

# INVESTOR ALERT

[Quarterly Newsletter of CREAT focusing on Investor Education and Protection]



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## SEBI AND ITS ROLE IN INVESTOR PROTECTION

The decade of the 1980's witnessed a phenomenal growth and development. For the first time the Indian securities market, demonstrated its potential not only to mobilize the savings of the house-hold sector but also to allocate it with some degree of efficiency for industrial development. By the end of the decade, the securities market emerged into the main stream of the financial system of the country, signifying one of the major economic processes of the decade of the 1990s.

There were notable changes in the capital structure of the companies across industries, new intermediaries and institutions were established in the securities market and a new awareness and interest in investment opportunities in the securities market were created among investors. In spite of these developments and the quantitative expansion of the market, its quality lagged far behind and there was absence of adequate professionalism and fair competition among the various players in the market. Besides, the regulatory framework then prevailing was fragmented, which made regulatory supervision and its enforcement difficult if not ineffective.

The Government therefore, felt

the need for setting up of an apex body for the first time, exclusively for investor protection and for the promotion of orderly and healthy growth of the securities market and constituted the Securities and Exchange Board of India on April 12, 1988. After the promulgation of the Securities and Exchange Board of India Ordinance on January 30, 1992,



SEBI was established as a statutory body on February 21, 1992.

The market development is predicated on a sound regulatory framework. The role of a regulatory body for securities market in a country is determined by the stage of development of securities market in the country. In the Indian context, having regard to the emerging nature of the market, the regulatory body must necessarily have the twin role of development and regulation. SEBI's efforts has always been to create an effective surveillance mechanism for the securities market, and encourage responsible and an accountable autonomy on the

part of all players in the market, who should discipline themselves and observe the rules of the game. This would be possible, if the intermediaries set themselves up as effective self-regulatory bodies. Self-regulation is therefore the cornerstone of the regulatory framework advocated by SEBI, which like management by exception would result in regulation by exception.

The SEBI Act has empowered SEBI to regulate the business of stock exchanges and all financial intermediaries associated with the securities market such as stock broker, merchant bankers, portfolio managers, underwriter's debentures trustees, and share transfer agents, registrars to issue and bank to issue. The Mutual Funds are also regulated by SEBI. The Act has also empowered SEBI to prohibit insider trading. Substantial acquisitions of shares and take over of companies are also regulated by SEBI. Since its becoming statutory body, SEBI has carried out wide ranging reforms in primary and secondary markets which seek to improve the market efficiency and provide greater degree of protection to the investor.

Inequitable and unfair practices such as insider trading effects the integrity, fairness and efficiency of the security market and impair the confidence of the investors. Regulations have been notified for the first time for prohibiting Insider trading and making a

**Continued page-2**

### INSIDE >>>>

Investing in Derivatives	- 3
Investment in Mutual Funds	- 4

**Continued page-2**



criminal offence under the SEBI Act. In the primary market, merchant bankers are the key intermediaries in issue management. They have been brought under the regulatory purview and capital adequacy norms, code of conduct, due diligence tests and capital adequacy norms, code of conduct, due diligence tests and allocation of responsibilities have been introduced for the merchant bankers to make them accountable. Portfolio managers, registrars to issues and other intermediaries critical in the issue management are also authorized and regulated by SEBI.

As a part of the liberalization process, the erstwhile requirement of approval of issuers to raise capital from the market through the Controller of Capital Issues was abolished and access to the market made easier; the pricing of the securities made free from any control. SEBI issued guidelines for disclosure and Investor Protection which the issuers have not to conform for raising capital from the market. These guidelines ensure that adequate disclosures are made by the issuers in prospectuses and offer documents so that the investor can make an informed investment decision. The prospectuses and all offer documents are vetted by SEBI before an issue is made. An advertising Code for public and right issue have also been introduced by SEBI to ensure fair and adequate disclosures to the investors.

Besides these, SEBI had also instituted an in-house system of direct redressal investor grievances. As a part of its developmental role and investor protection, SEBI has encouraged the formation of investor associations across the country to promote greater awareness among the investors. It also seeks to enlighten investors through various advertisements and programs on investor education and guidance.

In the secondary market, SEBI has taken a number of measures to improve the functioning of the stock exchanges as effective self regulatory organizations with a greater degree of accountability so that they can play a greater role in regulating the members, making them directly accountable for their actions and help them in maintaining ethical standards. It is continuously encouraging to stock exchanges for strict enforcement of their own rules and regulations. Trading hours on the stock exchanges have been increased, settlement cycles shortened, greater transparency introduced in the broker client relationship and capital adequacy norms laid down for brokers. Corporate memberships have been introduced on the stock exchanges and the governing boards of the stock exchanges

restructured to make them function with greater degree of autonomy and independence.

Mutual funds have now been allowed in the private sector and we have 26 mutual funds in the country both in the public and private sectors including the Unit Trust of India which is the oldest mutual fund in the country. Increasingly, the mutual funds are being encouraged to be the route for the small investor to access the capital market. Structural changes have been introduced to bring about a greater degree of accountability of the mutual fund and the disclosure standards of the mutual fund in the offer document, and NAV have been introduced for greater investor protection.

Takeover of companies is increasing and regulations are being framed for substantial acquisition of shares and takeover of companies to ensure that the process of takeover is fair, transparent and equitable to all the concerned parties and provides equality of opportunity and time to the shareholders to arrive at an informed decision.

Although reforms have been carried out in a number of areas, we are aware that there is a need and scope for further reforms. The stock exchanges have to be fully automated, and there is a need to link the 21 stock exchanges across the country. Besides, they have to be brought close to the investor and their access to them made easy. Settlement cycles would have to be further shortened to ensure efficient and faster settlement of trade. The market surveillance has to be stepped up to ensure integrity of markets. Trading in derivatives which is a critical constituent of a matured market would have to be introduced and we are moving in this direction. Depository institutions would have to be established and encouraged so that we can move in the direction of immobilization, and dematerialization with DVP arrangements in phases.

SEBI is a member of the International Organization of Securities Commissions (IOSCO). The regulatory standards and principles of IOSCO have been enshrined in the policies and the regulations framed by SEBI for ensuring harmonization of regulations which is very essential in the context of India's opening up to the global markets.

**(Source: Consumer Protection, October-1994)**

## Dos and Don'ts for Investors

### Issue of Securities

#### **Dos**

- Read the Prospectus / Abridged Prospectus and carefully note:
- Risk factors pertaining to the issue.
- Outstanding litigation and defaults, if any.
- Financials of the issuer.
- Company history.
- Background of promoter.
- Instructions before making applications. | In case of any doubt/ problem, contact
- The compliance officer named in the offer documents.
- In case you do not receive physical certificates/ credit to demat account or application money refund, lodge a complaint with compliance officer of issuer company and post issue lead manger as stated in the offer document

#### **Don'ts**

- Do not fall prey to market umours.
- Do not go by any implicit/ explicit promise made by the issuer or any one else.
- Do not invest based on bull run of the market index/ scrips of other companies in same industry/ issuer company.
- Do not bank upon the price of the shares of the issuer company to go up in the short run.

### **Investing in Derivatives**

#### **Dos**

- Go through all rules, regulations, bye-laws and disclosures made by the exchanges.
- Trade only through Trading Member (TM) TM registered with the exchange.
- While dealing with an authorized person, ensure that the contract note has been issued by the TM of the authorized person only.
- While dealing with an authorized person, pay the brokerage/ payments/ margins etc. to the TM only.
- Ensure that for every executed trade you receive duly signed contract note form your TM highlighting the details of the trade along with your unique client-id.
- Obtain receipt for collateral deposited with Trading Member (TM) towards margin.
- Go through details of Client Trading Member Agreement.
- Know your rights and duties vis-à-vis those of TM? Clearing Member
- be aware of the risk associated with your positions in the market and margin calls on them.
- Collect/ pay mark to market margins on your futures position on a daily basis from/ to your Trading member.

#### **Don'ts**

- Do not start trading before reading and understanding the Risk Disclosure Documents.
- Do not trade on any product without knowing the risk and rewards associated with it.

### **Collective Investment Scheme (CIS)**

#### **Dos**

- Before investing ensure that the entity is registered with SEBI.
- Read the offer document of the scheme especially the risk factors carefully.
- Check and verify the background/ expertise of the Promoters.
- Ensure clear and marketable title of the property/ assets of the entity.
- Ensure that the Collective Investment Management Company (CIMC) has the necessary infrastructure to carry out the scheme.
- Check the credit rating of the scheme and tenure of the rating.
- Check for the appraisal of the scheme and read the brief appraisal report.
- Read carefully the objects of the scheme.
- Check for the promise vis-à-vis performance of the earlier schemes in the offer document.
- Ensure that CIMC furnishes a copy of the Annual Report within two months from the closure of the financial year.
- Note that SEBI cannot guarantee or undertake the repayment of money to the investors.

#### **Don'ts**

- Do not invest in any CIS entity not having SEBI registration.
- Do not get carried away by indicative returns.
- Do not invest based on market rumours.

## Dealing with Brokers & Sub-brokers

### **Dos**

- Deal only with SEBI registered intermediaries.
- Ensure that the intermediary has a valid registration certificate.
- Ensure that the intermediary is permitted to transact in the market.
- State clearly who will be placing orders on your behalf.
- Insist on client registration form to be signed by the intermediary before commencing operations.
- Enter into an agreement with your broker or sub-broker setting out terms and conditions clearly.
- Insist on contract note/confirmation memo for traders done each day.
- Insist on bill for every settlement.
- Ensure that broker's name, trade time and number, transaction price and brokerage are shown distinctly on the contract note.
- Insist on periodical statement of accounts.
- Issue cheques/drafts in trade name of the intermediary only.
- Ensure receipt of payment/deliveries within 48 hours of payout.
- In case of disputes, file written complaint to intermediary/ stock exchange/ SEBI within a reasonable time.
- In case of sub-broker disputes, inform the main broker about the dispute within 6 months.
- Familiarize yourself with the rules, regulations and circulars issued by stock exchanges/SEBI before carrying out any transaction

### **Don'ts**

- Do not deal with unregistered intermediaries.
- Do not pay more than the approved brokerage to the intermediary.
- Do not undertake deals for others.
- Do not neglect to set out in writing, orders for higher value given over phone.
- Do not sign blank delivery instruction slip(s) while meeting security pay in obligation.
- Don't accept contract note/ confirmation memo signed by any unauthorized person.
- Don't delay payment/ deliveries of securities to broker/sub-broker.
- Don't get carried away by luring advertisements, if any.
- Don't be led by market rumors or get into shady transactions

## Investing in Mutual Funds

### **Dos**

- Read the offer documents carefully before investing.
- Note that investment in Mutual Funds June be risky.
- Mention your bank account number in the application form.
- Invest in a scheme depending upon your investment objective and risk appetite.
- Note that Net Asset Value of a scheme is subject to change depending upon market conditions.
- Insist for a copy of the offer document/key information memorandum before investing.
- Note that past performance of a scheme is not indicative of future performance.
- Past performance of a scheme may or may not be sustained in future.
- Keep track of the Net Asset Value of a scheme, where you have invested, on a regular basis.
- Ensure that you receive an account statement for the money that you have invested.
- Update yourself on the performance of the scheme on a regular basis.

### **Don'ts**

- Do not invest in a scheme just because somebody is offering you a commission or other incentive, gifts etc.
- Do not get carried away by the name of the scheme/Mutual Fund.
- Do not fall prey to promises of unrealistic returns.
- Do not forget to take note of risks involved in the investment.
- Do not hesitate to approach concerned person and then the appropriate authorities for any problem.
- Do not deal with any agent/ broker dealer who is not registered with Association of Mutual Funds in India (AMFI).

### **Awareness Program on Investor Protection**

The Second awareness program on Investor Protection was held on 21st February 2008 at Hotel V.T.Paradise, Bengaluru. More than 60 Participants attended the program. Resource persons from M/s.Wealthmax Management, Bengaluru,made presentations on Investor Grievance Mechanism in SEBI and also on Mutual Funds. These presentations were followed by discussion and a brief question - answer session . The highlight of the program was that this was the first time that representatives of consumer organizations from all over karnataka were provided with an oppurtunity to know about investor rights, investor protection , stock market operations etc.,



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