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RISE OF SEBI ON THE FALL OF “BIG BULL – A SCAM WHICH SHOOK THE INDIAN ECONOMY”

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ABSTRACT

The Indian securities market underwent a fundamental regulatory transformation following the securities scam of 1991–92, popularly associated with Harshad Mehta, the “Big Bull” of Dalal Street. The scam exposed deep structural and institutional deficiencies in India’s financial regulatory framework, including fragmented oversight, weak enforcement mechanisms, and the absence of a powerful market regulator. This paper examines the collapse of the Harshad Mehta reign over the Indian Stock Market which acted as a catalyst for the emergence and consolidation of the Securities and Exchange Board of India (SEBI) as a statutory and authoritative regulator. This study traces SEBI’s evolution from a non-statutory advisory body to a robust regulatory institution vested with legislative, executive, and quasi-judicial powers under the SEBI Act, 1992. This also analyses the legal, institutional, and judicial developments that followed the scam, including enhanced disclosure norms, market surveillance mechanisms, and investor protection measures. The study argues that the rise of SEBI represents a critical moment in India’s financial governance, underscoring the role of crisis-driven reforms in strengthening regulatory institutions. While concerns regarding regulatory overreach and due process persist, SEBI’s evolution remains central to restoring market confidence and ensuring the integrity of India’s capital markets in an increasingly globalised economy.

KEYWORDS: Securities Market, Stock Market Manipulation, Insider Trading, Bank Receipts Fraud, Securities and Exchange Board of India.

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INTRODUCTION:

Trust, transparency and regulation are the fundamental basics of the financial market of a country. Violation of any of these elements results in exploitation of the whole market system. It is also necessary for the regulatory body to monitor and control the system thereby having checks and balances over the same enabling smooth functioning of the system. The Harshad Mehta securities scam of 1992 stands as one of the most notorious financial scandals in the annals of Indian economic history³. The Scam of 1992 is one of the scams which not only impacted the Indian economy, but also entrenched the loopholes in banking system, capital markets and regulatory frameworks of the country. Mehta exploited the financial loopholes of the system enabling to attain an undue advantage over the same thereby skyrocketed the stock prices. Needless to state that, the above scam was one of the biggest one which estimated around Rs. 4,000 to 5,000 Crores way back in 1992. The scam involved the illegal diversion of funds from the banking system—estimated at approximately 4,000 crores at the time which now equivalent to tens of thousands of crores which were used to artificially inflate the prices of select stocks, thereby creating an unsustainable bubble that ultimately burst.⁴ Key institutions such as the Reserve Bank of India (RBI), the Securities and Exchange Board of India (SEBI), and major public sector banks were found to be complicit, complacent, or completely unaware of the scale and nature of the scam⁵. This article throws light over the aspect, modus operandi adopted by Harshad Mehta and how the Securities Exchange Board of India conferred powers to mitigate and investigate such kind of scam and scandal.

OBJECTIVES

1. To study about the stock market exploitation and its key mechanisms
2. To study about the interplay between Stock Market and Money market manipulation by Harshad Mehta
3. To study about the necessity of the Security and Exchange Board of India Act, 1992
4. To study on the regulatory and quasi-judicial powers conferred on SEBI
5. To analyze the amendments and structural changes brought about by SEBI.

³ Sarthak Jain, A Project on: Harshad Mehta vs Union of India (Scam 1992): An Economic Analysis (Aug. 30, 2022)

⁴ Kishore Kumar, 1992 Indian Stock Market Scam – The Complete Case Study of Harshad Mehta, Intellipaat (Jan. 21, 2025)

⁵ Sucheta Dalal, How Harshad Mehta Did It Again (Apr. 15, 2025)

REVIEW OF LITERATURE:

1. The article by Gupta on “*Scams that changed India’s Capital Market*”⁶ examines major **capital market scams in India**, focusing especially on the **Harshad Mehta scam of 1992** and the **Ketan Parekh scam of 2001**. It provides a **historical overview of the Indian capital market** and analyses how these high-profile frauds exposed deep **regulatory weaknesses** and systemic loopholes in financial oversight. It also explains the key insights which are relevant for the rise of SEBI.
2. One of the earliest and most authoritative academic analyses of the Indian securities scam of 1992 is provided by **Damachis (1994)** in his article “*The Bombay Securities Scam of 1992: The Systemic and Structural Origins*”⁷ which examines the scam not merely as an instance of individual fraud, but as a manifestation of deeper **systemic weaknesses embedded within India’s financial and regulatory architecture** during the pre-liberalisation period
3. The article by Subhasri Roy on “*The Big Bull’s Run – A Case study of the Harshad Mehta Securities Scam*”⁸ provides a **comprehensive case study** of the 1992 Indian securities scam orchestrated by Harshad Mehta. It deconstructs how systemic vulnerabilities in India’s financial and banking systems were manipulated to create an artificial and unsustainable bull market.
4. The article “*Decoding the Harshad Mehta Scam: Legal Loopholes and Financial Irregularities in India’s Securities Market*”⁹ by Aryan Das and Arpit Tiwary provides a **comprehensive legal and financial analysis** of the 1992 **Harshad Mehta securities scam**, highlighting the systemic failures in India’s financial regulatory framework and the resulting need for reform. It also throws light over the modus operandi adopted by Harshad Mehta in the manipulation of securities market (i.e, Ready Forward Deals and Bank receipts)
5. The article by Sai Sree Vyshnavi in “*The Rise and Fall of Harshad Mehta: Case Study on Financial Fraud and Post-Scam Reforms in India*”¹⁰, meticulously explains how Harshad Mehta exploited structural weaknesses in **Ready Forward (RF) deals** and the

⁶ SunText Review of Arts & Social Sciences - Volume 4:2 - published on 07 May 2023

⁷ Damachis, The Bombay Securities Scam of 1992: The Systemic and Structural Origins, 29 Econ. & Pol. Weekly 109 (1994).

⁸ Subhasri Roy, The Big Bull’s Run – A Case Study of the Harshad Mehta Securities Scam, Indian J. Fin. L. (2018).

⁹ Aryan Das & Arpit Tiwary, Decoding the Harshad Mehta Scam: Legal Loopholes and Financial Irregularities in India’s Securities Market, Nat’l L. Sch. India Rev. (2020).

¹⁰ Sai Sree Vyshnavi, The Rise and Fall of Harshad Mehta: Case Study on Financial Fraud and Post-Scam Reforms in India, Int’l J. L. Mgmt. & Human., Vol. 5, Issue 2 (2022).

misuse of **Bank Receipts (BRs)** to divert massive banking funds into the equity market, thereby artificially inflating stock prices.

6. The paper by Kapil Kamdar in “*Harshad Mehta’s case : Stock Market and Bank Receipts Scam*” examines the **1992 Harshad Mehta securities and banking scam**, explaining how Harshad Mehta manipulated the Indian stock market by exploiting **loopholes in the banking system and bank receipts (BRs)**, resulting in the siphoning of over **24,000 crore** through the share trading system over a span of three years.

SHARE AND STOCK MARKET:

A share represents a fractional ownership of a share capital of a Company to an investor/purchaser and inherits certain rights which include certain proprietary and governance rights including voting rights, right to dividends, claims upon assets in the event of liquidation of the Company, etc. A person who holds a share of a Company is known as the Shareholder and the place where these shares are listed and traded is known as Stock Market.

In its classification, the market may be primary or secondary. Primary Market represents the shares and equity which were initially listed for public purchase directly by the concerned Company after obtaining prior permission from the authority and compliance of the regulations. This process is known as listing and commonly known as IPO (Initial Public Offering). This does not involve trading or its related activities. Whereas, the Secondary market deals with buying and selling of shares and securities which were already listed in the primary markets.

A stock market is more like of a share market in its wider mechanism. While the share market involves in buying and selling of shares, the stock market encompasses the trading of **shares, stocks, and other marketable securities**, including bonds, derivatives, and mutual fund units. Stock market operates through recognized stock exchanges in India such as the **Bombay Stock Exchange and National Stock Exchange** popularly known as **BSE** and **NSE** which facilitates large scale participation by domestic and foreign investors. The stock market plays a pivotal role in the building of national economy by promoting capital formation, enhancing corporate governance and contributing to the economic stability and growth.

REGULATORY MECHANISMS PRIOR TO THE SECURITY

EXCHANGE BOARD OF INDIA (SEBI):

The history of buying and selling stocks in India dates to the 18th century and culminated in the establishment of the **Bombay Stock Exchange (BSE)** in 1875.¹¹ It is well-known as the oldest Stock Exchange in Asia and the BSE initially operated by depending on its own guidelines as a substitute without a proper regulatory body. The Indian Capital Market was majorly unregulated till the enactment of **Bombay Securities Contracts Control Act, 1925**. It is also pertinent to state that, as there were very few Indian Companies on the Pre-Independent era, the Indian Capital market could not develop and the securities which traded in the Stock Exchanges were very negligible.

Thereafter the British government in India, during the regime of Second World War, introduced the **Controller of Capital issues** under the Defence of India Act, 1939. The Core purpose of the Act was to serve the special provision for ensuring the public safety and defence of British India. However this act does not hold an elaborative provision for the securities and exchange but it on clear words expresses that for any matter relating to securities or of foreign exchange the government will be the one making any regulations providing that there was no separate entity dealing for this particular matter, thus expressing the need for a distinct regulations for the securities and exchange.¹²

Thereafter the **Capital Issues (Control) Act of 1956** took over and for the purpose to direct the resources towards the aid of war issues. It provided that without approval from the central government, no company can publically offer the securities for the purpose of sale.¹³ Therefore from the outset it has been clear that, by this act, all the powers vested with the Central Government and there was no separate body to govern the securities.

After the post-World War and Indian Independence, subsequent of the enactment of Capital Issues (Control) Act, the **Securities Contract (Regulations) Act, 1956** was enacted for the purpose to prevent undesirable transactions on securities by regulating the business of dealing therein, providing for certain other matters connected therewith¹⁴. This was the first

¹¹ Article by Savithiri Suresh on “Who regulated the Stock Market Regulation in India before SEBI?”

¹² Securities Regulations In India Before Sebi: Tracing Regulatory Authorities And Sebi’s Evolution Amid Financial Scandals - Indian Journal of Integrated Research in Law - Volume V Issue I

¹³ Capital Issues (Control) Act, 1947, S 3(2) (b).

¹⁴ Preamble to the Securities Contracts (Regulation) Act, 1956 (Act 42 of 1956) (India)

act which pointed out and mentioned about the recognized Stock Exchange and provides application and grant for recognized stock exchange¹⁵

However, even after introduction of stock exchange in this act, still the control had been held with the central government, giving no free authority to the securities body. So it's quite evident with all these three acts that either there were no elaborative provisions for the securities exchange or if there were provisions for these so there it under complete control of central government, this eventually led for the need of separate body for securities.

Therefore, the need for a separate body for securities exchange arose, which none of the prior act focus on and in order to fix this lacuna, the Securities Exchange Board of India, 1988 was established as a non-statutory body by way of passing of a resolution by the Government of India.

MEHTA'S MODUS OPERANDI IN SCAM 1992:

Harshad Shanthilal Mehta was born in Gujarat but brought up at Mumbai. Mehta's early career was rooted in the cement trade, following which he transitioned into the securities market as a jobber on the Bombay Stock Exchange. Later on learning the tricks of the stock market being a jobber, he quit the job and started a trading firm under the name and style of Growmore Research and Asset Management during the later half of the 1980's. It is a brokerage entity that soon came to be identified with exceptional financial performance and a predominant presence in the securities market. He initially started to manipulate the market by the concept of insider trading. It embodies the principle of buying or selling a public company's stock using secret, crucial information (material nonpublic information) not available to the general public, creating an unfair advantage and breaching a fiduciary duty. He obtained the crucial information regarding particular stocks with the help of labourers of the concerned entity due to which he starts to earn good amount of profits than the other stock broking entities.

Harshad Mehta believed in optimistic approach while investing. He strongly believed in the potential of undervalued blue-chip companies and focused on big names like ACC, TISCO, and the State Bank of India by not just quietly buying these stocks but rather buying large quantities of it and openly speaking about how undervalued these stocks were being

¹⁵ Section 2(f), 3 and 4 of The Securities Contracts (Regulation) Act, 1956 (Act 42 of 1956) (India)

perceived in the market.¹⁶ This in terms of Mehta referred to as “*THE REPLACEMENT COST THEORY*”¹⁷. Mehta not only manipulated the market with this concept, but also attained undue advantage over the same by buying and selling of stocks in a lot (higher quantities) by creating artificial demand of stocks and by gaining people’s confidence over the said stocks. Mehta invested those confidences which resulted in skyrocketing other affiliated stocks thereby gain a lump-sum amount as commission from the concerned companies which resulted in a win-win situation for him.

Later when the share market crashes in early 1980’s (1982), since Harshad Mehta was lack of funds, he started to use his growmore brokerage entity also to be a consultancy firm for fresh investors for a subscribed premium for his expertise over the field. Wherein he helped his investors and clients to earn more (by price rigging the stocks which their clients purchased) thereby self-sustained even when the market was unstable. Thereafter, he entered the money market¹⁸ wherein he found the loopholes at its earliest and mobilized the money market funds into share market thereby skyrocketing the price of stocks at an unimaginable high wherein the sensx touched its peak due to which he was even termed as “The Real Big Bull”. He also shattered the bear cartel whereby using the bank funds to keep buying stocks, forcing these traders to buy at higher prices to cover their positions, further driving up prices.

a) *Stamp paper fraud*¹⁹

Up to the early ’90s banks in India were not allowed to invest in the equity markets. However, they were expected to post profits and retain a specific ratio (threshold) of their government fixed interest bonds assets. Mehta skillfully extracted capital from the banking sector to meet the requirements of the bank, diverting these funds into the stock market. He also assured the banks of better interest rates while requesting them to deposit money into his account, pretending it was for purchasing securities from other banks. At that point, banks were required to engage a broker to buy securities and transfer bonds from other banks. Mehta temporarily utilized this money in his account to invest in shares, which significantly increased the demand for individual stocks (of well-established companies like ACC, Sterlite Industries, and Videocon), selling them,

¹⁶ Scam 1992: Harshad Mehta Scam Story, 5Paisa (Apr. 15, 2025)

¹⁷A Valuation method determining an asset's worth by the current market price to acquire a similar substitute, focusing on present-day utility rather than original cost, crucial for insurance, business valuation (especially for asset-heavy firms), and asset management to decide on upgrades, especially during inflation

¹⁸ The money market is a financial market sector where financial instruments with high liquidity and short maturities are traded.

¹⁹ Harshad Mehta Largest Stock Market Scam – CA Monk published on 03-06-2021

sharing a portion of the profits with the bank, and keeping the remainder for himself. This resulted in stocks like ACC (which was trading in 1991 for Rs.200/share) to nearly Rs.9,000/- in just three months.

b) Bank receipt fraud

Another instrument used in a big way was the **Bank Receipt**. In a ready-forward deal, did not move securities back and forth in actuality. Instead, the borrower, i.e. the seller of securities, gave the buyer a Bank Receipt. BR's serves as a receipt from the selling bank and promises that the buyer will receive the securities they have paid for at the end of the term. Having figured this out, Mehta needed banks, which could issue fake BRs, or BRs not backed by any government securities. Once these fake BRs were issued, they were passed on to other banks, and the banks, in turn, gave Mehta money, plainly assuming that they were lending against government securities when this was not the case. He took the Price of ACC from Rs.200 to Rs.9,000. An increase of 4,400% in stock markets was overheated, and the bulls were on a mad run. Since he had to book profits, the day he sold was when the markets crashed at 1992. During such period, the Securities and Exchange Board of India was established as a non-statutory body which could govern the security transactions but was not conferred with wider powers. SEBI inherited its wider powers after the scam started to expose.

The scam started unraveling when the State Bank of India wanted the return of real securities pertaining to an Ready Forward deal, and they were not forthcoming. Suspicion graduated to a full-fledged investigation when Sucheta Dalal, a journalist with The Times of India, wrote a front-page report revealing the anomalies.²⁰

RISE OF THE SECURITIES AND EXCHANGE BOARD OF INDIA:

The Securities and Exchange Board of India was constituted as a non-statutory body on April 12, 1988 through a resolution of the Government of India. In 1988, SEBI had limited powers. It is the apex regulatory authority entrusted with the regulation and development of India's securities market and granted statutory status through the **SEBI Act, 1992**. Chiefly it regulated the securities market and ensured its constant development. SEBI had no control over the transactions taking place between the brokers and the investors at that point of time and the same was within the jurisdiction of the Central Bureau of Investigation (CBI) to look into the matter. Since the **Harshad Mehta securities scam of 1991-92**, exposed significant

²⁰ Sucheta Dalal, The Great Bank Scam, Times of India, Apr. 23, 1992

deficiencies in India's financial regulatory framework, the same acted as a catalyst for strengthening SEBI's authority, transforming it from a largely advisory body into a robust statutory regulator with enforcement powers comparable to global securities regulators. Presently SEBI plays a central role in ensuring market integrity, protecting investor interests, and promoting orderly growth of the capital market.

POWERS CONFERRED ON SEBI AFTER SEBI ACT, 1992

In general, the powers conferred in SEBI after the Harshad Mehta scandal includes **regulatory, supervisory, investigative, and quasi-judicial functions** and the same can be categorized into:

Power to Enforce – SEBI was empowered to enforce regulatory actions and penalties more effectively. It gained authority to initiate investigations, conduct search and seizure operations, and impose penalties on market manipulators, insider traders, and fraudulent actors.

Power to Protect²¹ – The scandal highlighted the need to protect investors including investigative surveillance powers. SEBI introduced stricter disclosure requirements, mechanisms for investor grievance redressal, mandated Know Your Customer (KYC) norms, and established the Investor Protection Fund to help compensate investors.

Power to Oversee – SEBI expanded its oversight to cover more financial instruments and participants. It moved beyond primarily regulating stocks and bonds to include derivatives and mutual funds, allowing a more comprehensive regulatory framework including monitoring of intermediaries, stock exchanges and market practices²².

Power to Inform – SEBI took steps to improve market transparency with better disclosure norms, enhanced reporting standards, and the introduction of electronic trading platforms. Dematerialization of shares also reduced opportunities for fraud.

Power to Govern – Corporate governance reforms were introduced, such as guidelines for independent directors, audit committees, and disclosure of related party transactions, to ensure greater accountability and transparency within companies.

Changes also include :²³

- a. **Control over Issue of Capital:** The Capital Issues (Control) Act, 1947 was repealed in May 1992 which was a major initiative of liberalization. With this, Government's control

²¹ Section 11(1) of the Securities and Exchange Board of India Act, 1992

²² Section 11(2) of the Securities and Exchange Board of India Act, 1992

²³ A Historical Perspective of the Securities Market Reforms – March 23, 2004 by SEBI

over issue of capital, pricing of the issues, fixing of premia and rates of interest on debentures etc. ceased and the market was allowed to allocate resources to competing uses. In the interest of investors, SEBI issued **Disclosure and Investor Protection (DIP)** guidelines. The guidelines allow issuers, complying with the eligibility criteria, to issue securities the securities at market determined rates. The market moved from merit based to disclosure based regulation.

- b. **Establishment of Regulator:** A major initiative of regulation was establishment of a statutory autonomous agency, called SEBI, to provide reassurance that it is safe to undertake transactions in securities. It was empowered adequately and assigned the responsibility to protect the interests of investors in securities, promote the development of the securities market, and regulate the securities market. Its regulatory jurisdiction extends over corporates in the issuance of capital and transfer of securities, in addition to all intermediaries and persons associated with securities market. All market intermediaries are registered and regulated by SEBI. They are also required to appoint a compliance officer who is responsible for monitoring compliance with securities laws and for redressal of investor grievances.
- c. **Screen Based Trading:** A major developmental initiative was a nation-wide on-line fully-automated **Screen Based Trading System (SBTS)** where a member can punch into the computer quantities of securities and the prices at which he likes to transact and the transaction is executed as soon as it finds a matching sale or buy order from a counter party. SBTS electronically matches orders on a strict price/time priority and hence cut down on time, cost and risk of error, as well as on fraud resulting in improved operational efficiency. It allowed faster incorporation of price sensitive information into prevailing prices, thus increasing the informational efficiency of markets. It enabled market participants to see the full market on real-time, making the market transparent. It allowed a large number of participants, irrespective of their geographical locations, to trade with one another simultaneously, improving the depth and liquidity of the market. The SBTS shifted the trading platform from the trading hall of an exchange to brokers' premises. It was then shifted to the PCs in the residences of investors through the Internet and to hand-held devices through WAP for convenience of mobile investors. This made a huge difference in terms of equal access to investors in a geographically vast country like India.
- d. **Risk management:** A number of measures were taken to manage the risks in the market so that the participants are safe and market integrity is protected. These include:

- i) **Trading Cycle:** The trading cycle varied from 14 days for specified securities to 30 days for others and settlement took another fortnight. Often this cycle was not adhered to. This was euphemistically often described as T+ anything. Many things could happen between entering into a trade and its performance providing incentives for either of the parties to go back on its promise. This had on several occasions led to defaults and risks in settlement. In order to reduce large open positions, the trading cycle was reduced over a period of time to a week initially. Rolling settlement on T+5 basis was introduced in phases. All transactions moved to rolling settlement from December 2001. T+5 gave way to T+3 from April 2002 and T+2 from April 2003.
- ii) **Dematerialisation:** After the 1992 scam took place, the settlement system on Indian stock exchanges gave rise to settlement risk due to the time that elapsed before trades are settled. Trades were settled by physical movement of paper. In many cases the process of transfer took much longer, and a significant proportion of transactions ended up as bad delivery due to faulty compliance of paper work. Theft, forgery, mutilation of certificates and other irregularities were rampant, and in addition the issuer had the right to refuse the transfer of a security. All this added to costs, and delays in settlement, restricted liquidity and made investor grievance redressal time consuming and at times intractable.

To obviate these problems, Act 22 of 1996²⁴ was passed to provide for the establishment of depositories in securities with the objective of ensuring free transferability of securities with speed, accuracy and security by making securities of public limited companies freely transferable subject to certain exceptions; dematerializing the securities in the depository mode; and providing for maintenance of ownership records in a book entry form.

- iii) **Settlement Guarantee:** Trade and settlement guarantee funds were set up to guarantee settlement of trades irrespective of default by brokers. These funds provide full novation and work as central counter party. The Exchanges/clearing corporations monitor the positions of the brokers on real time basis thereby guaranteeing the settlement for the purchasers

Other major scams such as Ketan Parekh scam which employed tactics like pump and dump and circular trading, that led to losses amounting to INR 40,000 crores, Sahara

²⁴ The Depositories Act, 1996 (Act 22 of 1996), India

Scam in which the management of the Sahara Group breached the Companies Act 2013 by issuing Optionally Fully Convertible Debentures (OFCDs) and raising funds in a wrong way, In Satyam Scam, its founder B Ramalinga Raju manipulated financial statements to exaggerate sales, earnings and cash balances, amounting to INR 7,000 crore made its significant contributions in structuring the present Securities and Exchange Board of India.

CONCLUSION:

The rise of the Securities and Exchange Board of India (SEBI) can be seen as a direct response to the fall of the Big Bull, Harshad Mehta. Harshad Mehta's manipulation of the stock market through fraudulent activities such as misusing bank funds and inflating stock prices ultimately caused a massive financial crisis and the collapse of many investors' wealth.

In the aftermath of the scam, SEBI's role became critical in reshaping and regulating India's financial markets. SEBI was empowered with more authority to ensure transparency, safeguard investor interests, and prevent market manipulation. It introduced stringent regulations on the stock market, including rules for trading, disclosures, and auditing practices. SEBI also focused on creating a more disciplined, transparent and accountable environment for investors, with greater oversight over financial institutions and intermediaries.

The rise of SEBI, with its enhanced regulatory framework, played a key role in restoring investor confidence, preventing further scams, and ensuring the stability of the Indian stock market. Through its actions, SEBI helped transform India's financial markets into a more organized and trustworthy system for investors, marking a new era of market regulation.

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