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# **ANALYSIS OF THE ROLE OF SEBI IN SAFEGUARDING RETAIL INVESTORS IN INDIA**

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## **Abstract**

The stability and developmental trajectory of the Indian securities market are fundamentally contingent upon the preservation of investor confidence, particularly among the burgeoning demographic of retail participants. This research report investigates the multifaceted role of the Securities and Exchange Board of India (SEBI) as the primary statutory guardian of retail interests. Following the democratisation of finance through digital platforms, retail participation has surged from 40 million demat accounts in 2020 to over 150 million by mid-2024, exposing a vulnerable segment of the population to complex risks such as information asymmetry, market manipulation, and sophisticated digital fraud. The report examines the evolution of SEBI from its non-statutory origins in 1988 to its current status as a quasi-judicial, quasi-legislative, and quasi-executive powerhouse under the SEBI Act of 1992. It provides a granular analysis of the regulatory landscape, including the Listing Obligations and Disclosure Requirements (LODR) Regulations, 2015, and the Prohibition of Insider Trading (PIT) norms, alongside a detailed evaluation of grievance redressal through the revamped SCORES 2.0 platform. Furthermore, the study explores the judicial recognition of SEBI's protective mandate through landmark cases like the Sahara and Price Waterhouse disputes, while identifying the "restitution gap"—the systemic failure to return disgorged funds to victims. The report concludes with structural recommendations, including the adoption of a US-style Fair Fund mechanism and enhanced digital surveillance to combat the rise of unregistered "finfluencers" and pre-investment scams.

## **Keywords**

SEBI, Retail Investor Protection, Securities Law, Market Surveillance, SCORES 2.0.

## **Introduction and Research Problem**

The Indian capital market has undergone a paradigm shift, transitioning from a broker-centric physical ecosystem to a high-frequency, digital-first environment. Central to this transformation is the retail investor—defined as an individual whose investment in a single

issue typically does not exceed ₹2 lakhs—who has become the bedrock of market liquidity and household financialisation. The Securities and Exchange Board of India (SEBI), established under the SEBI Act, 1992, is mandated to ensure that this growth is not compromised by malpractices. However, the rapid expansion of participation has outpaced traditional regulatory perimeters.

The central research problem lies in the widening gap between market innovation and investor protection. As retail investors transition from savers to active market participants, they face a "power imbalance" compared to dominant institutional players who possess superior technological infrastructure and access to unpublished price-sensitive information. Emerging threats such as unregulated financial influencers ("influencers"), pump-and-dump schemes on social media, and the lack of a mandatory restitution framework for victims of market-wide fraud threaten to erode the very trust that SEBI seeks to maintain. While SEBI's surveillance and enforcement mechanisms are robust, the practical challenge of returning recovered "unlawful gains" to identifiable victims remains a significant hurdle in the pursuit of equitable financial justice.

### **Research Objectives**

This report aims to fulfil the following strategic objectives through an in-depth analysis of regulatory, judicial, and technological frameworks:

- To evaluate the effectiveness of the SEBI (LODR) Regulations, 2015, in mitigating information asymmetry and ensuring corporate accountability for retail investors.
- To analyse the operational evolution of the SEBI Complaints Redress System (SCORES 2.0) and its efficacy in resolving investor grievances within stipulated timelines.
- To investigate the preventive role of market surveillance mechanisms, such as ASM and GSM, in curbing speculative excesses and price rigging.
- To scrutinise the impact of judicial precedents, specifically the Sahara and Satyam cases, in defining the boundaries of SEBI's jurisdiction over non-traditional market actors.
- To identify the limitations of the Investor Protection Fund (IPF) and propose legislative amendments for a proactive restitution mechanism.

## Research Questions

The investigation is structured around several critical inquiries that address the core of the regulatory challenge:

1. How do the SEBI (LODR) and PFUTP Regulations function to create a level playing field between retail and institutional investors?.
2. What are the specific challenges posed by digital-era frauds, and how effective is SEBI's AI-driven surveillance ("Sudarshan") in neutralising these threats?.
3. Why does the current Indian legal framework struggle with the distribution of disgorged funds, and what can be learned from international models like the SEC's Fair Fund?.
4. To what extent does the "defaulter" requirement for the Investor Protection Fund act as a barrier to timely compensation for small investors?.

## Research Hypotheses

The following propositions guide the analytical narrative of this report:

- **Hypothesis 1:** The implementation of stringent disclosure norms under LODR and risk-labeling (Riskometers) in mutual funds has a direct positive correlation with increased retail investor participation and market stability.
- **Hypothesis 2:** The shift toward digital grievance redressal (SCORES 2.0) and Online Dispute Resolution (ODR) significantly reduces the average resolution time for retail complaints compared to traditional manual processes.
- **Hypothesis 3:** Despite extensive enforcement, the lack of statutory clarity on "automatic restitution" leads to an "undue enrichment" of government-held funds (IEPF) rather than the financial restoration of affected victims.

## Research Methodology

This study adopts a doctrinal and analytical research methodology, synthesising primary legal sources, regulatory circulars, and secondary academic data. The analysis is grounded in the provisions of the SEBI Act, 1992, the Securities Contracts (Regulation) Act (SCRA), 1956, and the Companies Act, 2013. Data for the evaluation of investor behaviour and regulatory efficacy is drawn from the SEBI Investor Survey 2025 (covering 90,000 households) and the SEBI Annual Report 2023-24. The effectiveness of grievance mechanisms is assessed through empirical data on complaint disposal from the SCORES 2.0 platform. Furthermore, a comparative legal analysis is performed between Indian regulations and the US Sarbanes-Oxley

Act to propose structural reforms in investor restitution.

## Literature Review

The academic discourse on investor protection in India has transitioned from focusing on foundational establishment to assessing technological and corporate governance challenges. Early literature, such as Acharya et al. (2007), highlighted SEBI's pivotal role in emerging from the post-1992 scams to improve corporate governance. Subsequent studies by Mishra (2010) established a positive link between SEBI's surveillance and market resilience during periods of volatility.

Recent scholarship (2023-2025) has focused on the "digital transformation" of the market. Research by Singh (2021) and Bhardwaj (2025) emphasises that while digital KYC and e-trading have improved accessibility, they have introduced new risks such as "influencer" manipulation and algorithmic trading biases. Furthermore, the work of Agrawal (2025) critically identifies the "missing link" in investor restitution, noting that the Investor Protection and Education Fund (IEPF) has ballooned to over ₹533 crore, yet direct compensation to victims of fraud remains rare. Critics argue that the current focus on "investor education" must be balanced with a "rights-based restitution" framework to maintain long-term confidence.

## Research & Analysis

### 1. Who are Retail Investors and Why They Need Protection

The concept of the "retail investor" in India is synonymous with the "small investor"—the individual who seeks to grow their hard-earned savings through equity, debt, or mutual funds. Regulatory definitions often categorise them based on investment size, typically those applying for securities worth up to ₹2,00,000 in a public issue.

#### The Power Imbalance and Systematic Vulnerability

Retail investors operate under several inherent disadvantages compared to institutional players like Mutual Funds, Foreign Portfolio Investors (FPIs), and Alternate Investment Funds (AIFs). These institutional entities possess:

- **Informational Superiority:** Access to advanced research, direct lines to management, and sophisticated data analytics.
- **Technological Infrastructure:** High-frequency trading (HFT) and algorithmic models

that can execute trades in microseconds, often leaving retail investors to deal with "lagged" price discovery.

- **Financial Resilience:** The ability to absorb volatility that might otherwise wipe out the life savings of a retail participant.

The need for protection arises from these imbalances. Without a strong regulator, the market becomes a "lemons market" where information asymmetry leads to the exploitation of the uninformed by the informed, eventually causing a total collapse of investor trust.

### Common Risks in the Digital Era

Risk Type	Mechanism of Harm	Impact on Retail Investors
<b>Information Asymmetry</b>	Insiders trade on non-public information before the retail public is aware.	Retail investors buy at inflated prices or sell at undervalued rates.
<b>Market Manipulation</b>	Pump-and-dump schemes or "marking the close" strategies.	Artificial volatility leads to forced liquidations and capital loss.
<b>Digital Fraud</b>	Fake trading apps, "assured return" schemes on WhatsApp.	Total loss of principal before the investor even enters the formal market.
<b>Unregistered Advice</b>	"Finfluencers" promoting stocks for undisclosed commissions.	Investors follow unresearched tips, leading to systematic portfolio erosion.

## 2. Legal Framework for Retail Investor Protection

The protection of retail investors is not merely a policy objective but a statutory mandate embedded in several key pieces of legislation. This legal architecture provides SEBI with the authority to regulate, investigate, and punish.

### The SEBI Act, 1992: The Foundational Pillar

The SEBI Act is the primary source of the regulator's power. Section 11 of the Act explicitly states that it is the "duty of the Board to protect the interests of investors in securities". The Act

grants SEBI a unique "quasi-trinity" of powers:

1. **Quasi-Legislative:** Power to draft regulations like LODR, PIT, and ICDR.
2. **Quasi-Executive:** Power to conduct investigations, search and seizure, and enforce compliance.
3. **Quasi-Judicial:** Power to pass orders, levy penalties, and issue debarment directions.

### Ancillary Statutes

While the SEBI Act provides the authority, other statutes define the "territory" of operation:

- **Securities Contracts (Regulation) Act (SCRA), 1956:** Governs the recognition and regulation of stock exchanges and the listing of securities.
- **Depositories Act, 1996:** Facilitates the transition to paperless trading, ensuring that the custody of retail assets is secure and verifiable through electronic records.
- **Companies Act, 2013:** Section 125 establishes the Investor Education and Protection Fund (IEPF), which serves as a repository for unclaimed dividends and disgorged gains.

## 3. Objectives of SEBI with Respect to Retail Investors

SEBI's mission is centred on three core pillars: protecting investors, promoting market development, and regulating the market. For the retail investor, these objectives translate into specific operational goals.

### Ensuring Market Integrity and Fairness

SEBI strives to create a "level playing field." This means that a retail investor in a rural district should theoretically have the same access to material information as a fund manager in Mumbai. The objective is to eliminate "fraud, dishonesty, and artificiality" from the price discovery process.

### Preventing Exploitation and Misinformation=

In a market where "information is currency," SEBI's objective is to ensure that the currency is not counterfeit. By mandating rigorous disclosures in prospectuses (ICDR) and continuous reporting (LODR), SEBI prevents companies from luring retail investors into "vanishing companies" or Ponzi-style offerings.

#### 4. SEBI’s Regulatory Measures for Retail Investor Protection

To achieve its objectives, SEBI has implemented a suite of regulatory measures that act as "guardrails" for the retail journey.

##### Disclosure and Transparency: The LODR Mandate

The SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, are perhaps the most vital tool for retail protection. They ensure that listed entities remain accountable through timely disclosures.

Requirement	Frequency	Objective for Retail Investors
<b>Financial Results</b>	Quarterly/Annual	Provides regular health checks
Requirement	Frequency	Objective for Retail Investors
		on the company’s profitability.
<b>Material Events</b>	Within 24 hours	Ensures immediate reporting of mergers, defaults, or resignations.
<b>Related Party Transactions</b>	Periodic Approval	Prevents "tunneling" where promoters siphon funds to sister concerns.
<b>Shareholding Patterns</b>	Quarterly	Alerts investors to promoter selling or institutional entry/exit.

A significant 2025 amendment to LODR introduced a "quantitative materiality" threshold. Companies must now disclose any event if its expected impact exceeds the lower of 2% of turnover or 2% of net worth, removing the "subjective discretion" that companies previously used to hide bad news.

##### Regulation of Intermediaries

Retail investors rarely interact with the exchange directly; they rely on brokers, sub-brokers, and investment advisors. SEBI mandates the registration of these intermediaries and enforces a strict Code of Conduct. This includes:

- **Capital Adequacy:** Ensuring brokers have the financial strength to settle trades.
- **KYC Compliance:** Standardising the onboarding process to prevent money laundering

and identity theft.

- **Segregation of Funds:** Requiring brokers to keep client funds separate from their own business capital to prevent "misuse of client collateral".

## 5. SEBI's Role in Preventing Market Abuse

Market abuse—comprising insider trading and fraudulent practices—is the greatest threat to retail capital. SEBI's surveillance and enforcement frameworks are specifically designed to detect and deter these activities.

### Insider Trading (PIT) Regulations, 2015

Insider trading occurs when those with access to Unpublished Price-Sensitive Information (UPSI) trade to make a profit or avoid a loss at the expense of the general public. SEBI mandates:

- **Trading Windows:** Restricting when promoters and directors can trade.
- **Structured Digital Databases (SDD):** Requiring companies to maintain a digital trail of who has access to UPSI to assist in forensic investigations.

### Prohibition of Fraudulent and Unfair Trade Practices (PFUTP)

The PFUTP Regulations target manipulative behaviour such as "price rigging" (artificial price inflation) and "circular trading" (trading between group entities to create a false appearance of volume).

### Surveillance Mechanisms: ASM and GSM

To protect retail investors from "high-risk" volatility, SEBI and the exchanges use Graded Surveillance Measures (GSM) and Additional Surveillance Measures (ASM).

- **Mechanism:** When a stock shows abnormal price-to-earnings ratios or volume spikes without underlying fundamental news, it is moved to these categories.
- **Restriction:** Trading is often restricted to "trade-to-trade" (no intraday), and 100% margins are required, which prevents retail investors from being trapped in "pump-and-dump" cycles orchestrated by operators.

## 6. Investor Education and Awareness Initiatives

A well-informed investor is the best-protected investor. SEBI, alongside the Investor Education and Protection Fund Authority (IEPFA), conducts extensive outreach.

### Financial Literacy Programs

Between FY 2019-20 and FY 2024-25, the IEPFA conducted over 71,000 awareness programs nationwide. These programs cover:

- The basics of budgeting and saving.
- How to identify fake trading apps and Ponzi schemes.
- The importance of diversifying across sectors and avoiding excessive leverage.

### The Saaṛthi App and SMART Initiative

SEBI launched the **Saaṛthi** mobile app to provide retail investors with a "single point of truth" for educational resources. Additionally, the **SMART** (Securities Market Awareness Recognition and Training) initiative empowers a network of trainers to reach rural and Tier-2 city populations, bridging the gap between urban and rural financial literacy.

## 7. Grievance Redressal Mechanism for Retail Investors

When regulations fail, and education is not enough, the retail investor needs a fast and reliable way to seek justice. SEBI's grievance redressal system has undergone a major digital overhaul.

### SCORES 2.0: The Revamped Redressal System

The SEBI Complaints Redress System (SCORES) was upgraded to version 2.0 in April 2024 to make the process more efficient.

Feature	SCORES 1.0	SCORES 2.0
<b>Resolution Timeline</b>	30 Calendar Days	21 Calendar Days
<b>Routing</b>	Manual processing by SEBI	Auto-routing to the concerned entity
<b>Escalation</b>	Manual follow-up	Auto-escalation to higher authorities
<b>KYC Integration</b>	Manual entry of details	Fetches from KRA via PAN/OTP
<b>Review System</b>	Single-level	Two-level (First by MII, Second by SEBI)

### **Online Dispute Resolution (ODR)**

SEBI has integrated the ODR platform to handle disputes that require mediation or arbitration. This provides a legally binding resolution mechanism that is faster and more cost-effective than traditional civil courts. In December 2024 alone, SEBI disposed of 5,636 complaints, with an average resolution time of just eight days for Action Taken Reports (ATRs).

## **8. Judicial Support and Key Case Laws**

The judiciary has played a crucial role in validating and expanding SEBI's protective powers, often intervening when technical loopholes are exploited by large corporations.

### **Sahara India Real Estate Corp. Ltd. v. SEBI (2012)**

This landmark case involved Sahara raising over ₹24,000 crores from 30 million people through "Optionally Fully Convertible Debentures" (OFCDs). Sahara argued that since these were "private placements" issued by unlisted companies, SEBI had no jurisdiction.

#### **Supreme Court Decision:**

- **Public Issue Threshold:** The Court ruled that any offer to more than 49 persons (as per the then Companies Act) is a "public offer" and falls under SEBI's jurisdiction.
- **Substance Over Form:** The Court looked past the name "OFCD" and recognised it as a security subject to SEBI's investor protection norms.
- **Restitution:** The Court ordered Sahara to refund the entire amount with 15% interest and tasked SEBI with the monumental job of verifying and repaying 3 crore investors.

### **Price Waterhouse v. SEBI (Satyam Scandal)**

Following the Satyam fraud (2009), SEBI barred Price Waterhouse (PW) from auditing listed companies. PW challenged this, arguing that only the ICAI has jurisdiction over auditors.

#### **Judicial Outcome:**

- The Bombay High Court and SAT upheld SEBI's jurisdiction, ruling that if an auditor's negligence or connivance leads to the publication of false accounts, it constitutes "fraud" affecting the securities market.
- However, the SAT later emphasised that for SEBI to exercise this power, it must prove "intent and knowledge" (mens rea) and that the action must be "preventive or remedial" rather than purely punitive.

### **Clariant International Ltd. v. SEBI**

This case reinforced the protection of minority shareholders during takeovers. The Supreme Court held that shareholders are entitled to interest on the offer price if the acquirer delays the public announcement. This ensures that retail investors are compensated for the "loss of interest" and the delay in receiving liquidity for their shares.

## **9. Challenges in Protecting Retail Investors**

Despite the successes, the "digital-first" market has created new frontiers that test the limits of regulatory enforcement.

### **The Rise of "Finfluencers" and Social Media Fraud**

Social media has decentralised financial advice. "Finfluencers" with millions of followers often promote stocks without being SEBI-registered.

- **Pump-and-Dump:** Influencers buy a stock, promote it to their followers ("the pump"), and sell when the price rises ("the dump"), leaving retail followers with devalued shares.
- **Survey Data:** A 2025 survey found that 8% of retail investors reported being duped by influencer advice, and 63% of influencers failed to disclose sponsorships.

### **The Restitution Gap**

A significant legal problem researched is the "missing link" in investor restitution. While SEBI collects hundreds of crores in disgorgement, returning this money to the specific victims is procedurally difficult.

- **Discretionary Payouts:** Compensation from the IEPF is often discretionary rather than mandatory.
- **Identification Hurdles:** Quantifying the exact loss of each retail investor in a market-wide fraud is a "daunting—often impossible—task" for the current system.

### **Pre-Investment Scams and Technological Sophistication**

Many frauds now happen "before the gate." Fake trading apps lure investors into depositing money into personal bank accounts rather than regulated brokerage channels. These activities often fall outside SEBI's traditional perimeter because the victim never actually interacts with a registered intermediary.

## 10. Suggestions and Recommendations

To solve the identified legal problems and strengthen the protective aegis, the following solutions are proposed:

### Adoption of a US-Style "Fair Fund" Mechanism

In the United States, the Sarbanes-Oxley Act allows the SEC to pool civil penalties and disgorged profits into a "Fair Fund" to be distributed to victims.

- **Proposal:** India should amend the SEBI Act to create a mandatory "Restitution Fund." This would move away from the "discretionary" nature of the IEPF and ensure that any money recovered from a wrongdoer is primarily used to compensate the specific investors who were harmed by that transaction.

### Legislative Strengthening of Restitution Rights

Currently, the law does not provide an automatic right to compensation for victims of market manipulation.

- **Solution:** Amend the SEBI Act, SCRA, and Depositories Act to embed a statutory right to compensation. This would provide clearer eligibility criteria and simpler processes, possibly integrated with the SCORES 2.0 and ODR platforms.

### Removing the "Defaulter" Trigger for IPF

The Investor Protection Fund (IPF) at exchanges currently only pays out if a broker is declared a "defaulter".

- **Solution:** Expand the scope of the IPF to include losses from any securities fraud or market manipulation, regardless of the broker's solvency status. This would provide a safety net for retail investors caught in systemic market excesses.

### AI-Driven Social Media Monitoring and Removal Powers

To combat "finfluencer" fraud, SEBI needs faster enforcement.

- **Solution:** Grant SEBI the legal authority to order the "immediate removal" of misleading financial content from social media platforms. The "Sudarshan" AI tool should be integrated with platform-level APIs to flag and block unregistered investment advice in real-time.

### Multi-Metric Materiality for Corporate Governance

To prevent "phantom" Related Party Transactions that extract value from minority shareholders, SEBI should refine the materiality threshold.

- **Solution:** Move from a single metric (turnover) to a multi-metric approach (consolidated revenues, assets, or net worth) to define material RPTs, ensuring that even "low-value but recurring" transactions are scrutinised by audit committees.

### Conclusion

The role of SEBI in protecting retail investors has transformed from a passive oversight function to a proactive, technologically-driven guardianship. Through the enforcement of the SEBI Act, the rigorous disclosure requirements of the LODR, and the persistent surveillance of market abuses, SEBI has fostered an environment where over 150 million retail accounts now participate in the nation's economic growth. The upgrade to SCORES 2.0 and the integration of Online Dispute Resolution demonstrate a commitment to timely and efficient justice for the small investor.

However, the "restitution gap" remains the final hurdle. For investor protection to be complete, the regulator must transition from merely "punishing the wrongdoer" to "restoring the victim". The proposed shift toward a US-style Fair Fund mechanism and the removal of procedural barriers like the "defaulter trigger" for compensation are essential steps toward a more equitable market. As India moves toward a T+0 settlement cycle and higher levels of digital participation, the continuous evolution of SEBI's regulatory and technological strategies will be the defining factor in maintaining the trust and integrity of the world's most dynamic capital market.

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