ways that benefit a large options position sensitive to the specific index level.

The critical analytical point is that each individual constituent stock trade executed by Jane Street may have been a bona fide market-clearing transaction at prevailing prices. The manipulation, if SEBI's allegations are substantiated, resided not in any individual fraudulent trade but in the strategic design of the trading programme , the deliberate coordination between derivatives positioning and cash market activity to engineer the index level toward outcomes beneficial to the derivatives book. This is a fundamentally

different evidentiary challenge from circular trading: there is no smoking-gun transaction; the case must be built by reconstructing the entire strategy across two market segments over extended time periods.

The retail investor harm dimension is significant. Indian retail investors are among the world's most active derivatives traders , SEBI's own data shows that over 90% of individual traders in the Futures and Options segment incur losses. When a sophisticated algorithmic operator

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systematically benefits from index levels that it has itself influenced, the transfer of wealth from retail options buyers and sellers to the manipulating entity is structural and ongoing , not a single fraud event but a continuous extraction embedded in market
microstructure.

SEBI Framework Limitations

The Jane Street case exposed SEBI's most significant and least easily remediated limitation: the absence of a cross-product, cross-segment surveillance capability
adequate for detecting algorithmic manipulation strategies that are designed to be invisible at the individual transaction level but are economically meaningful at the strategy level.

SEBI's IMSS and exchange surveillance systems were architecturally designed in an era of cash equity market surveillance. Their extension to derivatives markets has been progressive but has not incorporated the cross-segment correlation analysis that algorithmic manipulation in derivatives markets requires. Detecting that Jane Street's cash market trading in Bank Nifty constituents was systematically correlated with the settlement-beneficial movement of Bank Nifty options at positions Jane Street held
required: first, access to Jane Street's complete derivatives position book; second, correlation of that position book with every cash market order Jane Street placed in the constituent stocks; and third, statistical analysis demonstrating that the correlation exceeded what would be expected from a non-manipulative market-making or arbitrage strategy. This analysis required data and analytical capabilities that SEBI assembled only through physical raids , seizing Jane Street's own computer systems to reconstruct the strategy.

The contrast with a world in which MiFID II-equivalent algorithm tagging and transaction reporting existed is stark. Under MiFID II, every order Jane Street submitted to any EU trading venue would have been tagged with the strategy identifier generating it, and full order-level data would have been reported to an EU trade repository accessible to ESMA
and national competent authorities in near-real-time. Reconstructing Jane Street's strategy would not have required physical raids , it would have required a database query on

already-available transaction records. The investigative timeline would be weeks rather than the multi-year process that physical-seizure-based investigation typically requires.

The PFUTP Regulations' definition of market manipulation, while broad, was designed primarily with transaction-based manipulation in mind , wash trades, spoofing, layering , rather than strategy-level manipulation where the manipulative intent is proven by the statistical relationship between positions across market segments. SEBI's interim order in the Jane Street

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case necessarily relied on inference from trading patterns , a legally more complex evidentiary framework than the direct documentation of fraudulent transactions that traditional manipulation cases involve. The legal framework for algorithmic manipulation prosecution needed strengthening simultaneously with the surveillance architecture needed to detect it.

The high-frequency nature of Jane Street's strategies also overwhelmed SEBI's investigative processing capacity. Seizing 100+ computers from 80+ locations is itself an indication that SEBI lacked the electronic data access infrastructure to obtain the relevant records through normal regulatory demand , a power that the SEC exercises routinely through its Electronic Data Gathering and Analysis requirements and the CAT's continuous data capture.

US SEC and EU ESMA Comparative Analysis

The SEC's approach to cross-product manipulation involving options and their underlying securities is developed through a body of enforcement actions , most notably actions against traders using options positions to generate economic incentives for cash market manipulation designed to benefit those positions. The SEC's Regulation SCI (Systems Compliance and Integrity) and market maker examination programmes provide continuous regulatory insight into large derivatives market makers' trading patterns , SEBI has no equivalent examination programme for algorithmic trading firms.

The EU's ESMA framework under MAR Article 12 explicitly defines market manipulation to include conduct that 'secures the price of a financial instrument at an abnormal or artificial level, language broad enough to encompass index-influencing strategies. Crucially, MAR Article 16 imposes a mandatory suspicious transaction and order reporting (STOR) obligation on investment firms, which would have required any firm observing Jane Street's market activity , including brokers executing its orders , to file a STOR report with the relevant national competent authority upon forming a reasonable suspicion. This distributed detection mechanism , deputising market participants as regulatory sensors , means that the detection burden does not fall exclusively on SEBI's own surveillance systems.

Cross-Case Synthesis: The Common Architecture of Regulatory Arbitrage

Examining the five cases together reveals that the specific mechanisms differ , circular trading networks, subsidiary opacity, governance concealment, offshore beneficial ownership, algorithmic manipulation , but the structural regulatory vulnerabilities exploited are consistent across all five. Each case exploited at least three of the five systemic

limitations identified in Chapter 4: surveillance architecture blind spots, disclosure

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threshold manipulation, inter-agency coordination gaps, enforcement timeline latency, and appellate deterrence erosion.

The temporal pattern is equally revealing. The Ketan Parekh scam exploited entity aggregation blind spots and cooperative bank regulatory gaps in 1999-2001. IL&FS exploited subsidiary opacity and multi-regulator jurisdictional fragmentation from 2014-2018. Yes Bank exploited compliance architecture conflicts of interest and SEBI-RBI information silos from 2016-2019. Adani exploited offshore disclosure threshold calibration and MLAT-dependent beneficial ownership verification from 2023 onwards.

Jane Street exploited cross-product algorithmic surveillance gaps in 2025. Each successive case demonstrates adaptation , fraudsters learning from prior enforcement actions and designing schemes around the specific vulnerabilities that remained unaddressed after each prior reform cycle. This is regulatory arbitrage as an evolutionary phenomenon: the schemes escalate in technical complexity as the simpler exploitation vectors are progressively closed.

The comparative analysis with the US SEC and EU ESMA frameworks consistently demonstrates that the regulatory gaps exploited in India are not gaps in well-designed regulatory systems , they are gaps in regulatory design that the US and EU closed years or decades earlier, motivated by their own analogous enforcement failures. The SEC's CAT was motivated by the 2010 Flash Crash, which revealed the same surveillance fragmentation problem that Ketan Parekh exploited. ESMA's beneficial ownership frameworks were motivated by offshore tax evasion and money laundering cases directly analogous to the Adani offshore structure allegations. MiFID II's algorithm tagging requirement was motivated by high-frequency trading surveillance failures directly analogous to the Jane Street detection problem.

India is not confronting novel challenges. It is confronting, with a decade or more of delay, the same surveillance and regulatory architecture failures that its peer regulators have already addressed. The reform agenda proposed in Chapter 6 is accordingly not speculative , it is the adaptation and contextualisation of proven solutions to India's specific institutional, statutory, and political context. The principal challenge is not

designing the reforms: it is building the institutional will and political consensus to implement them before the next major regulatory arbitrage failure materialises.

CHAPTER 6

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Reform Architecture for Indian Securities Regulation: Legislative Interventions, Regulatory Redesign, and Fraud Prevention Mechanisms

Introduction: The Reform Imperative

The preceding chapters have constructed a detailed anatomy of regulatory arbitrage in Indian securities markets , the deliberate exploitation of known surveillance blind spots, disclosure threshold loopholes, inter-agency coordination failures, and appellate deterrence erosion by sophisticated multi-entity fraudsters. The five case studies examined , Ketan Parekh, IL&FS, Yes Bank-Rana Kapoor, Jane Street, and Adani Group , are not historical curiosities. They are the visible manifestations of a systemic architectural problem that, absent fundamental reform, will continue to produce new iterations of the same fraud patterns with escalating sophistication and market impact.

This chapter synthesises the diagnostic findings of Chapters 3, 4, and 5 into a comprehensive reform architecture. The recommendations proceed from a foundational premise: incremental regulatory amendments within the existing framework have been SEBI's dominant reform modality for three decades, and the persistence of sophisticated regulatory arbitrage despite thirty years of post-scandal tightening demonstrates that incremental reform is structurally insufficient. What India's securities regulatory landscape requires is architectural reform , a fundamental redesign of surveillance infrastructure, disclosure philosophy, inter-agency coordination, enforcement pipeline, and appellate structure , rather than further patching of a framework whose foundational assumptions are misaligned with the complexity of contemporary financial markets.

The chapter is organised around six reform pillars: surveillance and technology modernisation; disclosure and beneficial ownership transformation; inter-agency coordination architecture; enforcement pipeline acceleration and penalty redesign; appellate structure reform; and investor protection and whistleblower empowerment. Each pillar integrates legislative recommendations (requiring Parliamentary action), regulatory **recommendations (implementable by SEBI through its existing rule-making powers), and institutional recommendations (requiring administrative restructuring). The chapter also**

addresses the most common fraud typologies identified across India's market history and proposes mechanism-specific prevention frameworks for each.

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Understanding How Common Frauds Operate: A Mechanistic Analysis

Before prescribing prevention, it is analytically necessary to understand, with precision, how each major fraud typology operates , because effective prevention must target the mechanism, not merely the outcome. Indian securities fraud, across its historical range, resolves into five dominant mechanistic categories.

Circular Trading and Coordinated Artificial Volume

The oldest and most persistent fraud typology in Indian markets is circular trading , the coordinated buying and selling of the same securities among a network of related entities to create artificial volume, signal false market activity, and inflate prices before distribution to unsuspecting retail investors. The Ketan Parekh scheme, while the most celebrated example, was a sophisticated elaboration of circular trading patterns that SEBI had documented since the Harshad Mehta era.

The mechanism operates in three phases. In the accumulation phase, the operator quietly builds a position in a low-liquidity stock , often a small or mid-cap company , using a network of entities that maintain the fiction of independence. In the inflation phase, coordinated buy orders among related entities create artificial trading volume and price momentum. Because exchange surveillance systems detect anomalous price movements relative to prior trading patterns, the inflation is typically calibrated to stay below alert thresholds , a 3-5% daily appreciation that compounds over weeks into dramatic absolute gains. The critical insight is that the manipulation is not dramatic on any given day; it is systematic over time. In the distribution phase, the operator sells accumulated shares into the artificial demand created by retail investors attracted by the price momentum , leaving them holding overvalued securities that collapse when the artificial support is withdrawn.

Prevention requires attacking all three phases simultaneously. Accumulation-phase prevention requires entity-level beneficial ownership aggregation: if SEBI's surveillance systems could attribute all trading by entities with common beneficial ownership to a single 'economic person,' threshold-based alerts would trigger far earlier. Inflation-phase prevention requires cross-entity, not just single-scrip, surveillance: monitoring whether the same beneficial owner's vehicles are on opposite sides of trades. Distribution-phase prevention requires real-time tracking of promoter and large holder selling into retail buying , a pattern that is statistically detectable with modern market microstructure analysis.

Related-Party Transaction Diversion and Subsidiary Opacity

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The IL&FS model represents a second fraud typology , the use of subsidiary structures and related-party transactions to conceal financial stress, divert funds, and misrepresent the financial position of a listed entity to its investors and creditors. This typology has antecedents in the Satyam fraud and has recurred in various forms across Indian corporate history.

The mechanism exploits the gap between consolidated financial reporting (which shows aggregate group performance) and the actual cash flow dynamics at the operating subsidiary level. A holding company can maintain the appearance of solvency at the consolidated level while individual subsidiaries are experiencing severe liquidity stress , provided that inter-company loans, guarantees, and related-party receivables are structured to obscure the subsidiary-level deterioration. In IL&FS, the 340+ subsidiary structure meant that the commercial paper market was effectively funding infrastructure assets through a chain of intra-group transactions that collectively constituted a liquidity transformation business , but that was invisible as such to any single regulator examining only its portion of the structure.

The prevention framework for this typology is fundamentally about consolidated group transparency rather than entity-level disclosure. If regulators could observe the full cash flow network of an IL&FS-type group , including intra-group funding flows, maturity profiles, and concentration of refinancing risk , the systemic liquidity risk would be detectable before crisis. This requires regulatory data access at the group level, not merely at the listed holding company level.

Disclosure-Evasion Fraud: Governance and Guarantee Concealment

The Yes Bank pattern represents a third typology: the deliberate concealment from boards, shareholders, and regulators of transactions that, if disclosed, would reveal conflicts of interest, undisclosed related-party relationships, or deteriorating financial conditions.

Rana Kapoor's issuance of personal guarantees to entities connected to Yes Bank's stressed borrowers , without board disclosure , exemplifies a fraud that operates not through market manipulation but through governance opacity.

This fraud typology is enabled by a specific vulnerability: the compliance infrastructure of listed companies is managed by employees of those companies, creating a structural conflict of interest in disclosure compliance. The Compliance Officer who is responsible for ensuring LODR disclosure is an employee of the company whose management is potentially concealing information. The Board, which is supposed to exercise oversight, may itself be complicit or inadequately informed. Statutory auditors have independent

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reporting obligations, but the auditor's commercial relationship with the auditee creates incentive structures adverse to aggressive disclosure enforcement.

Prevention here requires independence architecture: compliance functions with reporting lines genuinely independent of management, audit committee compositions that are not captured by promoter influence, and whistle-blower channels with real external accountability. Critically, it requires regulators to have proactive access to governance process data , not merely reactive review of what companies choose to disclose.

Offshore Structure and Beneficial Ownership Concealment

The Adani controversy and the Ketan Parekh offshore routing represent a fourth typology: the use of multi-jurisdictional corporate structures to obscure the identity of ultimate beneficial owners, enabling promoters to hold economic interests that violate regulatory norms (minimum public shareholding, FPI investment limits) without triggering disclosure requirements.

The mechanism relies on the gap between legal and economic ownership. A Mauritius-incorporated fund that is legally owned by a Cyprus holding company, which is in turn beneficially owned by an Indian resident, appears from SEBI's vantage as a foreign institutional investor , regulated by SEBI's FPI framework at the point of its Indian market participation but opaque as to its ultimate beneficial owner. Participatory Notes (P-Notes) add another layer of opacity: an FPI can issue P-Notes to end investors who have no direct relationship with Indian regulators, and whose beneficial ownership is known only to the issuing FPI.

The fraud prevention framework for this typology requires piercing the offshore veil as a regulatory baseline rather than an investigative exception. This means requiring beneficial ownership disclosure down to natural persons as a condition of market access , not as a post-detection investigation step.

Algorithmic and Derivatives Market Manipulation

The Jane Street matter represents the emerging frontier of fraud , the use of sophisticated algorithmic strategies to exploit the structural mechanics of index calculation, options pricing, and market microstructure in ways that transfer wealth from retail participants to the operator. This typology is qualitatively different from its predecessors because the manipulative 'intent' is embedded in mathematical strategy design rather than in specific fraudulent transactions.

The mechanism , as alleged , involves accumulating large derivatives positions sensitive to index levels, then systematically influencing the index level through cash market activity at

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key calculation points (particularly near market close), and profiting from the derivatives move. Each individual trade in the cash market may be a bona fide order at prevailing prices. The manipulation is in the strategic ensemble of trades, not in any individual fraudulent transaction. This makes detection fundamentally different from circular trading: there is no single 'smoking gun' transaction; the fraud is reconstructed from the pattern of a complete trading strategy.

Prevention requires a surveillance architecture that can analyse strategies rather than individual transactions , cross-product, cross-segment analysis that can reconstruct the relationship between derivatives positioning and cash market activity in real time.

Pillar I: Surveillance and Technology Modernisation

Legislative Recommendation: Mandating a Consolidated Audit Trail

Recommendation: Parliament should amend the Securities Contracts (Regulation) Act, 1956 to require the creation of a National Market Audit Trail (NMAT) , a centralised repository, modelled on the US Consolidated Audit Trail (CAT), that captures every order, modification, cancellation, and execution across all SEBI-regulated trading venues, in real-time, with full entity attribution including beneficial ownership identifiers.

The NMAT should be operated by an independent body , potentially a SEBI subsidiary or a reconstituted market infrastructure institution , with mandatory data submission obligations on all trading members, clearing members, and depositories. Data retention should extend to ten years. SEBI should have unrestricted query access to NMAT data for surveillance and investigative purposes, while market participants' access to their own data should be appropriately governed.

The critical design requirement is entity consolidation: every order submitted to any Indian trading venue should be attributed to the ultimate beneficial owner (UBO) of the trading account, not merely the immediate account holder. This collapses the multi-entity circular trading mechanism at source , when SEBI can see that entities A, B, C, D, and E are all submitting orders attributable to the same UBO, coordinated trading patterns become instantly visible.

Regulatory Recommendation: Pending legislative action, SEBI should immediately exercise its powers under Section 11 of the SEBI Act to mandate standardised, real-time order-level reporting by all trading members to a SEBI-controlled data repository. Current exchange-level

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audit trails should be standardised to a common format and made

accessible to SEBI's surveillance systems within minutes of order submission , not on a next-day batch basis.

Regulatory Recommendation: Algorithm Tagging and Strategy Registration

SEBI should issue a fresh circular under its PFUTP Regulations and algorithmic trading framework requiring algorithmic trading firms to register every distinct trading strategy with SEBI, assign a unique strategy identifier to all orders generated by that strategy, and include the strategy identifier in the order message transmitted to the exchange. This creates an algorithmic audit trail analogous to MiFID II's algorithm identification requirements.

Strategy registration should require disclosure of: the strategy's objective; its primary instruments and market segments; its typical order frequency and size profile; and any relationships between its equity and derivatives components. This registration requirement does not constitute prior approval , it is a disclosure mechanism , but it creates an information base from which SEBI can correlate cross-product trading patterns with specific algorithmic strategies and detect manipulation at the strategy level rather than the transaction level.

Institutional Recommendation: Establishment of a Market Intelligence and Analytics Division

SEBI should create a Market Intelligence and Analytics Division (MIAD) , a dedicated internal unit staffed by quantitative analysts, data scientists, financial engineers, and market microstructure specialists , with the specific mandate of building, deploying, and maintaining AI/ML-based surveillance models. The MIAD should be exempt from standard civil service pay scales and empowered to recruit at market-competitive compensation , recognising that the expertise required is available in the private sector at compensation levels that government pay bands cannot match.

The MIAD's surveillance models should cover: entity network analysis (identifying common beneficial ownership across market participants through trading pattern correlation); cross-product manipulation detection (correlating derivatives positioning with cash market activity); intra-day marking patterns (detecting systematic end-of-day price influence attempts); and sentiment-price divergence analysis (detecting coordinated social media pump-and-dump schemes). Model outputs should generate automated alerts with associated evidence packages that can be escalated directly to enforcement without the current manual review bottleneck.

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Pillar II: Disclosure and Beneficial Ownership Transformation

Legislative Recommendation: The Beneficial Ownership Disclosure Act

Recommendation: Parliament should enact a standalone Beneficial Ownership Disclosure Act that creates a mandatory, real-time, publicly accessible register of ultimate beneficial owners for all entities holding Indian securities above a defined threshold , whether through domestic or offshore structures.

The core elements of this legislation should include: (a) a definition of 'ultimate beneficial owner' that identifies the natural person who ultimately owns or controls the economic interest, piercing all intermediate corporate layers regardless of jurisdiction; (b) a mandatory disclosure threshold of 1% of any listed company's equity, triggered by aggregate holdings across all vehicles attributable to the same UBO , not by any individual vehicle's holding; (c) a 'group acting in concert' definition broad enough to capture economic concert (coordinated trading, common investment mandate, shared beneficial ownership) rather than merely contractual concert; (d) automatic disclosure of any P-Note issuance with identification of the end investor's beneficial owner; and (e) extraterritorial jurisdiction, with market access to Indian exchanges conditioned on compliance.

The threshold reduction from the current FPI-level disclosure norms to a 1% UBO-aggregate threshold would directly address the Adani-type offshore structure. If every Mauritius fund holding Adani shares were required to disclose its UBO, and if those UBOs were aggregated across all vehicles for threshold calculation, any promoter-linked concentration above 1% would trigger disclosure , regardless of how many intermediate structures were interposed.

Regulatory Recommendation: Related-Party Transaction Overhaul

SEBI should fundamentally redesign the related-party transaction disclosure framework under LODR Regulations to extend obligations to material unlisted subsidiaries.

Specifically:

The materiality threshold for RPT disclosure should be reduced to 5% of consolidated net worth or 2.5% of consolidated turnover, whichever is lower , with no carve-outs for transactions below ₹1 crore. All RPTs above the threshold at any group entity (listed holding company or material subsidiary, defined as contributing more than 10% of consolidated revenue or assets) should be disclosed to the stock exchange of the listed parent on a real-time basis.

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SEBI should introduce a mandatory quarterly 'Group Cash Flow Statement' for listed companies with more than 10 material subsidiaries, requiring consolidated disclosure of all intra-group fund flows, inter-company loan balances, guarantee exposures, and maturity profiles. This statement should be prepared by the statutory auditor , not

management , and filed directly with SEBI's surveillance system rather than merely included in the annual report.

Regulatory Recommendation: Insider Trading Framework Strengthening

The PIT Regulations should be amended to: (1) require pre-clearance for all trades by designated persons above a de minimis threshold of ₹2 lakh, not merely 'trades that could be based on UPSI'; (2) transfer pre-clearance administration from the company's compliance officer to an independent third-party compliance administrator (a SEBI-registered entity with independence from the listed company); and (3) mandate real-time reporting of all designated person trades to SEBI's surveillance system with a 30-minute reporting window.

The 'trading plan' mechanism under PIT Regulations , allowing designated persons to schedule future trades with advance disclosure , should be reformed to require plans to be lodged with SEBI directly (not merely with the company's compliance officer), with SEBI verification before the plan becomes operative.

Pillar III: Inter-Agency Coordination Architecture

Legislative Recommendation: The Financial Market Intelligence Authority

Recommendation: Parliament should create a Financial Market Intelligence Authority (FMIA) , a statutory inter-agency body with independent legal personality, operational budget, and data access powers , to serve as India's equivalent of the US FinCEN, operating as the intelligence hub for financial market crime across all regulatory boundaries.

The FMIA should have: (a) mandatory membership of SEBI, RBI, IRDAI, MCA, ED, FIU-IND, CBI, and the Income Tax Department; (b) a centrally funded budget independent of any member agency; (c) a statutory right to access data from all member agency systems, including SEBI's trading records, RBI's bank transaction data, MCA's company registry, and ED's financial intelligence database; (d) powers to conduct joint investigations with concurrent authority across all member agencies' mandates; and (e) a statutory obligation to share actionable intelligence with member agencies within 48 hours of assessment.

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The FMIA should maintain a real-time Beneficial Ownership Intelligence Database that aggregates ownership records from SEBI's FPI registry, RBI's FEMA records, MCA's beneficial ownership declarations under the Companies Act, and intelligence from foreign counterparts through IOSCO's multilateral MOU. This database should be the single source of truth for cross-agency beneficial ownership queries , eliminating the current situation

where each agency separately investigates the same offshore structure through different investigative channels.

Regulatory Recommendation: SEBI-RBI Joint Investigation Protocol

SEBI and RBI should execute a comprehensive Joint Investigation Protocol , modelled on the SEC-Federal Reserve MOU , that establishes: (a) a mandatory joint case assessment within 30 days of any fraud allegation involving both a listed company and a regulated bank;

(b) a shared evidence repository for joint investigations with agreed access protocols; (c) joint investigation teams with designated leads from each agency; (d) a unified enforcement timeline ensuring that SEBI and RBI enforcement actions in related matters are coordinated rather than sequential; and (e) a joint media communication policy for major enforcement actions to prevent regulatory message fragmentation.

Legislative Recommendation: Expedited MLAT Procedure for Securities Fraud

Parliament should amend India's bilateral treaty implementation framework to create an expedited Mutual Legal Assistance procedure specifically for securities market investigations , distinct from the general criminal MLAT channel. This expedited procedure should: target a 90-day response timeline from foreign jurisdictions (compared to current multi-year MLAT delays); be designated as a civil regulatory assistance channel (eliminating the requirement for a pending criminal investigation); and be operationalised through direct SEBI-to-foreign-regulator communication under the IOSCO MMoU, bypassing the Ministry of External Affairs routing that currently adds months to offshore investigation timelines.

Pillar IV: Enforcement Pipeline Acceleration and Penalty Redesign

Legislative Recommendation: Enforcement Pipeline Reform Act

Recommendation: Parliament should enact an Enforcement Pipeline Reform Act amending the SEBI Act, 1992 to structurally compress investigation-to-enforcement timelines and substantially enhance the deterrence calculus.

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Investigation timelines: A statutory maximum investigation period of 18 months from the date of formal investigation order to the issuance of a show cause notice should be imposed, with a 6-month extension available only upon written approval by the SEBI Board. This does not limit SEBI's ability to reopen matters on new evidence , it disciplines the primary investigation timeline.

Disgorgement as mandatory remedy: The current discretionary disgorgement provision under Section 15JB of the SEBI Act should be made mandatory for all violations involving illicit profits above ₹10 lakh, with the burden of proof for quantum placed on the accused rather than SEBI. The disgorgement quantum should include not merely direct trading profits but all downstream economic benefits , advisory fees, management fees, carried interest, and asset price appreciation in entities controlled by the accused , attributable to the fraud.

Penalty enhancement: Maximum civil penalties under the SEBI Act should be enhanced from ₹25 crore to ₹500 crore per violation, or five times the illicit gain, whichever is higher , aligning India's penalty framework with the quantum of modern market frauds. A minimum penalty floor should be established: for violations involving illicit profits above ₹1 crore, the minimum penalty should be 100% of illicit profits, irrespective of adjudicating officer discretion.

Asset attachment at investigation stage: SEBI should be empowered to seek provisional asset attachment orders from a designated Special Court at the investigation stage , not merely post-adjudication , upon demonstrating a prima facie case and risk of asset dissipation. This eliminates the current window during which accused entities can transfer assets to offshore vehicles during the 3-7 year investigation and adjudication process.

Regulatory Recommendation: Structured Settlement with Disgorgement

SEBI should redesign its consent order (settlement) framework to require, as a non-negotiable condition of any settlement, full disgorgement of demonstrable illicit profits plus a minimum penalty of 50% of the disgorgement amount. The current settlement framework, which allows negotiated penalties that often represent a fraction of illicit gains, effectively subsidises fraud resolution at the expense of deterrence.

Settlement agreements should be published in full , including the methodology used to calculate illicit profits , to create a public record that calibrates market expectations regarding enforcement outcomes. The US SEC's practice of detailed settlement press releases and court-filed settlement documents provides a model: the public enforcement record itself serves a deterrence function beyond the specific case.

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Legislative Recommendation: Special Securities Fraud Courts

Parliament should designate Special Securities Fraud Courts , dedicated benches of Sessions Courts or the High Courts, with assigned judges having financial market expertise , to handle criminal prosecutions arising from SEBI referrals. These courts should operate under compressed procedural timelines (mandatory daily hearing schedules for active

trials, 18-month trial completion target) and judges should receive specialised training in financial market instruments, accounting, and economic expert testimony.

Currently, SEBI's criminal referrals to CBI or police proceed through ordinary criminal courts with no specialisation, resulting in trials lasting decades , the Harshad Mehta criminal cases took over twenty years to reach final verdicts. This timeline renders criminal prosecution essentially non-deterrent for financially sophisticated fraudsters who can retain elite legal counsel to exploit procedural avenues indefinitely.

Pillar V: Appellate Structure Reform

Legislative Recommendation: SAT Procedural Reform

The SEBI Act should be amended to restructure SAT's review jurisdiction along the following lines:

Factual deference: SAT should be required to apply a 'perversity' standard (or 'substantial evidence' test) when reviewing SEBI's factual findings in contested enforcement proceedings , similar to the standard applied by US federal courts of appeals reviewing SEC ALJ decisions. SAT should only disturb SEBI's factual conclusions if they are not supported by substantial evidence on the record as a whole. Questions of law should remain subject to de novo review.

Stay conditions: SAT should be statutorily prohibited from staying a SEBI penalty order without the accused depositing a minimum of 50% of the penalty in an escrow with SEBI. The current practice of stays on deposit of 10-15% of the penalty, pending 2-3 year appellate processes, constitutes an effective penalty reduction that the SAT has no statutory authority to grant.

Priority hearing: SAT should be required to finally adjudicate any matter involving penalties above ₹1 crore within 12 months of the appeal filing , with a statutory provision for matter transfer to a bench of three members if the standard two-member bench cannot meet this timeline.

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Institutional Recommendation: Internal Adjudicatory Independence

SEBI should restructure its internal adjudicatory process by creating an Internal Review Panel (IRP) , modelled on the UK FCA's Regulatory Decisions Committee , composed of members who are entirely independent of SEBI's investigation and enforcement functions. The IRP should review all draft enforcement orders before issuance, with authority to query the investigation team, call for additional evidence, and modify findings. This internal due

process layer would reduce the rate of successful SAT appeals on procedural grounds, while simultaneously improving the quality and fairness of SEBI's enforcement output.

IRP members should be appointed by the SEBI Board following a public selection process involving an independent appointments committee , not appointed by the SEBI Chairman alone , and should serve fixed, non-renewable terms to protect their independence.

Pillar VI: Investor Protection and Whistleblower Empowerment

Legislative Recommendation: The Securities Whistleblower Protection and Reward Act

Recommendation: Parliament should enact a Securities Whistleblower Protection and Reward Act, creating a standalone statutory framework for securities market whistleblowing with financial rewards and employment protection mechanisms, drawing from the US SEC Whistleblower Program under Section 21F of the Securities Exchange Act.

The Act should provide: (a) monetary rewards of 15-30% of sanctions exceeding ₹1 crore that result from original information provided by the whistleblower; (b) absolute employment protection including reinstatement, back pay, and damages for whistleblowers who suffer retaliation from their employer; (c) identity protection with statutory prohibition on SEBI disclosing the whistleblower's identity without consent, including in enforcement proceedings; (d) a dedicated Whistleblower Office within SEBI , separate from its Investigation Department , to receive, evaluate, and protect whistleblower submissions; and (e) criminal penalties for retaliation against whistleblowers.

The SEC's Whistleblower Program has generated over $1.3 billion in awards since 2012 and has facilitated numerous major enforcement actions , including fraud schemes that surveillance systems would likely not have detected independently. A comparable Indian program would leverage the insider knowledge of company employees, auditors, bankers, and advisors , the people with the most direct access to the information that regulators most need.

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The Yes Bank AT-1 bond misselling, for instance, was known to relationship managers across multiple bank branches who had no accessible, protected channel for disclosure.

Regulatory Recommendation: Retail Investor Protection Fund Enhancement

SEBI's Investor Protection and Education Fund (IPEF) should be redesigned to serve as an active compensation mechanism for retail investors harmed by adjudicated fraud , rather than primarily an investor education vehicle. Specifically:

SEBI should establish a Securities Fraud Compensation Scheme funded by mandatory contributions from enforcement disgorgement proceeds, with a defined per-investor cap (e.g., ₹10 lakh per affected investor per fraud) and streamlined application procedures accessible through online claims processing. Priority should be given to retail investors (holdings below ₹10 lakh) who can demonstrate direct loss causation from a specific adjudicated violation.

This reform addresses a fundamental fairness problem in Indian securities enforcement: SEBI successfully prosecutes fraud, imposes disgorgement, and recovers illicit profits , but those recovered funds typically flow to SEBI's general corpus rather than to the retail investors who bore the actual loss. The SEC's Fair Fund mechanism, established by the Sarbanes-Oxley Act, provides the model: disgorged amounts are distributed to harmed investors through court-supervised distribution plans. India lacks an equivalent mechanism, leaving retail fraud victims without compensation even when enforcement succeeds.

Legislative Recommendation: Strengthening the SCORES Platform

SEBI's complaints resolution system, SCORES, should be elevated from an administrative grievance platform to a statutory complaints resolution mechanism with binding timelines , codified in the SEBI Act. Specifically: all complaints should receive a substantive response within 30 days; complaints unresolved at 60 days should automatically trigger an ombudsman review; and the SEBI Ombudsman (an institution currently advisory in nature) should be empowered to award compensation up to ₹25 lakh without recourse to SAT.

Fraud-Specific Prevention Mechanisms: A Regulatory Toolkit

Preventing Circular Trading and Price Manipulation

Beyond surveillance architecture improvements, the most direct prevention mechanism for

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circular trading is liquidity-adjusted circuit breakers , dynamic price movement limits that contract as trading volume in a scrip concentrates among a small number of entities. Currently, NSE and BSE apply uniform circuit breaker limits (5%, 10%, 20%) across all scrips, regardless of the entity concentration of trading. A concentration-adjusted circuit breaker would narrow the permissible daily price band when, for example, the top five
trading entities account for more than 60% of daily volume in a scrip , triggering exchange-level surveillance review before further price movement is permitted.
Additionally, SEBI should mandate that all scrips with market capitalisation below ₹500 crore are subject to trade-by-trade surveillance , requiring real-time entity attribution

before each trade is confirmed , rather than the end-of-day batch surveillance currently applicable to the bottom tier of listed companies. These low-cap, low-liquidity scrips are the most susceptible to circular trading precisely because their thin liquidity means small absolute volumes can move prices dramatically.

Preventing Offshore Structure Fraud

The most effective prevention mechanism for offshore beneficial ownership concealment is the conditional market access model: no FPI, P-Note issuer, or derivative counterparty should have access to Indian securities markets without prior registration of ultimate
beneficial owners down to natural persons in India's Beneficial Ownership Intelligence Database. This registration must be updated within 48 hours of any change in UBO. FPIs that fail to update UBO disclosures within the required timeframe should have their trading access automatically suspended pending compliance verification.

SEBI should also establish a Suspicious FPI Flag System , similar to the EU's ESMA Guidelines on suspicious transaction reporting under MAR , where FPIs that exhibit trading patterns inconsistent with their disclosed investment mandate, or whose trading is
concentrated in scrips also trading in the accounts of their disclosed UBO's other Indian vehicles, are automatically flagged for enhanced due diligence.

Preventing Governance and Disclosure Fraud

The single most effective structural reform for preventing Yes Bank-type governance fraud is the mandatory externally-administered compliance function for listed companies above a defined size (total assets above ₹500 crore, or market capitalisation above ₹1,000 crore). Rather than allowing listed companies to employ their own compliance officers who are structurally subordinate to management, SEBI should require these companies to engage SEBI-registered External Compliance Administrators , independent firms (analogous to registered auditors) that

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administer the LODR compliance function without employment relationship to the listed company.

The External Compliance Administrator would be responsible for: real-time SEBI disclosure filings (independent of management approval); pre-clearance of designated person trades; RPT identification and disclosure; and board meeting information flow (ensuring that material information reaches the board and, where required, SEBI, even if management prefers non-disclosure). The Administrator would report directly to the Audit Committee and to SEBI, not to the Managing Director.

Preventing Algorithmic Market Manipulation

Preventing Jane Street-type algorithmic manipulation requires three coordinated interventions. First, options open interest position reporting should require any entity holding options positions above 2% of the open interest in a single contract series to report its cash market positions in the underlying constituents daily to SEBI , enabling cross- product surveillance for coordinated positioning.

Second, index calculation transparency should be enhanced: NSE and BSE should publish real-time simulation of index values five minutes before official calculation , enabling market participants and SEBI surveillance to observe whether concentrated order flow is systematically biasing the calculation toward a specific level that benefits large derivatives positions.

Third, algorithmic strategy declaration (as recommended in Pillar I) combined with post-trade strategy audit , requiring all high-frequency and algorithm trading firms to submit complete order records tagged by strategy within 24 hours of each trading day , would enable SEBI to conduct retroactive strategy-level analysis that current transaction-level surveillance cannot support.

Implementation Roadmap and Sequencing

Reform of the scope proposed here cannot be implemented simultaneously. The sequencing should be driven by two considerations: the urgency of the vulnerability being addressed, and the time required for institutional capacity to absorb the reform. The following three-phase roadmap reflects this logic.

Phase I (0-18 months): Regulatory action within existing SEBI powers. SEBI should immediately implement algorithm tagging requirements, enhanced FPI UBO disclosure thresholds, the External Compliance Administrator framework for large listed companies, and

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the mandatory disgorgement-plus-penalty settlement floor, all implementable through regulatory circulars and amendments to existing SEBI regulations without Parliamentary action.

Phase II (18-36 months): Legislative package. Parliament should enact the Beneficial Ownership Disclosure Act, the Securities Whistleblower Protection and Reward Act, and the Enforcement Pipeline Reform Act as a coordinated legislative package, ideally in a single Parliamentary session to maintain momentum. The FMIA can be created in this phase through a Presidential Order under Article 77, pending full statutory codification.

Phase III (36-60 months): Institutional build-out. The NMAT (National Market Audit Trail), the Market Intelligence and Analytics Division, the Securities Fraud Compensation

Scheme, and the Special Securities Fraud Courts require sustained institutional investment, technology procurement, recruitment, training, and infrastructure, over 3-5 years. International technical assistance from SEC, FCA, and ESMA should be formalised through regulatory cooperation agreements to accelerate knowledge transfer.

Conclusion: From Reactive Enforcement to Preventive Architecture

The history of Indian securities regulation is, in important respects, a history of reactive reform, each major scandal prompting legislative amendments and regulatory circulars that address the specific mechanism of the most recent fraud while leaving the architectural vulnerabilities intact. Harshad Mehta produced electronic trading and depositories. Ketan Parekh produced circuit breakers and entity-level surveillance improvements. Satyam produced audit committee reforms. IL&FS produced NBFC regulatory tightening. Each reform was necessary and meaningful, and yet the next fraud came, exploiting the next unaddressed gap.

This pattern will continue unless India's regulatory reform philosophy shifts from reactive gap-patching to proactive architectural design. The reform pillars proposed in this chapter, centralised audit trail, mandatory beneficial ownership transparency, integrated inter- agency intelligence, compressed enforcement timelines, appellate structure recalibration, and whistleblower empowerment , collectively constitute a redesign of the regulatory architecture rather than an amendment to any of its existing components. Individually, each reform addresses a documented vulnerability. Collectively, they create a regulatory environment where the costs and risks of sophisticated financial fraud substantially exceed its expected returns, which is the only sustainable basis for market integrity.

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India's capital markets are at a watershed. The country's ambition to become a global financial centre, reflected in the GIFT City project, the internationalisation of Indian equity indices, and the deepening of domestic institutional investor participation, requires a regulatory infrastructure that commands international confidence. The cases examined in this dissertation have demonstrated that the current architecture does not yet command that confidence. The reform agenda proposed here is not merely a response to past frauds, it is the institutional foundation for India's next chapter as a serious participant in global capital markets.

Footnotes

1. Source: SEBI Orders and RBI Reports related to Ketan Parekh Scam (2001).
2. Source: IL&FS Crisis Investigation Reports (2018).
3. Source: Enforcement Directorate and RBI findings on Yes Bank–Rana Kapoor Case.