REPORT OF THE EXPERT COMMITTEE

CONSTITUTED BY THE HON'BLE SUPREME COURT OF INDIA

VIDE ORDER DATED MARCH 2, 2023

REPORT DATED MAY 6, 2023

INDEX

EXECUTIVE SUMMARY AND PREFACE

1. On January 24, 2023, a report came to be published by Hindenburg Research[1] (*hindenburgresearch.com*) on the Adani Group, with a sensational title: "*Adani Group: How The World's 3rd Richest Man is Pulling the Largest Con In Corporate History*", leading to a few writ petitions being filed as public interest litigation.

2. Dealing with the petitions, in an order dated March 2, 2023, the Hon'ble Supreme Court directed the Securities and Exchange Board of India to investigate the following aspects, and to file a status report within two months:-

   a. Whether there has been a violation of Rule 19A of the Securities Contracts (Regulation) Rules 1957 ("**SCRR**");

   b. Whether there has been a failure to disclose transactions with related parties and other

[1] Hindenburg Research describes itself on its website as a research firm that specialises in "forensic financial research". The firm claims to uncover "hard-to-find information from atypical sources" and in particular, purports to seek out situations where companies may have a combination of accounting irregularities, bad actors in management, undisclosed related party transactions, illegal / unethical business or financial reporting practices and undisclosed regulatory, product or financial issues.

relevant information which concerns related parties, to SEBI, in accordance with law; and

c. Whether there was any manipulation of stock prices in contravention of existing laws.

3. This Committee was constituted as an 'Expert Committee' and SEBI was directed to keep this Committee apprised about its investigations. The remit of the Committee was set out as follows:-

a. To provide an overall assessment of the situation including the relevant causal factors which have led to the volatility in the securities market in the recent past;

b. To suggest measures to strengthen investor awareness;

c. To investigate whether there has been regulatory failure in dealing with the alleged contravention of laws pertaining to the securities market in relation to the Adani Group or other companies; and

d. To suggest measures to:-

i. strengthen the statutory and/or regulatory framework; and

ii. secure compliance with the existing framework for the protection of investors.

4. The Committee asked for a detailed factual briefing from SEBI to be apprised of its investigations. The Committee felt it would be fruitful to also seek inputs from market participants on the various larger facets within its remit. Based on the briefings received, review of the material on record, and the remit of the Committee, it was felt necessary to also seek inputs from the Directorate of Enforcement, the Central Board of Direct Taxes and the Investor Protection and Education Fund Authority for briefings.

5. The Committee is pleased to present its report dated May 6, 2023. This Executive Summary aims to give a snapshot of the findings and observations of the Committee including the measures it suggests, wherever the same has been sought.

On Volatility:

6. Volatility is not an inherent vice for the market. Market participants place buy and sell orders in line with their demand and supply, and based on their assessment and expectations, which is in turn, based on their assessment of information available to them, and its anticipated impact.

7. It is seen empirically that the Indian market was not unduly volatile as is seen from a comparison of the Indian volatility index (India VIX) with the CBOE volatility index (CBOE VIX). There was certainly high volatility in the Adani stocks after publication of the Hindenburg Report. The market's expectations from, and confidence in the Adani Group was shaken by the allegations in the Hindenburg Report, which was inferential. Although based on publicly available information, it questioned the foundational premises on which the market had priced Adani stocks.

8. The mitigating measures from the Adani Group such as paring down the debt secured by encumbrances on their shareholding, infusion of fresh investment into Adani stocks by way of investment of nearly USD 2 billion by a private equity investor and the like, built confidence in the stocks.

9. The market has re-priced and re-assessed the Adani stocks. While they may not have returned to the pre-January 24, 2023 levels, they are stable at the newly re-priced level.

10. Empirical data shows that retail investors' exposure to the Adani stocks has increased after January 24, 2023.

11. The Committee concluded, based on empirical evidence, that the Indian market as a whole was not unduly

volatile during the period under reference. The volatility in the Adani stocks was indeed high, which is attributable to the publication of the Hindenburg Report and its consequences.

On Investor Awareness:

12. Between 2019 and 2022:-

a. Out of the total trading by individuals in the cash segment, approximately 67% by value is by way of intra-day trades and only 33% results in delivery of shares;

b. Total number of unique individual traders who traded through the top ten brokers in equity F&O segment has increased by over 500% in FY22 as compared to FY19;

c. Approximately 88% of the individual traders were active traders.

d. 89% of the individual traders (i.e. 9 out of 10 individual traders) in equity F&O segment incurred losses, with an average loss of Rs. 1.1 lakh during FY22; and

e. Despite such losses, share of individuals in total F&O turnover is very high – during the last four years, it has been around 27-29%.

13. The Committee notes that SEBI has recognised the increasing number of intra-day traders who are coming into the market and the need to alert and inform them in advance of their trades. SEBI has identified areas that need attention and has briefed the Committee on its plan to address these areas. The Committee agrees with steps proposed in this regard, and suggests implementation as early as possible in a time-bound manner.

14. The securities market is meant to function on the premise of investors making informed decisions. Increasingly, the stock trading is almost entirely digital even at the consumer's end, and it should be possible to make relevant and pertinent information easy to access at the point of transaction, including information about the issuer of the security that is being transacted in, as well as information on regulatory caution attached to such securities.

15. The Indian securities market works on a disclosure-based regime. Disclosures are mandated at the time of issue of capital as well as continuously during the time the securities are listed for trading.

16. There is an urgent need to introspect and take a hard close look at whether there is a surfeit of disclosures that loads the investors with so much data and noise

that the real content necessary to make an informed decision may be lost.

17. The government needs to bring sharp focus to the area of unclaimed properties such as securities, dividends and bank deposits belonging to deceased investors. The entire process requires an imaginative re-engineering. This would be best served by creating a Central Unclaimed Property Authority to handle and reunite unclaimed private assets to the successors of deceased investors. Such an agency has to be a full-time hands-on real time proactive agency that actively seeks out to discharge a mandate of reuniting assets of dead individuals with their successors.

18. The Committee believes that financial literary must be introduced as a matter of pedagogy right from school curriculum. Financial security of a society is as vital as national security for a society to be robust. School and university curricula must be attuned to bring in a culture of financial awareness and literary. Earning, saving, investing, earning returns, and giving back to society, are part of a virtuous cycle. The era of treating money with an unstated element of stigma must end.

19. The Committee has suggested specific measures that must be adopted in the chapter dealing with this subject.

On Regulatory Failure:

20. The three areas of investigation into alleged violations, explicitly spelt out in the Hon'ble Supreme Court's order dated March 2, 2023, are:

    a. Minimum Public Shareholding;

    b. Disclosure of transactions with related parties in accordance with law; and

    c. Stock price manipulation

Minimum Public Shareholding

21. The issue of minimum public shareholding is dependent on whether 13 overseas entities including 12 foreign portfolio investors ("**FPIs**") are compliant with disclosure of their beneficial owners, as stipulated by law. The Report deals with the law governing the subject and SEBI's reading of the law, in detail.

22. SEBI (FPI) Regulations, 2014 ("**FPI Regulations**") had mandated a requirement to disclose the ultimate beneficial ownership by natural persons above the FPI. This was part of a provision that dealt with "opaque structures" in ownership of FPIs. In any case, the declaration of the "ultimate beneficial owner" under SEBI Regulations was required to conform to the disclosure of "beneficial owner" under the Prevention of

Money Laundering Act, 2002 ("**PMLA**") and thereby under Rule 9 of the Prevention of Money Laundering (Maintenance of Records) Rules, 2004 ("**PMLA Rules**").

23. Three facets are clear:-

a. First, the FPIs in question have made declarations of the beneficial owner by identifying the natural persons controlling their decisions for purposes of the PMLA. This is the declaration that comports to compliance with the FPI Regulations;

b. Second, the very requirement to disclose the last natural person above every person owning any economic interest in the FPI was done away with in 2018 pursuant to a recommendation of a Working Group and the provisions on "opaque structure" were deleted on the premise that declarations under the PMLA constitute sufficient compliance; and

c. Third, SEBI has been investigating the ownership of the 13 overseas entities since October 2020 despite the aforesaid legislative change that had been effected in 2018.

24. The foundation of SEBI's suspicion that led to investigations into the overseas entities' ownership is that they have "opaque" structures because the ultimate chain of ownership above the 13 overseas entities is not

clear. SEBI has found 42 contributories to the assets under management of the 13 overseas entities. Various avenues have been pursued – including the Directorate of Enforcement, Central Board of Direct Taxes and various securities market regulators in the seven jurisdictions where the 42 contributories are situated. SEBI has drawn a blank.

25. What is evident is that all along, the legislative policy of SEBI under the FPI Regulations requiring disclosure of beneficial owner was in consonance with the requirements under the PMLA. Besides, in 2018, the very provision dealing with "opaque structure" and requiring an FPI to be able to disclose every ultimate natural person at the end of the chain of every owner of economic interest in the FPI, was done away with.

26. Yet, in 2020, the investigation and enforcement has moved in the opposite direction, stating that the ultimate owner of every piece of economic interest in an FPI must be capable of being ascertained. It is this dichotomy that has led to SEBI drawing a blank worldwide, despite its best efforts.

27. Without such information SEBI is unable to satisfy itself that its suspicion that has been aroused can be put to rest. The securities market regulator suspects wrongdoing, but also finds compliance with various

stipulations in attendant regulations. Therefore, the record reveals a chicken-and-egg situation.

28. In these circumstances, the Committee is of the view that it would not be possible to return a finding of a regulatory failure in relation to compliance with the regulatory stipulations governing minimum public shareholding stipulation. There indeed has to be a coherent enforcement policy, which is dealt with in Chapter Five.

Related Party Transactions

29. At the heart of the allegations about disclosure of alleged related parties and transactions with them is the definition of the terms "related party" and "related party transaction". Both these terms have been amended by SEBI substantially in November 2021 and with a deferred prospective effect – with some changes taking effect on April 1, 2022 and others on April 1, 2023. India has among the widest definition of these terms across jurisdictions.

30. Transactions by related parties with subsidiaries of listed companies and transactions with unrelated third parties that are intended and purposed to benefit a related party have been explicitly brought into the fold. While amendments were made in November 2021, they were given deferred effect to enable companies to re-arrange their affairs to become compliant with the law.

Providing a deferred effect to enable society to re-arrange affairs provides a "glide path", which is good practice in economic legislation, where disruptive changes must not hurt the ease of appreciating what is expected of members of society.

31. One regulatory approach would have been to test such structures on the strength of the unamended regulations. Section 12A of the SEBI Act, 1992 outlaws contrivances and devices that are structured to circumvent the law – in effect, a framework against anti-avoidance. Another regulatory approach is to make amendments to spell out what would be covered by the legal requirements.

32. The exercise of choice among these two approaches is SEBI's prerogative in its legislative capacity, and an expression of its best judgement of what is appropriate policy. So long as there is nothing unreasonable or subversive in choosing one path over the other, there is no scope for an adverse comment on the approach or to arrive at a finding of a "regulatory failure".

33. Having adopted the path of making explicit stipulations prospectively, the feasibility of testing the principles underlying the regulations governing related party transactions has been eroded.

Further Investigations

34. In any case, on both counts – minimum public shareholding and related party transactions – SEBI is seeking more time to to effect more investigations. This is matter between SEBI and the Hon'ble Supreme Court.

35. SEBI has also identified 13 specific transactions where it is investigating the underlying transactions regardless of whether the transactions are legally considered "related party transactions" from the standpoint as to whether or not these transactions were fraudulent. SEBI is actively engaged in collecting data on these transactions. The Committee would therefore be unable to comment without further input, except to say the investigations must be completed in a time-bound manner in accordance with law.

36. The Committee has restricted itself to its stated remit – of ascertaining whether there has been a regulatory failure. The Committee is of the view that it would not be possible to return a finding of a regulatory failure in the context of the regulations prevailing when the transactions were effected. There indeed has to be a coherent enforcement policy, which is dealt with in Chapter Five.

Price Manipulation

37. SEBI has explained its approach to dealing with the various automated alerts that are thrown up by the trading system, how they are generated, and how they are analysed and investigated for potential market abuse and price or volume manipulation.

38. From the alerts generated by the algorithm that mines the traded data, the information is analysed based on set criteria including:-

a. Concentration of net buyers/ net sellers in the scrip;

b. Contribution of net buyers to the increase in Last Traded Price ("**LTP**") during a price rise period and contribution of net sellers during price fall period;

c. Whether any group of entities traded among themselves, which might have led to increase/ decrease in the price of the scrip;

d. Whether delivery was taken by the entities in a scrip and what proportion of deliveries were taken vis-a-vis their trading volume in that particular scrip;

e. Trading behavior of the top LTP contributors in a particular scrip vis-a-vis their trading behavior across all other scrips;

f. Category of entities appearing in the top net buyers, net sellers and net LTP contributors e.g.

Sovereign Wealth Funds, Mutual Funds, brokers, individuals, etc.;

g. Whether the trading entities profited or incurred losses from the trades;

h. Concurrent corporate announcements or news flows about the company, triggering positive or negative sentiment in the scrip;

39. If the trading pattern appears to be suspicious based on the aforesaid criteria, further examination is conducted. If the trading pattern does not arouse suspicion, then the alerts are closed.

40. In the case of the Adani stocks, 849 alerts were generated by the system, and were considered by stock exchanges resulting in four reports to SEBI – two well prior to the Hindenburg Report and two after January 24, 2023.

41. SEBI has explained the analysis done, taking the example of Adani Enterprises Ltd., breaking the trading data into four "patches" (periods of time) where the stock price rose significantly.

42. The report sets out the detail of the analysis across the multiple patches. In a nutshell, no pattern of artificial trading or "wash trades" among the same parties multiple times was found. In one of the patches where the price rose, the FPIs under investigation were net

sellers. One investing entity that had purchased across the patches had purchased far more of other securities. In a nutshell, there was no coherent pattern of abusive trading that has come to light.

43. SEBI has also found that some entities have taken short positions prior to the publication of the Hindenburg Report and have profited from squaring off their positions after the price crashed upon publication of the report.

44. All of these are still under investigation and the Committee therefore does not express any opinion on merits. Suffice it to say, it would not be possible to return a finding of regulatory failure on this count since SEBI has an active and working surveillance framework to take notice of high price and volume movements and has applied itself to the data generated by such surveillance, applying objective criteria, to consider if the integrity of the natural price discovery process has been manipulated.

On Suggested Strengthening Measures:

45. SEBI is well empowered and has been conferred with robust powers ranging from licensing of intermediaries to legislative, executive and quasi-judicial powers to discharge its role. The Committee does not perceive a need to confer even more powers on SEBI at this stage.

46. The Committee believes the regulator must be well structured and its own governance must be well thought through. Effective measures to ensure greater transparency in law-making, greater societal involvement in contributing to the law, and consequently greater acceptance and compliance with the regulations, should be the focus.

47. There is a need to develop a proper enforcement policy that would optimise the utilisation of precious regulatory resources on the field. There is a sharp increase in proceedings initiated by SEBI over the years.

48. The increase in proceedings initiated begs the need to empirically study how settlement of proceedings can be made an effective and viable alternative. There is an unstated perception of reluctance to settle potential proceedings arising from causes of action identified. SEBI has formulated empirical criteria for computing the quantum of settlement amount and there should be very little scope to not be objective about the terms of settlement.

49. An effective enforcement policy would mean laying down criteria on the basis of which SEBI may choose whether to initiate proceedings and what type of proceedings to initiate, in a clear, reasoned and non-arbitrary fashion. Enforcement must also be consistent with the legislation and policy stance of SEBI.

50. It is seen from judgments in SEBI matters that at times, different officials adjudicate the same issue differently. Judicial discipline is a must. Unless the ratio laid down by one adjudicating official has been upset or re-stated in appeal, it should be followed by others dealing with later cases. Likewise, once a ruling is set aside in appeal, unless the appellate order is stayed by the Hon'ble Supreme Court or a writ court, future adjudication by SEBI must abide by the law declared by the appellate order.

51. SEBI must adopt (as indeed any regulator) a firm timeline for initiation of investigations, completion of investigations, initiation of proceedings, disposal of settlement, and disposal of proceedings. This must be embedded into the law. Needless to say, elements of such a timeline may be directory and other elements may be mandatory (as with any economic legislation) but a complete absence of timelines in the law is a stark feature that needs correction.

52. The regulatory objective of SEBI may be better served by timely and sharp action in a few large and complex cases as compared with frittering energy and resources in thousands of tiny cases. Every single case has a consequence but for a regulator to achieve its objective, it has to be strategic on how best it can prosecute cases of serious significance.

53. As regards surveillance and administrative actions, such as inclusion of stock-specific derivatives, the element of human intervention must be brought down to the bare minimum and to the core strategic elements.

54. Some wider structural changes that are apt have already been recommended by working groups and committees in the past. This Committee does not intend to elaborate upon and repeat the merits of these. Such recommendations have already been well articulated with serious intellectual resources having been expended in recommending such changes (such as recommendations of the Financial Sector Legislative Reforms Commission). Some of these measures that need specific attention for implementation are:-

a. The creation of a Financial Redress Agency that handles investor grievances across sectors. This could be a first step to an eventual unified regulator, but at the least, it is vital to implement a central redress agency that can focus on investor grievance redressal across sectors. At the enterprise level, the service providers are mostly one unified economic enterprise and at the consumer level, the investor is the same. The types of abuse could be replicated across sectors by the common enterprise, but grievance redressal for the investor is split across regulators working in silos;

b. The process for recovering unclaimed private property is also spread across agencies – different for securities and monies connected to securities, and different for bank deposits. The same successor in title to the same deceased person has to engage with multiple agencies. This anomaly has to be addressed on a war footing;

c. In complex enforcement matters, where the skill-set and expertise of multiple regulatory and enforcement agencies would be necessary, it would be vital to have a framework by which a multi-agency committee ("**Investigating Committee**") with a temporary shelf life (just what is required for investigating that particular case). Such a committee may be set up by the Government of India under the aegis of the Financial Stability and Development Council. At the end of the investigation, with the initiation of appropriate proceedings, such a committee must be disbanded. The framework being suggested must stipulate criteria by which a case may be referred to such an Investigating Committee, by designating it as a "systemically important investigation". The Government must be able to resort to such a framework only when the case involved has serious cross-sectoral repercussions

and would need multi-disciplinary skill sets to be brought to bear in a coordinated manner.

d. Within SEBI (as indeed any other regulator), the doctrine of separation of powers must be followed in letter and spirit. The quasi-judicial arm of the regulator has to be necessarily ring-fenced from the executive arm so that it is truly a check and balance. If performance of the quasi-judicial officers is appraised by the executive arm, the very foundation of separation of powers would stand nullified.

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CHAPTER ONE

INTRODUCTION AND APPROACH

The Context:

1. On January 24, 2023, a report came to be published by Hindenburg Research[2] (*hindenburgresearch.com*) on the Adani Group, with a sensational title: "*Adani Group: How The World's 3rd Richest Man is Pulling the Largest Con In Corporate History*". Hindenburg claimed to have held short positions in US-traded bonds issued by the Adani Group and non-Indian traded overseas derivatives instruments.

2. The Hindenburg Report set out details of its investigation which could be broadly divided into the following allegations:-

   (a) alleged fudging of compliance with minimum public shareholding requirements with certain foreign

[2] Hindenburg Research describes itself on its website as a research firm that specialises in "forensic financial research". The firm claims to uncover "hard-to-find information from atypical sources" and in particular, purports to seek out situations where companies may have a combination of accounting irregularities, bad actors in management, undisclosed related party transactions, illegal / unethical business or financial reporting practices and undisclosed regulatory, product or financial issues.

portfolio investors classified as public shareholders, being suspected of being fronts for the promoters of the Adani Group;

(b) alleged price manipulation, aided by a suppressed float of shares contributing to lack of depth in trading, making it easy to manipulate the price of these shares;

(c) alleged circumvention of regulations governing related party transactions; and

(d) other miscellaneous attendant allegations.

3. The publication of the Hindenburg Report just preceded the opening of a Rs. 20,000-crore public offering of equity shares by Adani Enterprises Ltd that was scheduled for January 27, 2023. The securities offering had been billed as the largest ever follow-on public offering by any company listed in the Indian securities market.

4. It is now a matter of public record that the price of shares of the listed companies in the Adani Group including Adani Enterprises nose-dived in the aftermath of the Hindenburg Report, with various attendant developments following in rapid succession – ranging from international banks suspending the acceptance of encumbrances over securities issued by the Adani Group to secure their

lending; to review of whether Adani securities should be included in stock indices; to investors who were keen on investing in green energy initiatives placing on hold their intended plans, to name a few.

5. The subscription book for the Rs. 20,000-crore Adani Enterprises securities offering, although built, was shelved pursuant to the sustained fall in stock prices.

6. Multiple writ petitions came to be filed before the Hon'ble Supreme Court of India seeking various reliefs, ranging from seeking investigations into the allegations made by Hindenburg against the Adani Group, and also seeking investigations into the activities and intention of Hindenburg.

7. In its order dated February 10, 2023, the Hon'ble Supreme Court had expressed a view that there was a need to review the existing regulatory mechanisms in the financial sector to ensure that they are strengthened with a view to protect Indian investors from volatilities in the market.

Constitution of this Committee and its Remit:

8. Dealing with the multiple writ petitions, in an order dated March 2, 2023, the Hon'ble Supreme Court directed the Securities and Exchange Board of India ("**SEBI**") to investigate the following aspects, without limiting the

scope of investigation into any other aspect, expeditiously, and to file a status report within two months:-

a. Whether there has been a violation of Rule 19A of the Securities Contracts (Regulation) Rules 1957 ("**SCRR**");

b. Whether there has been a failure to disclose transactions with related parties and other relevant information which concerns related parties, to SEBI, in accordance with law; and

c. Whether there was any manipulation of stock prices in contravention of existing laws.

9. With a view to protect Indian investors against volatility of the kind witnessed in the recent past, the Hon'ble Supreme Court constituted this Committee for the assessment of regulatory failure, if any, and to suggest measures to strengthen the regulatory framework. SEBI was directed to keep this Committee apprised about its investigations.

10. The remit of the Committee was set out by the Hon'ble Supreme Court in Paragraph 15 of its order dated March 2, 2023 as follows:-

a. To provide an overall assessment of the situation including the relevant causal factors which have led

to the volatility in the securities market in the recent past;

b. To suggest measures to strengthen investor awareness;

c. To investigate whether there has been regulatory failure in dealing with the alleged contravention of laws pertaining to the securities market in relation to the Adani Group or other companies; and

d. To suggest measures to:-

i. strengthen the statutory and/or regulatory framework; and

ii. secure compliance with the existing framework for the protection of investors.

Approach of the Committee:

11. The Committee held its first meeting on March 17, 2023. The remit of the Committee having been explicitly set out by the Hon'ble Supreme Court, the Committee noted that it would need specific factual briefing from SEBI to be apprised of its investigations. While the Committee would seek inputs and views from SEBI on all the four facets of the remit of the Committee, it was felt that as regards the

suggestion of measures to strengthen investor awareness; to strengthen the statutory and / or regulatory framework; and to secure compliance with the existing framework for protection of investors, it would be fruitful to also seek inputs from market participants.

12. Accordingly, a written briefing from SEBI was sought in advance and a detailed briefing was scheduled for April 2, 2023 to ensure that SEBI apprises the Committee in line with the Hon'ble Supreme Court's directions.

Committee's Invitees for Inputs:

13. On the facets of the Committee's remit other than facts specific to the Adani Group, the Committee decided to seek written inputs from a few noted individuals of standing in the Indian securities market. These are:-

a. Dr. C.K.G. Nair, Director of the National Institute of Securities Markets;

b. Association of Mutual Funds of India;

c. Mr. Nimesh Kampani, founder of the JM Financial Group;

d. Mr. Vallabh Bhansali, founder of the Enam Group;

e. Mr. Sunil Sanghai, NovaaOne Capital Private Ltd., a merchant banker;

f. Mr. Nithin Kamath, founder Zerodha Capital, stock broker with India's largest retail investor client base.

14. SEBI presented the Committee with a detailed written submission and a presentation deck. The Committee was briefed by Ms. Madhabi Puri Buch, Chairperson, SEBI and SEBI officials on April 2, 2023. The other invitees were invited to present to the Committee at a meeting scheduled for April 6, 2023, on which date, Dr. Nair, Mr. Sanghai and Mr. A. Balasubramaniam, President, Association of Mutual Funds of India made their presentations. Written inputs were also received from Mr. Kampani and Mr. Kamath.

15. The Committee held further deliberations on April 13, 2023 to discuss the inputs received until then, and the remit of the Committee and its precise approach in the light of inputs received from various persons including SEBI. Since SEBI had submitted that it had made references to the Directorate of Enforcement and to the Central Board for Direct Taxes, it was decided to seek inputs from these two agencies too to explain their views to the Committee on the subjects referred to them. Since suggestion of measures to improve investor awareness is part of the remit of the Committee, it was felt necessary to

interact with the the Investor Education and Protection Fund Authority as well.

16. The Committee then met on April 26, 2023 and on April 27, 2023 to interact with these agencies, and have a follow-up interaction with SEBI. Presentations were made by:-

a. Mr. Sanjay Kumar Mishra, Director, Directorate of Enforcement;

b. Ms. Anita Shah Akella, CEO, Investor Education and Protection Fund Authority; and

c. Mr. Nitin Gupta, Chairman, Central Board of Direct Taxes.

17. It was felt by the Committee that considering the remit of the Committee extended to facets of systemic measures to be suggested beyond the Hindenburg-Adani controversy and considering the cross-border character of the operations involved, it would be apt to invite international banks and securities firms to present to the Committee. Towards this end, invitations were extended to JP Morgan, Goldman Sachs, Citibank, BankAm Merrill Lynch and Morgan Stanley.

18. It became apparent that none of the international securities firms and banks were desirous of engaging in

the matter. A few of them cited conflict of interest owing to commercial relationships with the Adani Group. Goldman Sachs suggested that the Committee may profit from engaging with the Asia Securities Industry and Financial Markets Association, an industry body, which too disclaimed any expertise or ability to contribute to the Committee.

19. Various written submissions and presentations made by SEBI and the invitees were taken on record. Various documents and records presented by the regulatory and enforcement agencies and indeed the inputs received in writing from other invitees are set out in the Compilation of Submissions, which is a distinct and separate volume. Since the investigations and files involved are still current and this Committee Report having been sought in a sealed envelope, the Committee has decided to mark the Compilation of Submissions too as confidential.

20. The Committee has given its serious consideration to every draft suggestion proposed by SEBI and the invitees. Some of the inputs have been expansive in nature, with some draft suggestions commended for the Committee's endorsement, not strictly being linked to the core context and remit of the Committee. The Committee decided to stick to its remit and also do its best to deal with suggestions received in connection with the same. Each and every submission on recommendations commended

for endorsement is not separately dealt with in an exhaustive manner, taking into account the core remit and objective of the task on hand, and the time available for completing it.

21. At the meeting with SEBI held on April 26, 2023, SEBI presented the current status of its findings on various facets of the allegations, but termed them as *prima facie*. These are dealt with in this report in detail. SEBI indicated to the Committee that it plans to seek an extension of time of one year from the Hon'ble Supreme Court to complete its investigations. After this meeting, the Committee was informed that SEBI had filed an application before the Hon'ble Supreme Court seeking an extension of time of six months. The Committee sought from SEBI and obtained a copy of the application filed by SEBI seeking extension of time.

22. The Committee has decided not to comment on whether further time would be needed or should be granted, since in the Committee's view it is for SEBI to convince the Hon'ble Supreme Court in this regard.

23. Suffice it to say, the Committee has given its active consideration to the detailed briefings that SEBI has provided in the matter and has reviewed the current status as reported to the Committee by SEBI. The Committee has presented its views on the basis of the position made

known to the Committee at this stage based on investigations that have gone on since October 2020. The remit of the Committee under the Hon'ble Supreme Court's order dated March 2, 2023 is clear and the Committee has worked towards discharging its duty within this remit to submit this report.

Structure of this Report:

24. This report is organised in the same sequence as the remit for the Committee set out in Paragraph 15 of the Hon'ble Supreme Court's order dated March 2, 2023. This report is organised in the following structure:-

a. Executive Summary and Preface

b. Chapter One: Introduction and Approach

c. Chapter Two: Volatility Assessment

(responsive to the Committee's remit under Paragraph 15(a))

d. Chapter Three: Investor Awareness

(responsive to the Committee's remit under Paragraph 15(b))

e. Chapter Four: Alleged Contraventions and Regulatory Failure

(responsive to the Committee's remit under Paragraph 15(c))

f. Chapter Five: Regulatory Framework and Compliance – Strengthening Measures

(responsive to the Committee's remit under Paragraph 15(d))

Acknowledgements:

25. The Committee would be remiss if it did not place on record its appreciation for the efforts of two officers – Ms. Surbhi Jain, Joint Secretary, Capital Markets, Department of Economic Affairs, Ministry of Finance; and Mr. Amarjeet Singh, Executive Director, SEBI.

26. Ms. Jain served as the designated Nodal Officer pursuant to the Hon'ble Supreme Court's order dated March 2, 2023. Mr. Singh was designated by SEBI as the all-weather officer that the Committee desired for proper co-ordination and engagement with SEBI to ensure that the Committee indeed receives all that it needs to receive from SEBI.

27. Both these officers have worked extensively through this period of two months to enable the Committee to get information and data sought from SEBI and other agencies and individuals, so that the Committee could form its opinion within the stipulated timeframe.

28. The Committee also desires to place on record its appreciation of the staff in the Registry of the Hon'ble Supreme Court, who have ably assisted the Committee in conduct of meetings smoothly, both in person and online, whether on court-working days, or on weekends.

29. Finally, for completeness, it must be mentioned that the Hon'ble Chairman Justice (Retd.) Abhay Manohar Sapre sought the views of the members about the direction of the Hon'ble Supreme Court to fix remuneration for the members. Every member of the Committee respectfully commended for acceptance, the principle that the role expected of them in this Committee is a matter of public duty and they did not desire to be remunerated for the work done on the Committee. The Committee was unanimous that the work expected of the members was a call of duty and that they would waive the proposal to provide remuneration for the work done.

* * * * *

CHAPTER TWO

VOLATILITY ASSESSMENT

Introduction and Context:

1. Protection from undue volatility in the stock market is one of the prime drivers of the Hon'ble Supreme Court's order dated March 2, 2023. The publication of the Hindenburg Report on January 24, 2023 led to prices of Adani stocks nose-diving in the securities market. For days, the prices kept falling and then resumed rising, but the prices are not at the level they were in prior to January 24, 2023.

2. The gyrations in the stock prices, leads one to ask some pertinent questions. Has the Indian stock market as a whole been volatile due to these developments? Or is the volatility restricted to some select stocks? More pertinently, what precisely is volatility? Is volatility a necessary element in any free market where price discovery is a product of interplay of demand and supply, as influenced by information that affects demand and supply? How volatile has the Indian market been?

3. In this Chapter the Committee investigates these questions and returns specific findings on the situation at hand.

What is Volatility:

4. A plain English meaning of the term "volatile" would be instructive. The term "volatile" has been variously defined as the propensity to change rapidly and unpredictably, usually for the worse. Just two definitions – one from an English dictionary and another from an investment portal – should suffice to give a flavour of what is meant by volatility. They are extracted below:-

Cambridge Dictionary[3]:

*The quality or **state of being** likely to **change suddenly**, especially **by becoming worse**.*

[Emphasis Supplied]

Investopedia[4]:

*Volatility often refers to **the amount of uncertainty or risk related to the size of changes in a security's value**.*

*A higher volatility means that a security's value can potentially be spread out over a larger range of values. This means that the **price of the security can change***

[3] https://dictionary.cambridge.org/dictionary/english/volatility#
[4]https://www.investopedia.com/terms/v/volatility.asp

dramatically over a short time period in either direction.

A lower volatility means that a security's value does not fluctuate dramatically, and tends to be more steady.

[Emphasis Supplied]

5. By inherent character, stock markets are not meant to be still. Market indices see movement every nano-second when the market is open for trading. Intense volatility can be troublesome for investors of all kinds. Yet, some expectation of movement in prices is foundational in how markets function. Impact on stock prices arising from events and developments, is an inherent and inexorable feature of the securities market.

6. Market volatility is the frequency and magnitude of price movements. The bigger and more frequent the price swings, the more volatile the market would be. A statistical tool conventionally used to measure market volatility would be the measurement of "standard deviation", which gives a sense of how much something moves from an average benchmark value. The standard deviation is directly proportionate to the volatility. Greater the deviation from the standard, more the volatility in the price movement. This is where indices too play a role in presenting a benchmark to compare price movements with.

7. Indices are constructed by deriving prices of stocks that are expected to be representative of the market. As the price of the constituent stocks moves, the value of the index would move. Typically, to give a true reflection of the market using the index as a barometer, it would stand to reason that extremely volatile stocks do not form constituents of the index. Therefore, when one looks at indices as a barometer of the market, the inherent expectation would be one of less volatility.

8. A volatility index, popularly known as "VIX" is a measure that has come to be in vogue for markets to measure volatility. The VIX was first created by the Chicago Board Options Exchange ("**CBOE**") in 1993, with an intent to reflect the implied volatility of the S&P 500 index over the next 30 days. This is popularly known as the sentiment index or the fear index, and is calculated using the prices of index options on the S&P 500 index. If the VIX were to rise, it would indicate an increased risk of a decline in the stock market, signalling nervousness among investors. A drop in the VIX translates into expectation of a rise in the stock markets, as lower volatility is associated with lower risk. The National Stock Exchange ("**NSE**") computes an India VIX to measure volatility in the Indian market.

9. Sharp movements in prices of a share, both upward and downward, is reflected in its volatility measure.

Volatility is generally expected to be higher if liquidity in the stock is low. Liquidity is expected to be low if there is low floating stock in these companies. Selling pressures typically builds up based on a combination of factors including short-selling, seriousness and nature of rumours or allegations levelled, news coverage of such developments, announcements by various stakeholders, investors' propensity to adopt measures to play safe, automatic stop-loss triggers leading to even more selling in anticipation of further price drop.

10. It is noteworthy that while volatility can cause fear, it also prompts companies to respond. Volatility is a symptom signal sent to the decision-makers in companies that they need to address some facet of their operations that causes volatility.

11. In the case of the Adani Group, it is a matter of public record that the fall in prices led to the promoter group reducing its borrowings backed by pledge of securities issued by these companies, and indeed a large private equity investor has acquired a substantial equity stake from the promoters of the Adani Group for just short of USD 2 billion. These are reflective of the symptomatic signals and the reactions to the signals.

Volatility and Adani Stocks:

List of Dates and Events – post-Hindenburg Report:

12. A list of dates and events relating to events that would have a direct impact on Adani stocks is set out below:-

Date	Event
January 24, 2023	Hindenburg report on the Adani Group
January 29, 2023	Adani group response, dismissing all allegations.
January 31, 2023	Adani Enterprises FPO subscribed 1.12 times; Abu Dhabi's IHC commits $381m in Adani Enterprises, ~15% of the offering.
February 1, 2023	Swiss lender Credit Suisse Group AG stops accepting bonds from Adani Group companies as collateral for margin loans to its private banking clients.
February 2, 2023	Adani Enterprises calls off its $2.5 billion follow-on public offering
February 6, 2023	Reports emerge that the Adani Group will rein in its spending by half, further triggering the fall in stock value for its listed entities.
February 8, 2023	French firm Total Energies decides to pull out from Adani Group's $50 billion green energy plan.

Date	Event
February 9, 2023	Adani Group abandons its plans to buy a coal plant in India for $850 million.
February 10, 2023	MSCI cuts the free-float status of four Adani firms: Adani Enterprises, Adani Total Gas, Adani Transmission, and ACC. Moody's downgrades ratings outlook of four Adani firms.
February 15, 2023	Adani Group decides to halt its investment in a coal-to-polyvinyl chloride (PVC) plant in Gujarat. The company had planned to spend $4 billion on the project.
February 23, 2023	Fitch Ratings has affirmed the 'BBB-' ratings on the $400m senior secured notes issued by Adani Transmission Ltd.
February 24, 2023	S&P affirms Adani Green's rating at BB+
March 2, 2023	Hon'ble Supreme Court Order
March 2, 2023	US investment firm GQG invests $1.9 billion in Adani companies
March 9, 2023	NSE puts Adani Enterprises, Adani Power and Adani Wilmar under the short-term ASM framework Stage-I
March 10, 2023	Asset sale in Adani Cements worth $450 million, as part of efforts to reduce debt and restore

Date	Event
	investor confidence in his conglomerate. Adani owns 63% of Ambuja Cements.
March 13, 2023	Adani Transmission and Adani Total Gas put under the Stage-II of long-term additional surveillance measures.
March 23, 2023	FITCH Rating affirms ratings for Adani Ports at BBB-1 with stable outlook.
March 27, 2023	AMG Media Networks acquires 49% stake in Quintillion Business Networks.
March 28, 2023	Ken report on non-repayment of USD 2.15 billion loan against shares by Adani Group.

13. The Committee desired to know the representation of the various Adani stocks on any stock index in India. It was found that Adani Enterprises and Adani Ports had minuscule representation in the Nifty-50 (cumulatively 2% on January 24, 2023) while the other Adani stocks had representation in other indices such as the Nifty Next-50, Nifty Midcap 150 and Nifty100 ESG.

14. Therefore, impact of the Adani Group-related events on the overall market was low on account of index weightage being NIL in Sensex-30 and around 2% in Nifty-50. Except for a short blip period of about two weeks since January 24, 2023, the Indian market continued to perform well vis-a-vis the MSCI Emerging

Market Index and the two have recently converged. The Committee examined these facets based on facts presented by SEBI. The Committee also engaged with market participants with experience, and did not restrict its engagement to discussions with the securities market regulator.

15. Data provided by SEBI suggests that after the volatile effect on the Adani Group stocks, participation by retail investors in ownership of these securities has in fact gone up. Such enhanced participation by retail investors would be a classic pointer to markets reacting to price falls – they can lead to a herd mentality of everyone moving in one direction, but they can equally lead to views contrarian to the herd, developing into a countervailing force on price discovery.

16. Between January 24, 2023 and February 27, 2023, the market capitalisation of the Adani stocks saw significant erosion in value terms – around Rs. 12.4 lakh crores. This reduced to around Rs. 10 lakh crore by March 9, 2023. However, deeper analysis of this is warranted. Computation by SEBI shows that:-

a. As on January 24, 2023, all individual investors including "retail investors" (any investor with under Rs. 2 lakh in value of holdings is classified as a "retail" investor) and high networth investors (approximately 33 lakh unique investors) taken

together held approximately Rs. 57,500 crore worth shares of listed Adani companies;

b. The maximum value erosion witnessed by these shareholders between January 24, 2023 and February 27, 2023 was approximately Rs. 29,200 Crores (around 51% value erosion);

c. Subsequent to the reversal of price trend post February 27, 2023 in Adani stocks, this value erosion came down to around Rs. 21,850 crores (around 38% value erosion);

d. While it becomes apparent that at first blush it had appeared that the losses suffered by small investors was in several lakhs of crores of rupees, computations submitted by SEBI places the loss of value of retail investors in Adani stocks at about Rs 3,700 crores; and

e. When one adds to this, the value lost by other individuals including high networth investors the loss in market would aggregate to about Rs 22,000 crores.

17. SEBI has computed these values after excluding the significant number of shares bought by individuals after the publication of the Hindenburg Report, and adjusting for net selling by individuals exceeding their holding on January 24, 2023 (either by way of short selling, or due

to selling shares received through off market transfers etc.) after the publication of the Report[5].

18. Volatility in an entire market could emerge from macro-economic conditions or developments that have a market-wide impact. For example, the onset of a pandemic could impact stock markets around the globe. Likewise, a fiscal crisis, a currency crisis in a market or war could lead to the stock market in that jurisdiction getting volatile. So also, circumstances of uncertainty about individual companies could lead to securities issued by that company experiencing volatility.

19. Securities issued by the Adani Group appear to have steadily kept rising over the past few years and after the Hindenburg Report was published, they dramatically lost value. The recovery of prices in these stocks after some remedial action (such as cutting of exposure to debt backed by pledge of shareholding in these companies, and procuring institutional investment in the securities of these companies), although not high enough to bring these stocks to pre-January 24, 2023 levels, has also been substantial.

20. SEBI has submitted findings of a review of a sample of 35 global stocks that have been targeted by activist

[5] In the interest of brevity, the detailed methodology is not being repeated in this report. It is contained in the written submissions of SEBI, which is compiled separately.

short-sellers. Generally three price-related outcomes are seen:

a. the stock price falls significantly, but recovers;

b. the stock price falls significantly and fails to recover;

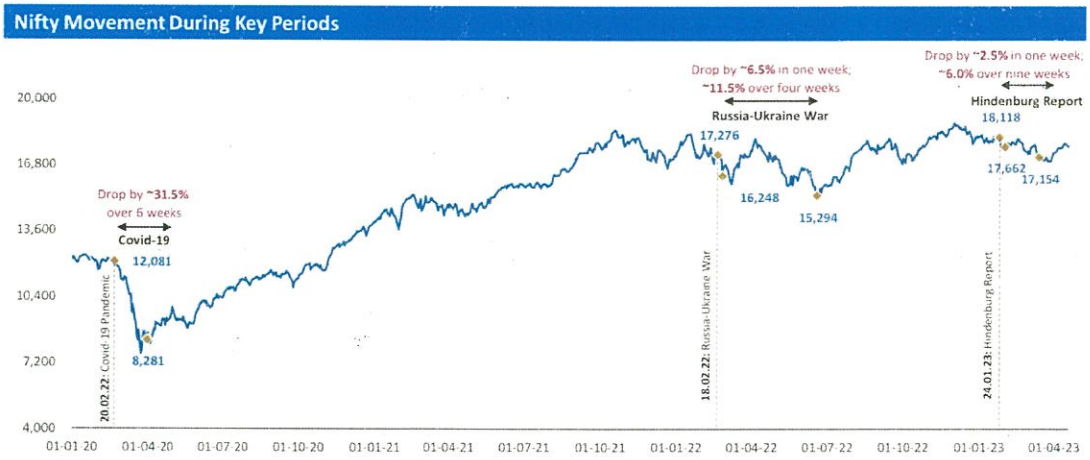
c. the stock price remains largely stable or rises, regardless.

21. According to data presented by SEBI, using the impact on Adani Enterprises as a benchmark – it is the flagship Adani listed company accounting for 25% of the market capitalisation of Adani listed stocks (excluding very recent acquisitions *viz.* ACC, Ambuja Cements and NDTV) – the maximum fall from the prices prior to January 24, 2023 (when the Hindenburg Report was published), was about 65% on February 27, 2023. As of April 19, 2023, that fall has been mitigated to 46%.

22. The Committee sought from SEBI a volatility assessment of the Indian securities market for period starting between January 2020 (prior to the Covid-19 pandemic) and now. Specifically, the scenarios emerging from the impact of the pandemic, the Ukraine war, bank failure in the US, publication of the Hindenburg Report. The Committee desired to study market-wide volatility and stock-specific volatility.

23. Looking to causal factors, it would be seen that in the case of the fall in prices after the pandemic broke out, evidently, the causal factor to which one could attribute the fall would be the pandemic and one could say that the pandemic caused a 33% fall over six weeks. Such a causal factor is so significant that it would overshadow and overwhelm any other factor that contributes to price discovery in the market. However, when an event is company-specific or even industry-specific, it would be tough to attribute movements to any overwhelming and supervening cause.

24. The impact of various events on the Nifty-50 is summarised in the graphic below[6]:



Nifty50 dropped by ~31.5% and ~11.5% due to macro-economic shocks arising from Covid-19 and Russia-Ukraine war respectively. As compared to that, Nifty50 has dropped by ~2.5% and ~6.0% in one and nine weeks post the Hindenburg report respectively.

25. Some macro global factors need mention at this juncture. The prices for stocks that form part of an

[6] Presented by Mr. Sunil Sanghai, CEO of DhruvaNova, a merchant banker, an invitee who met the Committee and responded to queries.

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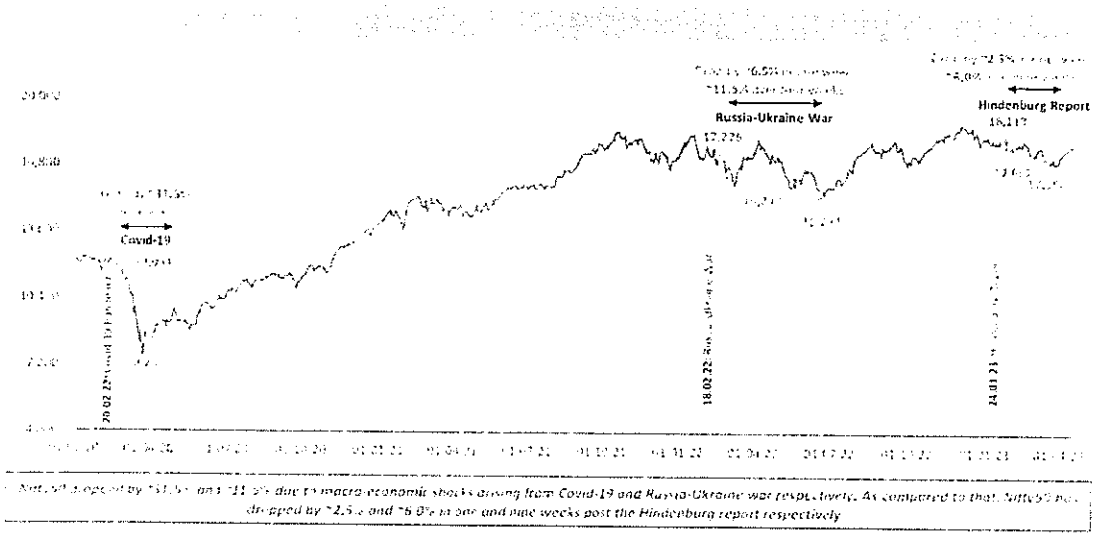

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index and the movement in stock indices are largely determined by the quantum of money chasing the assets. Put differently, the level of liquidity has an impact on price discovery. Greater the quantum of funds being invested, higher the price is likely to be. The loosening and tightening of money supply is an evident factor. If the US Federal Reserve tightens or loosens liquidity, other central banks are expected to react. As money supply changes, the quantum of funds that gets invested in assets also varies.

26. Likewise, events that have a worldwide impact tend to lead to "flight to safety" decisions – where capital abandons foreign assets and investors tend to cash out and return to their home jurisdictions. For example, when the Ukraine war broke out, investors from the US would tend to move monies out of the emerging markets to safer zones in their own home jurisdiction.

27. "Emerging Markets" (understood globally to be markets of developing nations that are increasingly getting integrated to the world markets) experience the impact of macro-level global trends. Typically, a global event such as the Ukraine war would impact all emerging markets, subject however to adjustments for country-level differences among them and peculiarities in their features that would lead to relatively lesser capital outflow or relatively greater capital inflow in that market. Therefore, comparing a country's market index

with an index that reflects emerging markets as a whole would be a good way to adjust for global factors.

28. SEBI rightly points out that to assess the impact of a specific company-level event on the broader market, it is necessary to adjust for the the impact of other contemporaneous factors that impact price discovery. This is where indices come in handy. For example, one way to adjust for the impact of global factors on Indian stock prices is to see the movement of Indian indices, relative to movement in global indices – say, a comparison of movement in the Nifty-50 with movement with say, MSCI Emerging Markets Index.

29. SEBI has also submitted that one must make a distinction between anticipated and unanticipated events when assessing volatility. When anticipated, expectations are built even before the actual events come about. For instance, the reaction in the form of a lockdown could have been hanging over the market well before it is actually implemented. Markets tend to adjust price on the basis of future expectations and when the event actually takes place, there may not be much of an impact if the development is on expected lines. On the other hand, unanticipated events such as the sudden collapse of the Silicon Valley Bank or the publication of the Hindenburg Report have a sharper and more sudden impact when they transpire.

30. Therefore when studying the causes of volatility, one must pick the period carefully and the duration of the event need to factor in the period in which the trend continued.

31. SEBI submitted that the events related to Adani Group companies did not have any significant impact at the systemic level. While the shares of the Group have seen significant decline in prices on account of selling pressure and may have dominated media attention, the markets remained largely stable and resilient.

32. The representation of the Adani Group in major India equity indices is relatively minor, given the limited free float market capitalisation of the group, and as a result, recent events did not pose any systemic market-level risk.

33. According to SEBI, Indian markets have seen far higher turbulent times in the past, especially during the Covid pandemic period, where Nifty-50 fell by around 26% during the period of March 02, 2020, till March 19, 2020 (13 trading days).

34. Even during such turbulent times, the markets continued to function in a robust manner, recovering far faster than other global markets. Investor wealth (market capitalisation of all listed companies) which was around Rs 145 lakh crore in Feb 2020 has almost doubled to about Rs 270 lakh crore now. Further,

overall market volatility in India is on par with or lower than that in major developed markets.

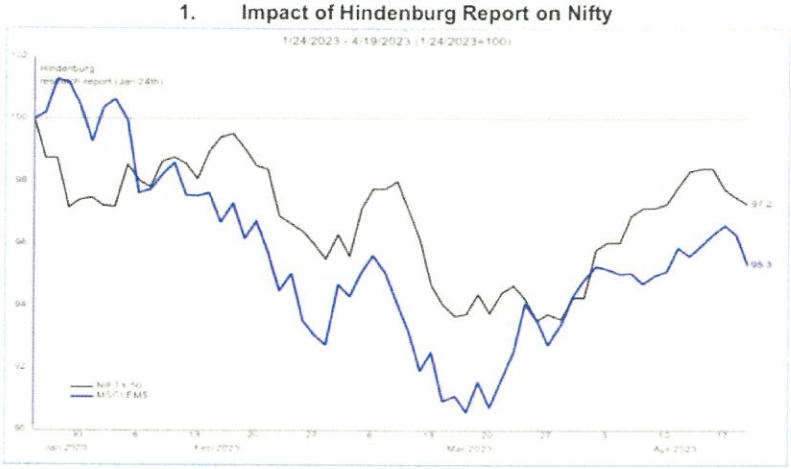
35. The following graphs were presented by SEBI:-

a. Comparison of the movement of MSCI EM Index and Nifty-50 between January 24, 2023 (the day Hindenburg Report was published) and April 19, 2023, indexed to January 24, 2023 prices (*Graph 1*);

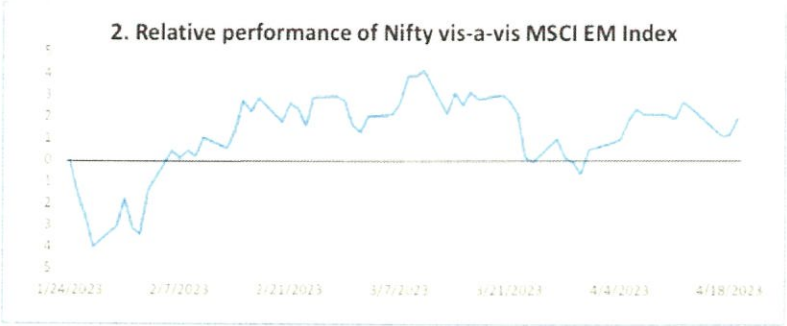
b. Performance of Nifty-50 vis-à-vis MSCI EM Index (Nifty-50 return *minus* MSCI EM return) from January 24, 2023 until April 19, 2023, indexed to January 24, 2023 prices (*Graph 2*);

c. Adani Enterprises prices from January 24, 2023 until April 19, 2023, indexed to January 24, 2023 prices (*Graph 3*).

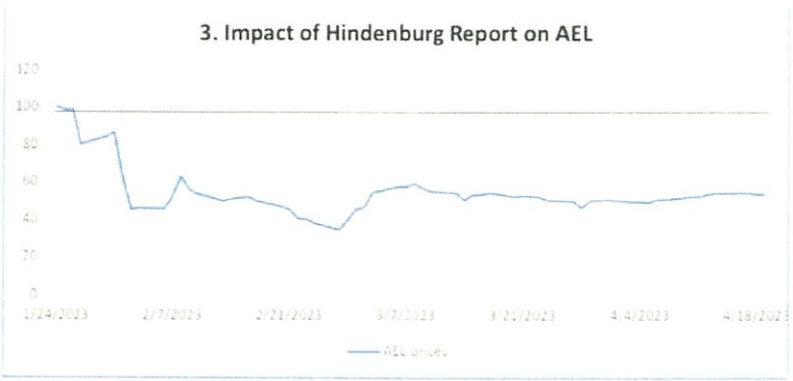
1. Impact of Hindenburg Report on Nifty



2. Relative performance of Nifty vis-a-vis MSCI EM Index



3. Impact of Hindenburg Report on AEL



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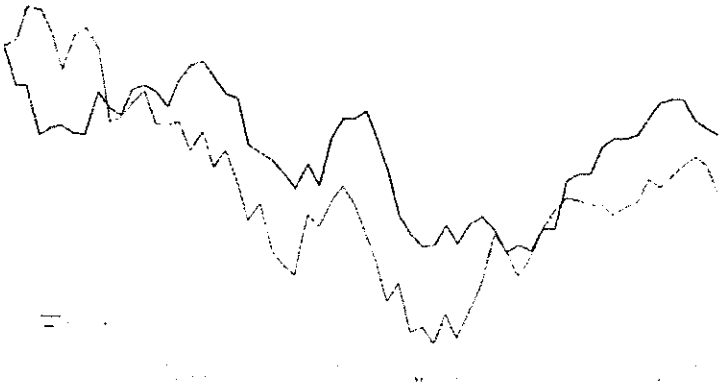


2. Relative performance of Nifty vis-a-vis MSCI EM Index

3. Impact of Hindenburg Report on AEL

36. Based on these data points and the graphs, it has been brought out that:-

a. While Nifty-50 fell after January 24, 2023, MSCI EM Index rose, outperforming Nifty-50 for the next 2 weeks till February 06, 2023;

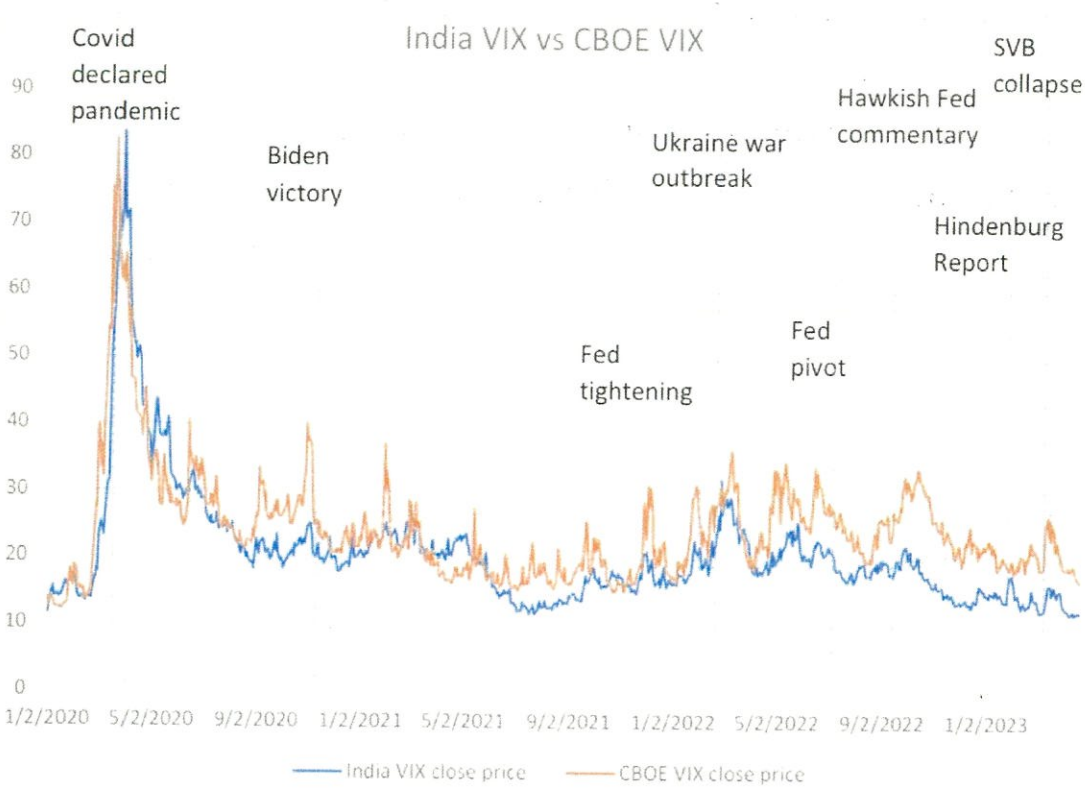
b. During the two-week period (from January 24 to February 06, 2023) when Nifty-50 underperformed MSCI EM Index, the maximum underperformance (relative to pre-Hindenburg prices) of Nifty-50 vis-à-vis MSCI EM Index was around 4% on January 27, 2023;

c. Subsequent to this short two-week blip, Nifty-50 has consistently outperformed MSCI EM Index (except for a short period of 3-4 days when the returns of the two indices relative to pre-Hindenburg prices, were more or less same (period between March 24 to March 30, 2023).

37. Thus, even if it is assumed that the entire 4% underperformance of Nifty-50 relative to MSCI EM Index was due to Hindenburg Report, the overall finding is that the Hindenburg Report had a negative impact on Nifty-50 only for a short period of 2 weeks immediately following the publication of the report and the maximum extent of this impact was 4%. After two weeks, the Nifty-

50 bounced back relative to MSCI EM Index, and continued to outperform it.

38. Finally, SEBI has also presented a comparison of the volatility index data for India as compared with the CBOE VIX for the period between January 2020 and April 18, 2023 – the graphic below would present a snapshot:-



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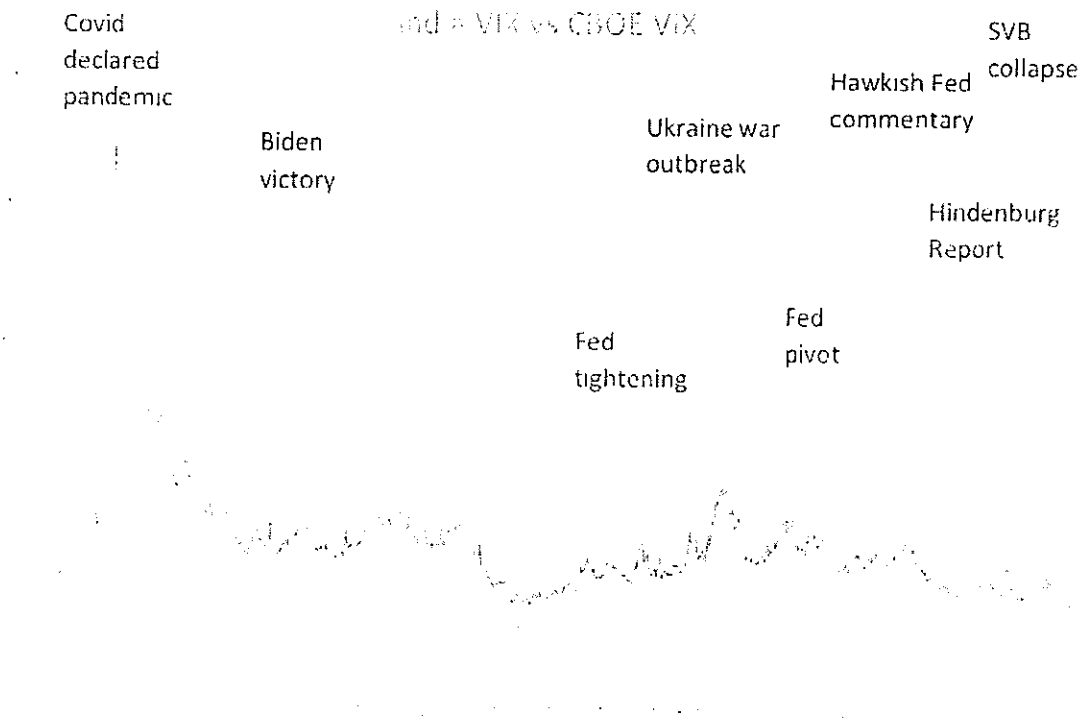

39. It can be seen that except for few weeks after the outbreak of Covid-19, India VIX has been consistently lower than CBOE VIX, including in the post Hindenburg Report period.

AMFI's Inputs on Volatility:

40. The Association of Mutual Funds of India[7] ("**AMFI**") made an interesting point. Close to 200 companies are traded in both the cash segment of the capital market as also the derivatives segment, enabling trades in futures and options in them on a daily basis. Market players comprising day traders who square off the trades within a trading day along with institutional participants contribute to volume and provide buy and sell liquidity to stocks in both segments of the market.

41. The market continues to become efficient over time due to increased participation coming from domestic investors and large foreign portfolio investors. Overall market depth has been increasing and participation levels have been rising. In particular, post-pandemic, the number of investors participating in the equity has increased exponentially. This is reflected in the number of demat accounts opened in the country during the lock down period.

[7] Represented by Mr. A. Balasubramaniam, President, who was one of the invitees and engaged with the Committee

42. Speculative trading volume has gone up substantially after stock exchanges introduced weekly options settlement as compared with the earlier monthly settlements. Most of the volume occurs in the weekly options market, leading to a sharper price discovery, the flip side of which is an inherent potential for increase in volatility. Since institutional investors such as mutual funds, insurance companies and pension funds use the derivatives segment purely for hedging and mainly deal in the cash segment, according to AMFI, an element of volatility is inherent in the derivatives market due to lack of depth in institutional participation.

43. AMFI's representative attributed the recent volatility in the market largely to news flows on monetary actions by global central banks (the US Federal Reserve in particular), slowdown in the global economy and events such as the Hindenburg Report.

44. Most of the leading hedge funds do not trade in derivatives in India and they trade instead in the Nifty-50 derivative on the stock exchange in Singapore. The recent market volatility can also be attributed to sovereign funds, quasi sovereign funds and pension funds selling stocks purely on the basis of the their mandates around environment and governance issues. Such sales are effected without looking at the stock price or valuations.

45. It was found that four of the larger Adani Group companies are in the F&O segment. They were observed to have middle-of-the-range volatility as well as impact cost. This is despite the observation that floating stock is low in these companies on account of promoter holding being high at around 57-73%.

Committee's Conclusions:

46. Taking into account the foregoing factual backdrop, the Committee returns the following findings:-

a. Volatility is not an inherent vice for the market. As market participants buy and sell securities, placing buy and sell orders in line with their demand and supply, they do so, based on their assessment and expectations, which is in turn, based on their assessment of information available to them, and its anticipated impact;

b. The price discovery in individual stocks would be informed by the events that transpire in connection with such individual stocks. The cumulative effect across stocks and the impact on price would lead to assessment of movements and volatility for the market;

c. The Indian market in general was not unduly volatile as is seen in comparison of the Indian volatility index (India VIX) with the CBOE volatility index (CBOE VIX);

d. There was certainly high volatility in the Adani stocks after publication of the Hindenburg Report, with the market's expectations from, and confidence in the Adani Group, being shaken by the allegations in the Hindenburg Report;

e. While the Hindenburg Report called for a probe and was inferential based on publicly available information, it presented together a formulation that questioned the foundational premises on which the market priced Adani stocks;

f. The intense adverse impact on Adani stock prices stood mitigated with measures such as the Adani Group promoters paring down the debt raised, secured by encumbrances on their shareholding, and infusion of fresh investment into Adani stocks by way of purchase of shares worth nearly USD 2 billion by a private equity investor from the promoters of the Adani Group;

g. The market has re-priced and re-assessed the Adani stocks and while they may not have returned to the pre-January 24, 2023 levels, they are stable at the newly re-priced level;

h. Empirical data that shows that retail investors' exposure to the Adani stocks has increased would point to the fact that investors and the market do make their own informed decisions and a fall in the price led to more capital including from retail investors coming into ownership of these stocks at a re-priced levels.

47. SEBI has submitted that only recently, it has made a regulatory intervention in terms of supervising the construction of stock indices. SEBI must consider directing index writers to construct indices to compute volatility of stocks that are constituents of indices so that volatility in these stocks can be compared with volatility in the indices. The availability of such data on a real time basis would enable the market to be more informed in making its investment and divestment decisions. SEBI must ensure that there are secular norms and periodic reviews for construction and design changes in indices.

* * * * *

CHAPTER THREE

INVESTOR AWARENESS

1. At the heart of any efficient market is the ability for market players to make informed investment decisions. The interplay of demand and supply in a market, leading to price discovery, is founded on the premise that participants who express their demand and supply do so in an informed manner.

2. Informed investment decisions not only means investors making informed decisions on whether to buy or sell or to refrain from doing either, but also brings within its remit, awareness of the ecosystem and the attendant risks, rewards, rules and regulations.

3. The Committee asked SEBI and various invitees to address the Committee on their views and perspectives on investor awareness and what measures they would suggest to improve investor awareness.

4. With the growth of the Indian economy increasing number of savers are looking to invest in the stock market to earn higher returns. However, data presented by SEBI shows that the increase is substantially in the riskier segment – the futures and options segment of the stock market – a segment that entails higher risk and specialised knowledge of the market. Most investors

have entered this segment perceiving it as a quick way to make money, mostly working on tips from brokers.

5. Investor education would need to cover three broad areas:-

   a. education of the lay investor who is primarily investing in stocks, to hold them for a longer period;

   b. investors coming into the market through the mutual fund route; and

   c. investors operating in the F&O segment, who are primarily day traders.

6. Investor education is today done by multiple agencies such as SEBI, the stock exchanges, the Investor Education and Protection Fund Authority and AMFI for the first two areas.

7. It is in the third area, the fastest growing segment of the market, where investors need significant education. SEBI is fully aware of the above and the need to have focus on the process of educating and making aware those who are increasingly entering this segment.

8. The Committee sought inputs from SEBI on the issue of consumer education and awareness. SEBI has recognised the increasingly larger number of intra-day

traders who are coming into the market and the need to educate them, alert them in advance of a trade so as to better inform them.

9. Sebi has identified areas that need attention and their plan to address these areas. The committee agrees with steps outlined by SEBI and suggests implementation of these as early as possible in a time bound manner.

SEBI Study on Individual Traders:

10. SEBI submitted that Indian investors are seen to be active in trading in stocks (buying and selling) as well as investing (holding on without reversing a trade). SEBI submitted the key findings of a research report published by it titled "*Analysis of Profit and Loss of Individual Traders dealing in Equity F&O Segment*"[8]. The report contains an analysis of trading by individual investors and how they fared in the equity futures and options ("**F&O**") segment between financial years 2019 and 2022.

11. The following findings were presented by SEBI as being the salient features of the report:-

    a. Out of the total trading by individuals in the cash segment, approximately 67% by value is by way of

[8] ...

intra-day trades and only 33% results in delivery of shares;

b. Total number of unique individual traders who traded through the top ten brokers in equity F&O segment has increased by over 500% in FY22 as compared to FY19;

c. Approximately 88% of the individual traders were active traders.

d. 89% of the individual traders (i.e. 9 out of 10 individual traders) in equity F&O segment incurred losses, with an average loss of Rs. 1.1 lakh during FY22; and

e. Despite such losses, share of individuals in total F&O turnover is very high – during the last four years, it has been around 27-29%.

12. Analysis of the foregoing indicates that a significant proportion of individual investors are engaged in intra-day trading derivatives trading. Data on delivery-based trades executed by individuals, their trading contribution to the F&O segment and the number of demat accounts with zero holdings, points to such individuals having a high risk appetite and them being more traders than investors.

13. Therefore, the investor education and awareness content is proposed to be designed appropriately to meet the requirements of the different categories of individuals in the securities market – the traders/ short term investors and the buy- and-hold investors/ long term investors.

Investors in Mutual Funds:

14. The mutual fund industry appears to have gained the confidence of the Indian investor in the past few years.

15. Assets under management of the mutual fund industry has increased by around 67% from Rs. 23.8 lakh crore as on March 31, 2019 to Rs. 39.46 lakh crore as on February 28, 2023.

16. Of these assets, exposure to equity through mutual funds at the end of February 2023 was Rs. 15.08 Lakh Crore as compared to Rs. 8.9 lakh crore at the end of March 2019.

17. During the same period, the number of systematic investment plans (where an investor commits a specific investment at regular specified intervals) and the number of unique mutual fund folios have also increased by around 120% and 90% respectively

indicating that interest of retail investors in medium to long term investment is also increasing.

18. It appears that individual investors with a medium to long term investment horizon are choosing to invest in mutual fund schemes rather than directly in the stock market.

Secondary Market Measures:

19. SEBI submitted that its measures to address the potential for market risks to impact settlement of trades have ensured that there has been no market default owing to price movements. The system of investors having to post margins to secure the trades they transact are linked to volatility of the share prices in which they transact.

20. The Indian securities market indeed has certain features to deal with sudden and unusual price movements and severe volatility. The objective of these measures is primarily to enable the market to take a pause and reflect on the information that is causing the sudden sharp movement in price. These are:-

    a. The index-based market-wide "circuit breaker" system (stoppage of trading) applies at 3 stages of the index movement [i.e., movement of Bombay Stock Exchange's Sensex or the National Stock Exchange's Nifty-50] in either direction. The

circuit breaker applies if the index move by 10%, 15% and 20% over the previous day's closing index. At these thresholds, a nationwide trading halt kicks in;

b. On individual shares, prices cannot move up or down by more than 20% within a day. This limit does not apply to stocks on which futures and options derivatives are traded.

c. As for stocks in the F&O segment, they are subject to price bands at 10% of the previous day's closing price but with the stock exchanges having the ability to dynamically flex the price bands subject to certain objective criteria being met, 15 minutes after the limits are reached.

Additional Surveillance Measures ("ASM"):

21. The ASM framework is a stock-specific surveillance measure. Based on specific characteristics of the issuer company and its returns as parameters, this framework imposes certain graded restrictions on the trading in the stock. The ASM framework is meant to alert investors to be extra cautious while dealing in the securities covered under its framework.

22. Once a stock attracts the ASM framework, measures such as reduced price bands, higher upfront margins (upto 100%) and mandatory gross settlement (prohibition on squaring up – known as the trade-to-trade system) automatically apply. These measures are triggered by the automated system as per defined thresholds of price movement, client concentration, etc without manual discretion.

Graded Surveillance Measures ("GSM"):

23. GSM framework entails a stock-specific surveillance measure that is triggered for securities with a price not commensurate with financial health and fundamentals. Under the GSM framework, various actions are taken such as requirement of 100% upfront margin, lower price bands, restriction on upward price movement, requirement of additional surveillance deposit, limited number of trading days per week, etc.

24. Securities that are put into the GSM framework are published on the website of Stock Exchanges. Trigger of GSM alerts investors to be extra cautious while dealing in such securities. This measure typically addresses potential market abuse in "penny stocks" where the networth of the issuer is lower than Rs. 10 crores, it has fixed assets of lower than Rs. 25 crores, market capitalization lower than Rs. 25 crores etc.

Cautionary Messages:

25. Stock exchanges, since 2018, have been flashing a message when the broker places an order in a stock that is under ASM or GSM highlighting that security is under surveillance and seeking a confirmation that the broker wishes to continue with the trade.

26. SEBI has made submissions on its expenditure on investor awareness programmes, media campaigns including social media, development of a mobile app etc. These are placed in the accompanying Compilation of Submissions and not elaborated here in the interest of brevity.

Investor Education and Protection Fund Authority

27. In the spirit of improving investor awareness, the Committee thought it fit to focus on a very important and highly neglected area – the framework in which unclaimed securities, dividends and bank deposits are handled. Investors routinely lose out on access to funds and properties of their next of kin due to the framework of the law in this regard.

28. The Committee called upon the Investor Education and Protection Fund Authority ("**IEPFA**") to present its workings and manner of administration of the IEPF. The fund has been established under Section 125 of the Companies Act 2013 with the objective of promoting Investor Education, Awareness and Protection, and is maintained under Consolidated Fund of India.

29. The Committee learnt that the unclaimed shares held under this head is to the order of Rs. 47,000 crores and cash to the extent of nearly Rs. 5,200 crores. The IEPFA is manned by a CEO holding additional charge and has a dozen officers.

30. The IEPFA explained the process for an investor claiming refund by way of an online application, which then undergoes a process of re-verification. In the interest of brevity, the submissions are set out in the accompanying Compilation of Submissions, and not elaborated here.

31. Akin to SEBI, the IEPFA too presented how media campaigns and financial literacy programmes are being invested in. The written submissions of the IEPFA are set out in the Compilation of Submissions and are not elaborated in this chapter in the interest of brevity.

32. It was evident from the interaction with the IEPFA that it is a classic example of capacity constraints of the State being visited upon a public-facing service, as a result of which the size of the assets lying with the IEPFA is evidently large. The IEPFA was candid in submitting that the process of IEPF refund has multiple stakeholders with the main service providers working on totally different electronic platforms that are not inter-operable. As a result the flow of data is not seamless and the process of refund takes way more than the statutory stipulated period. Rent-seeking behaviour from unscrupulous agents who offer services to get the refund for a percentage of the share of wealth released, is being widely reported. Further, the grievance redressal mechanism is very rudimentary and is unable to handle the volume of calls/ emails.

Depositor's Refunds:

33. Even while the Committee was deliberating about the issues being faced at the IEPFA, news reports about Writ Petition No. 185 of 2022, in the Hon'ble Supreme Court as Public Interest Litigation on the issue of refund of unclaimed deposits came to the Committee's attention. The Committee is in receipt of a detailed note akin to a white paper from the petitioner Ms. Sucheta Dalal on the subject of setting up a composite Central Authority

for Unclaimed Property, which is set out in the Compilation of Submissions.

34. Upon review of the white paper, the Committee commends the following measures:-

a. The problem of unclaimed assets is not unique to India. Most developed countries have found workable, technology-based solutions and verification processes to return any unclaimed funds/assets to the rightful legal heirs. This is a three-step process. First, the authorities make rigorous attempts to locate the rightful heirs or owners of unclaimed assets; second, when the owner is not traceable for anywhere between 7 and 10 years, the assets are transferred to a centralised fund; third, claimants do not lose the right to such funds and have access to searchable databases to track the funds and follow the process laid down to recover the money;

b. India has five different entities collecting unclaimed assets – four financial regulators and the Senior Citizens Welfare Fund (which pools unclaimed provident funds and Central saving schemes). There is no effort, legally mandated or otherwise, by any of them to contact the rightful owners; nor is there an effort to create a robust and

searchable database that will allow true owners or heirs to track the funds and file claims;

c. There is a need to create a centralised searchable database of unclaimed money and property of the general public that gets transferred to government-owned repositories such as the Depositor's Education and Awareness Fund ("**DEAF**") and IEPF on the premise that the property is not claimed by legal heirs or nominees;

d. The core objective of the database should be to "reunite unclaimed property (including all financial assets) with the rightful owner" and towards this end, enable proven legal heirs to get a full picture of the investments and savings of the deceased and claim their money/bequest in a smooth and efficient manner;

e. In order to be effective, a statutory central authority, backed by appropriate legislation must be empowered to track the rightful owners, resolve grievances and deal with security and privacy concerns;

f. It is only when the databases are inter-operable and integrated that the system would be effective. This will involve legal mandates and organisational

structure, with holistic IT-based automated processes;

g. The authority must create standard operating procedures since even within the same class of institutions (say, a bank, different managers add their own rules and demand sureties, fixed deposits, indemnity, etc) in connection with honouring claims;

h. A simple PAN-based KYC of the nominee (non-mandatory) may be considered to make the process of identification and transfer of assets much simpler;

i. Globally, there are different models of dealing with such funds with most of them having statutory backing. The ambit of what comprises unclaimed funds also differs widely. In the US, it also extends to royalties, unclaimed salaries, mining rights, etc, in addition to stocks, bonds, bank deposits and earnings thereon;

j. Some countries maintain a central database for unclaimed assets; others have managed to efficiently make the information available through multiple authorised agencies. In the United Kingdom, the agency operates as a public-private partnership.

Committee's Conclusions:

SEBI:

35. At this juncture, the Committee wishes to emphasize that having systems such as ASM and GSM in place is not the only solution. There has to be an actual and real prospect of the individual investor becoming aware of the heightened surveillance. Increasingly, the stock trading is almost entirely digital even at the consumer's end, and it should be possible to make relevant and pertinent information available at the point of transaction. Two significant online brokers *viz.* Zerodha Broking Ltd. and Paytm Money Ltd representing about 24% of the total clients, are said to have implemented measures to alert clients about stocks being on ASM or GSM at the point of entry of orders. This should become the norm rather than represent exceptions.

36. More importantly, one must bear in mind that the securities market is meant to function on the premise of investors making informed decisions. Right since 1991, when the Controller of Capital Issues as abolished and replaced by SEBI, the approach to the market has been that one must regulate the quality of disclosures available to the investors and enable investors to learn how to take informed decisions. Therefore, it is imperative that the regulatory framework must function on the basis of information being available to the

investors, information being easily accessible and information presented being capable of analysis.

37. The Committee notes that the disclosure-based regime can be broadly classified into the following two heads:-

a. Disclosures to be made at the time of issue of capital or offer of securities to list securities through a prospectus – governed by the SEBI (Issue of Capital and Disclosure Obligations) Regulations, 2018 ("**ICDR Regulations**");

b. Disclosures to be made after listing during the course of operations of a listed company to intimate material events and developments and other statutory disclosures – governed by the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 and the SEBI (Prohibition of Insider Trading) Regulations, 2015;

38. Under both heads, there is an urgent need to introspect and take a hard close look at whether there is a surfeit of disclosures that loads and burdens the investors with so much data and noise that the real content necessary to make an informed decision may be lost.

39. Offer documents and prospectus issued at the time of listing in compliance with the ICDR Regulations run into

several hundreds of pages, which begs the question as to whether investors actually read these documents.

40. Upon a request from the Committee, SEBI presented a chart comparing the annual disclosure requirements in the United States with the disclosure obligations in India to empirically demonstrate how India entails more disclosure than the United States. The document of comparison is placed in the Compilation of Submissions, and would show how a far wider and a far more expansive scale of disclosures is stipulated in India. This leads to noise and clutter that makes it burdensome and difficult for the investor to get to the core messaging that is needed. For instance, SEBI has stated that while only material related party transactions are required to be disclosed in the US, in India, every related party transaction is required to be disclosed.

IEPFA:

41. The Committee is of the view that various imaginative and creative measures can be easily attempted by the IEPFA, such as:-

a. The integrated portal announced in the Finance Minister Budget Speech should be expedited and process re-engineering delegation to the issuer companies based upon type and threshold of the claims must be considered;

b. The same may be reviewed on incremental basis from time to time considering the benefits on reducing the timeline for disposal of claims vis-à-vis the risks of fraud.

c. Pilot projects such as taking up names from the death registry in a given area to map it with the database of the IEPFA and proactively attempting to reach out to the next of kin should be considered;

d. Registered market intermediaries who are answerable to the regulatory regime of financial sector regulators could be identified and recognised as agents for service delivery to enable release of unclaimed dividend and securities;

e. An officer strength of a dozen personnel is evidently disproportionate. The IEPFA would need a full time Chief Executive Officer who would have specific key performance indicia that would be fixed by the governance oversight of the Authority.

42. The Government of India ought to give its active consideration to provide for a centralised authority to handle and process unclaimed private assets on the lines suggested for creating the Central Authority for Unclaimed Property. Unclaimed assets can emerge from various segments of the financial sector – be it securities market, insurance market, banking sector, pensions sector or any other such avenue in which living individuals would invest. The need for a centralised holistic approach must be recognised. The temptation, if any, to absorb assets belonging to members of society to the wider public exchequer, must be shunned. Such an agency has to be a full-time hands-on real time proactive agency that actively seeks out to discharge a mandate of reuniting assets of dead individuals with their successors.

Financial Literacy:

43. Finally, the Committee believes that there is a vital need to introduce financial literary as a matter of pedagogy right from school curriculum. Financial security of a society is as vital as national security for a society to be robust. Right through school and university curricula, there is a need for regulators to engage with educationists to bring in a culture of financial awareness and literary. India has for a while been the third largest economy in the world (in purchasing power terms) and the education our society gets must be

commensurate with such standing. Earning, saving and investing, earning returns, and giving back to society, are part of a virtuous cycle, and the era of treating money with an unstated element of stigma must not continue. Imparting appropriate education about the right role of money and how individuals should handle money, is therefore an important element of education to impart.

* * * * *

CHAPTER FOUR

ALLEGED CONTRAVENTIONS AND REGULATORY FAILURE

Introduction and Context:

1. In examining the remit of the Committee under Paragraph 15(c) of the Hon'ble Supreme Court's order dated March 2, 2023, the Committee kept sharp focus on the contents of Paragraph 10, which spelt out the specific areas on which SEBI's probe must focus and on which SEBI must apprise the Committee.

2. The three areas of investigation spelt out are:

   a. Whether there has been a violation of Rule 19A of the Securities Contracts (Regulation) Rules 1957;

   b. Whether there has been a failure to disclose transactions with related parties and other relevant information which concerns related parties to SEBI, in accordance with law; and

   c. Whether there was any manipulation of stock prices in contravention of existing laws.

3. These are taken up in sequence as sub-chapters, in this Chapter.

Minimum Public Shareholding – Regulatory Framework:

4. The very first aspect directed for investigation by the Hon'ble Supreme Court in its order dated March 2, 2023 is: Whether there has been a violation of Rule 19A of the Securities Contracts (Regulation) Rules, 1957. This is the provision dealing with the minimum public shareholding stipulation for listed companies to adhere to.

5. Public shareholding is essentially shareholding in the hands of all shareholders other than the promoters and the promoter group. The need for regulations to stipulate a minimum level of public shareholding has multiple objectives – a good float of shares that are not locked up from trading would lead to a good prospect of price discovery; greater the frequency of trading in shares of a company, greater the depth of the quality of the price discovery in the shares; and lesser the chance of the price being volatile, since higher the liquidity greater the ability to absorb spurt in demand or supply.

6. Rule 19A of the SCRR[9], as it now stands, is extracted with all the footnotes that show the legislative history since its introduction in June 2010, in **Annexure A** to this Report.

[9]

7. Even a plain reading would show that Rule 19A was introduced in June 2010, and has all along been subject of frequent and repeated amendments. The complexity of public sector undertakings and the temptation to treat them differently has also left its imprint on the provision.

8. From a regime of having to maintain a very high mandatory public shareholding, to a regime where different companies had different standards to meet to remain compliant, to a regime where all companies by and large comply with a common standard, the law governing minimum public shareholding has truly had a chequered history. It would be useful to examine this history in brief.

9. When India introduced exchange controls and forced multinationals to list their subsidiaries in India in the 1970s, promoter stake was to be kept at 40%, with minimum public offers of 60% being mandated by law. This changed when India opened up in the 1990s.

10. Suffice it to say that the first serious reform towards the current regime took place in August 2005[10]. SEBI introduced a policy change, which was well-intentioned, but created multiple classes of companies with varying

[10] Section 4.2 of SEBI's Board Memorandum provides a historical snapshot at:

public shareholding. In a nutshell, the change introduced could be summarised thus:-

a. As a general rule, every listed company was to ordinarily maintain a public shareholding of at least 25%;

b. However, since Rule 19(2)(b) permitted making a public offer with just 10% offer to the public, such companies would be compliant if they maintained a minimum public shareholding of 10%;

c. Government companies, infrastructure companies and sick industrial companies were exempt from minimum public shareholding requirements;

d. Listed companies, that were not compliant in 2005, were given two years to become compliant;

e. Listed companies that may become non-compliant due to issuance of shares that lead to a breach of the minimum public shareholding (for reasons such as corporate debt restructuring packages) would get one year to become compliant;

f. SEBI indicated that the ultimate objective is to reach a single level of minimum public shareholding for all, but did not stipulate an eventual timeframe for reaching this objective.

11. It was on June 4, 2010 that Rule 19A was introduced into the SCRR. From this stage, two instruments of law dealt with minimum public shareholding – the listing agreement to be executed with stock exchanges and the SCRR.

12. Originally different companies had different standards to comply with, and that was eventually streamlined to every listed company having to comply with a 25% minimum public shareholding. Time was given to companies to adhere to the new standard and there has been suspicion that many promoters of corporates would be prone to strike deals with friends and family to hold shares on their behalf and take on the role of "public shareholders" but given the influence or control over them, such holding was suspected as not being truly public shareholding.

13. The entire point of a minimum public shareholding norm was that there should be a free float available for price discovery. Shares held in the hands of public shareholders would not have any strings attached to the promoters and they would be free to trade in them without having to take consent of any promoter, and without being subjected to any preemptive right such as right of first refusal or right of last refusal.

14. Therefore, SEBI began regulating the manner in which compliance with minimum public shareholding may be achieved. SEBI got prescriptive in this regard, and spelt out the specific types of transactions by which a listed company could become compliant with minimum public shareholding. A concept of an "offer for sale" in the secondary market, without having to write a prospectus, was introduced, with micro-regulation requiring offers to institutional investors, with attendant norms. In the interest of brevity, the acute detail of such requirements is not being spelt out here.

15. The direct benefit of public shareholding having depth is that trading in the market would then have depth and therefore frequency of trading could be higher, leading to better price discovery for the listed securities. It is in this context that the allegations about the listed Adani companies in connection with minimum public shareholding must be considered, and for the Committee to examine if there is a regulatory failure or shortcoming in meeting the objectives for which the regulations have been made.

16. Therefore, since public shareholding is about the ability of a shareholder to decide for himself to trade in the shares without reference to the promoter and without strings attached to the promoter, the vexed question is to see who can actually take decisions on what to do with the shares.

FPI – Regulatory Framework:

17. This is where the regulatory framework governing foreign portfolio investors comes in. A quick word on the march of this law would be useful before going into the factual matrix involving listed Adani companies.

18. Initially, when India opened up its market in 1991 for cross border investment in the stock market, a category of investors was created with freedom to make portfolio investments in Indian companies. Any investment of not more than 10% was considered portfolio investment and institutional investors who register themselves with SEBI were permitted to trade freely on the Indian stock market.

19. The Indian Rupee was then not (and still is not) fully and freely convertible on the capital account. Foreign Institutional Investors ("**FIIs**") registered with SEBI could freely buy and sell shares on Indian stock exchanges and they could remit money inwards and outwards subject to their investments being compliant with what was specifically allowed. For instance, no FII could hold more than 10% in a listed company. It is another matter that different FIIs could collectively hold more in a listed company. Other obligations were

imposed such as ensuring that assets in India are held only through a "custodian" (another form of registered market intermediary), ensuring that funds flowed into and out of India only through a pre-identified designated bank account, and so on.

20. Over time, the requirement to register as an FII and comply with various regulatory requirements was considered by the market to be burdensome, and a product termed the "overseas derivative instrument" (colloquially and popularly called 'participatory notes') emerged. ODIs were nothing but bilateral contracts between an investor and an FII, whereby the FII would make an investment using its registration but pass on the risk and reward of the investment to a third party who would provide funds to the FII. The ODI market represented a significant component of secondary market trading at one time, and policy-makers felt the burden of compliance in accessing the Indian market was leading to inefficiencies and opaque sources of investments into India.

21. Based on the recommendations of the Working Group on Capital Inflows (where one of us was a member)[11], a concept of a 'foreign portfolio investor' ("**FPI**") was introduced. The idea was to make registering to invest in the Indian stock market easier, so that more investors from abroad would have access to the Indian markets

[11] The report dated July 30, 2010 is available at:

and would not have to be captive to the rent sought by FIIs, who alone enjoyed the privilege of investing in India. All existing FIIs were migrated to an FPI status. Since a foreign investor who would have to otherwise find an FII to contract an ODI, could directly come into India as an FPI, the economic rationale for a booming ODI market was also undermined, removing inefficiency in market access for foreign investors.

22. The process of registering too was simplified – rather than having to interact with SEBI to register, an FPI could designate and register with any depository participant who would in turn provide access to the Indian market (instead of an FII). The designated depository participant would be the one who would open a demat account for the FPI and monitor the trades from the perspective of regulatory compliance.

23. It is in this light that the the SEBI (Foreign Portfolio Investors) Regulations, 2014 [12] ("**FPI Regulations, 2014**") were conceived.

24. It is noteworthy that the FPI Regulations, 2014 in fact had stipulated a requirement that FPIs must not have an "opaque structure". Regulation 32(1)(f) of the FPI Regulations, 2014 originally provided as follows:-

> *32. (1) All designated depository participants who have been granted approval by the Board shall –*

[12] https://www.sebi.gov.in/legal/regulations/jan-2014/sebi-foreign-portfolio-investors-regulations-2014_26906.html

(f) ***ensure that foreign portfolio investor does not have opaque structure(s)****:*

Explanation 1.- For the purposes of this clause, "opaque structure" shall mean any structure such as protected cell company, segregated cell company or equivalent, where the details of the ultimate beneficial owners are not accessible or ***where the beneficial owners are ring fenced from each other or where the beneficial owners are ring fenced with regard to enforcement****:*

Provided that the ***foreign portfolio investor satisfying the following criteria shall not be treated as having opaque structure****:*

(i) the applicant is ***regulated in its home jurisdiction***

(ii) each fund or sub fund in the applicant ***satisfies broad based criteria****, and*

(iii) the applicant ***gives an undertaking to provide information regarding its beneficial owners as and when Board seeks this information****.*

Explanation 2.- ***For the purposes of Explanation 1, the definition of ultimate beneficial owner shall be as provided under the Master circular on Anti Money Laundering Standards or Combating the Financing of Terrorism, issued by the Board from time to time.***

[Emphasis Supplied]

25. With effect from December 31, 2018, Explanation 1 and Explanation 2 in the above definition were substituted. The changed provisions read as follows:-

*"****Explanation 1****. - For the purposes of this clause, "opaque structure" shall mean any structure such as (i)*

protected cell company, segregated cell company or equivalent, where the details of the ultimate beneficial owners are not accessible or where the beneficial owners are ring fenced from each other or where the beneficial owners are ring fenced with regard to enforcement, ***or (ii) where applicant or its investor(s) identified on basis of threshold for identification of beneficial owner have issued any bearer shares or maintain any outstanding bearer shares.***

Provided that the foreign portfolio investor satisfying the following criteria shall not be treated as having opaque structure:

(i) the applicant is regulated in its home jurisdiction;

(ii) each fund or sub fund in the applicant satisfies broad based criteria;

(iii) the applicant gives an undertaking to provide information regarding its beneficial owners as and when Board seeks this information; and

(iv) the applicant submits an undertaking that it does not maintain any outstanding bearer shares and it would not issue bearer shares in future.

Explanation 2*. - The phrase* ***"ultimate beneficial owner" shall have the same meaning assigned to the term "beneficial owner" as defined under the Prevention of Money Laundering Act, 2002."***

[Emphasis Supplied]

26. The changes were two-fold *viz.* (i) introduction of the legal standard that issuance of bearer shares would render the structure opaque; and (ii) adoption the meaning of "beneficial owner" under the Prevention of Money Laundering Act, 2002 [13] ("**PMLA**") for the meaning of "ultimate beneficial owner" in the FPI Regulations, 2014.

27. Therefore, while the phrase used in the FPI Regulations, 2014 is "ultimate beneficial owner", the meaning given to it would be the definition of the term "beneficial owner" under Rule 9 of the Prevention of Money Laundering (Maintenance of Records) Rules, 2004 [14] ("**PMLA Rules**").

28. Relevant extract from Rule 9 of the PMLA Rules, which stipulates what every client must declare as beneficial ownership to a "reporting entity" (banks and financial intermediaries), is set out below:–

"(1) Every reporting entity shall—

(a) at the time of commencement of an account-based relationship—

13.

14.

i. *identify its clients, verify their identity, obtain information on the purpose and intended nature of the business relationship; and*

ii. ***determine whether a client is acting on behalf of a beneficial owner (BO) and identify the beneficial owner and take all steps to verify the identity of the beneficial owner**: ..."*

*"(3) The **beneficial owner for the purpose of sub-rule (1) shall be determined as under**—*

*(a) **where the client is a company**, the **beneficial owner is the natural person(s)**, who, whether acting alone or together, or through one or more juridical persons, **has a controlling ownership interest** or who **exercises control through other means**.*

Explanation. — For the purpose of this sub-clause—

1. *"**Controlling ownership interest**" means ownership of or **entitlement to more than twenty-five per cent**. of shares or capital or profits of the company;*

2. *"**Control**" shall include the right to appoint majority of the directors or to control the management or policy decisions including by virtue of their shareholding or management rights or shareholders agreements or voting agreement*

*(b) **where the client is a partnership firm**, the **beneficial owner is the natural person(s)** who,*

*whether acting alone or together, or through one or more juridical person, **has ownership of entitlement to more than fifteen per cent**. of capital or profits of the partnership;*

*(c) **where the client is an unincorporated association or body of individuals**, the **beneficial owner is the natural person(s)**, who, whether acting alone or together, or through one or more juridical person, has ownership of or **entitlement to more than fifteen per cent**. of the property or capital or profits of such association or body of individuals;*

*(d) **where no natural person is identified under (a) or (b) or (c)** above, the **beneficial owner is the relevant natural person who holds the position of senior managing official**;*

*(e) **where the client is a trust**, the identification of beneficial owner(s) shall include **identification of the author of the trust, the trustee, the beneficiaries with fifteen per cent**. or more interest in the trust and **any other natural person exercising ultimate effective control** over the trust through a **chain of control or ownership**;"*

*[**Emphasis Supplied**]*

29. Therefore, what is piquant is that since the inception of the FPI Regulations, 2014, it had been the responsibility of the designated depository participant with which the FPI is registered, to ensure that the FPI does not have

an opaque structure. The FPI Regulations, 2014 were amended to provide that the term "ultimate beneficial owner" would mean the "beneficial owner" for purposes of the PMLA, with effect from December 31, 2018. By this amendment, it became abundantly clear that when the FPI Regulations, 2014 require identification of the "ultimate beneficial owner" it meant identification of the "beneficial owner" as stipulated in Rule 9 of the PMLA Rules. If this stipulation were not compiled with, it would lead to consequential action of potentially cancelling the registration of the FPI, removing its right to invest freely in the Indian stock market.

30. What is even more piquant is that on August 21, 2019, SEBI decided to delete the regulatory stipulation altogether. The deletion was made, accepting a slew of recommendations made by an expert Working Group appointed[15] by SEBI in a report dated May 24, 2019[16]. The Working Group's recommendations were also put out for public consultation including consultations with all other agencies including the Department of Revenue, Department of Economic Affairs, Reserve Bank of India and Ministry of Corporate Affairs. The recommendation of the Working Group stated as follows:

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[15]

[16] The report of the Committee headed Mr. H.R. Khan, former Deputy Governor, Reserve Bank of India is available at:

*"**All FPIs need to provide BO details** and **those who failed to provide** BO details including on account of bearer shares **cannot deal in securities market in India**. Thus, there is **no need for separate definition** of "opaque structure". The **"opaque structure" clause may therefore be removed** from FPI Regulations."*

[Emphasis Supplied]

31. The FPI Regulations, 2014[17], were repealed and replaced by the SEBI (Foreign Portfolio Investor) Regulations, 2019 [18] with effect from September 23, 2019. This version continued without any change to the amended position in this regard.

Legal Scope of the term "beneficial owner" under PMLA:

32. As seen earlier, the term "ultimate beneficial owner" was given the meaning given to it under the PMLA. Towards this end, circulars issued by SEBI invoke Rule 9 of the PMLA Rules. They refer to identification of natural persons who ultimately own or control an FPI but state that such persons should be identified in accordance with Rule 9 of the PMLA Rules.

33. In terms of the PMLA Rules, the determination of such ultimate owner, controller or person on whose behalf

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investments are made by the entity in question, is to be determined for any owner of such entity in question, holding 25% or more of such entity. The 25% ownership threshold to identify the ultimate beneficial owner under the anti-money laundering law was lowered by SEBI in its application to FPIs to 10% ownership threshold. This is quite consistent with the Companies Act, 2013, which too requires filings of ultimate beneficial owners for shareholders holding more than 10% in an Indian company.

34. On the strength of this requirement, in 2019, SEBI did away with the regulatory stipulation against having an "opaque ownership structure". The thinking evidently was that if every FPI was required to provide information about beneficial owners in respect of owners holding more than 10% of the FPI, there was no need to have a massive requirement to know the ultimate beneficial owner of every single owner of the FPI.

35. The complexity emerges from the fact that in FPIs that are collective investment pools such as mutual funds, 'participating shareholders' (the contributors) provide the funds that are placed under the control of the 'controlling shareholders' (the fund managers).

36. If a promoter were funding such participating shareholders, the simplest form would be to indirectly fund it by investing in the pool, but the key would be to

examine if the person funding the pool has a right to control decisions on behalf of the pool.

Adani Listed Companies and Public Shareholding:

37. The foundation of SEBI's suspicion that led to investigations into the shareholding of the FPIs in the Adani listed companies is that their ownership structure is "opaque" because the ultimate chain of ownership above the 13 overseas entities holding Adani Group stocks is not clear. SEBI has found 42 contributories to the assets under management of the 13 overseas entities, and has been pursuing various avenues to ascertain the same through engagement with overseas regulators and other Indian enforcement agencies.

38. The listed Adani companies assert compliance with minimum public shareholding requirements. In none of them do they admit to having promoter shareholding of above 75%. It has been a long-standing suspicion of SEBI that some of the public shareholders are not truly public shareholders and they could be fronts for the promoters of these companies.

39. Of the 13 overseas entities, 12 are registered as FPIs with SEBI through designated depository participants and one is a foreign financial body corporate. The collective holdings of these 13 overseas entities in the

six Adani listed companies between 2017 and 2020 has been summarised by SEBI in the table below:-

Company	FPIs/FI shareholding March 31, 2017 (%)	FPIs/FI shareholding March 31, 2018 (%)	FPIs/FI shareholding March 31, 2019 (%)	FPIs/FI shareholding March, 2020 (%)
Adani Enterprises Limited	12.87	16.91	14.96	15.56
Adani Transmission Limited	14.58	17.99	17.13	18.05
Adani Total Gas Limited	-	-	18.62	17.91
Adani Green Energy Limited	-	-	9.54	20.39
Adani Ports and Special Economic Zone Ltd.	6.53	-	-	-
Adani Power Limited	17.11	13.64	12.21	14.11

40. The probe by SEBI has therefore been focused on the ultimate economic ownership of these 13 overseas entities (the 12 FPIs and one financial institution).

Typically collective investment pools have two types of shareholders – shareholders who own the equity and control the funds raised, and shareholders who contribute the funds and participate in the returns generated by the controlling shareholders. It is the controlling shareholders who have title to the decisions taken by the collective investment pools.

41. Each of the 13 overseas entities has identified the beneficial owner for purposes of the PMLA Rules, and thereby these are the persons to be identified as the "ultimate beneficial owner" for purposes of the FPI Regulations. This is the information that the FPI Regulations require an FPI to provide, when sought. SEBI has confirmed that each of these 13 overseas entities have declared their ultimate beneficial owners as required by PMLA – it is as extracted below:-

Sl. No.	**FPI**	**Jurisdiction**	**Controlling shareholders**	**Name of BO Declared**	**Nationality / Country of operation of BO**
1	Elara India Opportunities Fund		Elara Capital PLC	Mr. Rajendra Bhatt	UK
2	Vespera Fund Limited		Elara Asset Management Ltd – held 100% by Elara Capital PLC	Mr. Rajendra Bhatt	UK

Sl. No.	FPI	Jurisdiction	Controlling shareholders	Name of BO Declared	Nationality / Country of operation of BO
3	Marshal Global Capital Fund Limited	Mauritius	Marshal Advisors Limited – held 100% by Lumen Capital Fund Pte Ltd	Mr. Nuni Venkata Ramana Murty	Singapore
4	Emerging India Focus Funds		Emerging India Fund Management Ltd – held by the Emerging Fund Trust	Trident Trust Company Limited as trustee of the trust – Mr. Jimmy Ernesta as settlor	Mauritius
5	EM Resurgent Fund		Emerging India Fund Management Ltd – held by the Emerging Fund Trust	Trident Trust Company Limited as trustee of the trust – Mr. Jimmy Ernesta as settlor	Mauritius
6	Cresta Fund Limited		Dertona Holdings Ltd.	Mr. Mark Dangel	Switzerland
7	Albula Fund Limited		Connor Investment Holdings Ltd	Ms. Anna Luzia von Senger Burger	Switzerland

Sl. No.	FPI	Jurisdiction	Controlling shareholders	Name of BO Declared	Nationality / Country of operation of BO
8	APMS Fund Limited		M. I. H. International Ltd	Mr Alastair Guggenbuhl-Even	Switzerland
				Mrs Yonca Even Guggenbuhl	Switzerland
9	LTS Investment Fund Ltd.		Helvetic Capital Management Ltd	Mr. Alastair Guggenbuehl-Even	Switzerland
10	Asia Investment Corporation (Mauritius) Limited		M. I. H. International Ltd	Mr Alastair Guggenbuhl-Even	Switzerland
				Mrs Yonca Even Guggenbuhl	Switzerland
11	Polus Global Fund		Fidelis Global Asset Management Ltd	Mr. Yajjadeo Lotun	Mauritius
12	New Leaina Investments Ltd.	Cyprus	Andetta Private Equity N V	Stitching for Sustainable Development, a Dutch Foundation – Mr. Jan Scheelings,	Netherlands

Sl. No.	FPI	Jurisdiction	Controlling shareholders	Name of BO Declared	Nationality / Country of operation of BO
				Ms. Margaret Ilse Sjak-Shie, Mr. Collin Peter de Wit.	
13	Opal Investments Pvt. Ltd (FI)	Mauritius	Zenith Commodities General Trading L.L.C.	Mr. Adel Hassan Ahmed Alali	UAE

42. Now, information about 42 investors in the FPIs who have invested their monies in these funds under the control of the beneficial owner identified and declared under the PMLA Rules, is available. These 42 contributors are spread across seven jurisdictions. It is the ownership pattern of these 42 investors about which SEBI has made references to the ED, CBDT and the regulators in various jurisdictions.

43. As noticed earlier, under the regulatory framework, the meaning of the term "ultimate beneficial owner" is to be adopted from the meaning of the term "beneficial owner" under Rule 9 of the PMLA Rules. A plain reading of Rule 9 of the PMLA Rules would show that in the context of FPIs, the "beneficial owner" is the natural person who has:-

a. where the FPI in question is a company, the beneficial owner is the natural person who has a "controlling ownership interest" or who exercises "control" through other means;

b. where the FPI in question is a partnership, the beneficial owner is the natural person who has an ownership of entitlement to more than 15% of the profits or capital in the partnership;

c. where the FPI in question is an unincorporated association or body of individuals, the beneficial owner is the natural person who has ownership or entitlement to more than 15% of the property or capital or profits of such association or body;

d. where no natural person is identified under the foregoing, the beneficial owner would be the natural person who holds the position of a senior managing official;

e. where the FPI in question is a trust, the author of the trust, the trustee and beneficiaries with interest of 15% or more in the trust property; or any natural person exercising ultimate effective control over the trust.

44. Therefore, at the heart of the provision is the person who has control over the FPI. If no person is identified, then senior officials would have to be identified. In the case of each of these FPIs, they have identified the beneficial owner for purposes of the PMLA. One would need to bring a case to show that these declarations are false. It does not appear that the Directorate of Enforcement ("**ED**") has taken a position that such declarations are inaccurate. SEBI has made a reference to the ED, and that is discussed subsequently.

45. The key issue therefore, is whether as the law stands, one could draw a conclusion that the FPIs are fronts for the promoters of the Adani Group. Indeed, what SEBI is investigating (and to be fair to SEBI it has been investigating this for years before the Hindenburg Report was published) is whether one could make a case that the FPIs are in fact investing funds of the promoters of Adani Group and therefore could be regarded as a front for the promoters. If such an outcome in the investigation would come about, it would mean that the promoters would not be compliant with the minimum public shareholding requirement.

46. SEBI has acknowledged that the declaration of those in control, and in effective control has been made in the capacity as the ultimate beneficial owner. However, SEBI has expressed suspicion about shareholders who have contributed capital that is invested by the FPIs.

SEBI has also stated that the controlling shareholders have full control and all the voting rights over the funds at the disposal of the FPIs.

47. SEBI has expressed its observations about participating shareholders in the following terms:-

> *"The economic interest in the above named 12 FPIs has been held by the PR shareholders [participating shareholders i.e. those with economic interest]. Investigation revealed that there were 42 such PR shareholders which are based out of multiple jurisdictions namely Cayman Islands, Malta, Curacao, British Virgin Islands, Bermuda, Ireland and United Kingdom. The brief observations regarding PR shareholders are as under:*
>
> - *Each of the 42 PR shareholders is incorporated in the form of a company in the abovementioned jurisdictions.*
>
> - *Each PR shareholder, incorporated as a company, in turn, has dual shareholding – Founder/ Controlling shareholders (CR shareholders) and Economic Interest shareholders who, in turn, have been found to be located across various jurisdictions including tax haven jurisdictions.*
>
> - *Details of the BOs of the CR shareholders of only 24 of the 42 PR shareholders were made available.*

- *Details of BOs of the remaining CR shareholders and the details of the EI shareholders of the 42 PR shareholders have not been made available so far."*

48. The material on record submitted by SEBI points to the controlling shareholders of the FPIs and the promoters of the Adani Group respectively, asserting that they are independent of each other. The Adani Group has affirmed on oath that no funds have been provided directly or indirectly by them to the FPIs to make investments in the listed Adani stocks. Likewise, it has been stated that the shareholders in control of the FPIs have similarly asserted an absence of connection with Adani and any funding by Adani.

49. The entire concern expressed by SEBI (and this precedes the publication of the Hindenburg Report) is that SEBI is unable to satisfy itself that the contributors of the funds to the FPIs are not linked to Adani. It appears that bank statements of the 13 entities were made available to SEBI and indeed bank account details of 42 participating shareholders were obtained. SEBI has been attempting to find out such contributors who have an economic interest in these FPIs. This is where it has hit a wall. It is evident that SEBI had drawn a blank in this investigation and the publication of the Hindenburg Report has revived SEBI's efforts to attempt

figuring out economic interest in the FPIs that have these investments in listed Adani stocks.

50. It is evident that such an exercise could be a voluminous one but potentially a journey without a destination. For instance, if SEBI were to get behind a contributing participating shareholder who has given funds to the FPI to invest on its behalf, and get to the shareholders of such contributors, it could well be that the contributors could in turn be bodies corporate or funds, and there could be multiple classes of shareholders and contributors above that level. The shareholder above could in turn have bodies corporate above it and so on, and it would be a humongous task to figure out who the ultimate beneficial owner is.

51. What is apparent is that the regulatory framework governing FPIs contains a specific stipulation for compliance with identification and disclosure of beneficial ownership. If such requirements have been complied with, the investigation is about whether the "spirit of the law" governing minimum public shareholding has been violated by reason of shareholding in the hands of FPIs that are compliant with the letter of the law.

52. What is also apparent is that SEBI has been investigating the matter since October 23, 2020 whereas the Hindenburg Report was published on January 24,

2023 – two years and three months later. It is however for SEBI to conclude its investigations in accordance with law within a precise timeframe. SEBI SEBI has made an application to the Hon'ble Supreme Court seeking extension of time to investigate, the Committee is refraining from commenting on this issue.

References to Other Enforcement Agencies:

53. In its pursuit of investors in the 13 overseas entities, SEBI has also made references on December 10, 2021 to the Central Board of Direct Taxes ("**CBDT**") and to the ED asking them to investigate for violation of tax law and PMLA respectively. Therefore, the Committee called upon these agencies to provide their explanations.

54. The response of the CBDT may be summarized as follows:-

a. SEBI had made a reference to the CBDT on December 10, 2021, on the premise that if it is established that the funds invested in the Adani Group through the FPIs were funds of the Adani Group or its promoters, it may lead to findings of tax evasion;

b. Unless a 'tax evasion petition' (the reference from SEBI would be one) contains specific, verifiable

and actionable intelligence, it cannot be taken up for investigation;

c. The tools available to the income-tax department to obtain information from overseas tax agencies are the double tax avoidance agreement ("**DTAA**"), tax information exchange agreement ("**TIEA**"), and multilateral convention on mutual administrative assistance in tax matters ("**MAAC**");

d. Of the jurisdictions in which the participating shareholders alluded to by SEBI reside, India has DTAA with three; TIEA with three and an exchange of information relationship with one;

e. An information requesting jurisdiction must "clearly establish foreseeable relevance" of the information sought for tax purposes and it cannot conduct roving and fishing enquiries;

f. Generic requests to foreign jurisdictions are not feasible since this leads to negative comments in the peer review by global agencies and it would impact India's reputation and such requests are not appreciated;

g. Recent intrusive searches into listed Indian companies with substantial foreign funding did not show that there was any adverse inference capable

of being drawn about such funding, as a rampant or endemic feature.

55. The response of the ED was quite similar to that the CBDT, and may be summarized as follows:-

a. SEBI stated that since the issue of tracing of fund flow falls under the domain of money laundering, which is under the purview of the ED, the reference was being made;

b. ED is not empowered to invoke the provisions of the PMLA without a prior registration of an offense falling within the scope of scheduled offences in the PMLA. SEBI had not filed any case under the scheduled offences listed in the PMLA;

c. The ED examined SEBI's reference under the PMLA as well as the Foreign Exchange Management Act, 1999 [19] ("**FEMA**") but no allegation of contravention of Section 12A of the Securities and Exchange Board of India Act, 1992[20] ("**SEBI Act**") or any violation of exchange controls has been reported by SEBI;

d. The ED has found intelligence about potentially violative and concerted selling by specific parties

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just ahead of the publication of the Hindenburg Report, and this may lead to credible charges of concerted destabilization of the Indian markets, and SEBI ought to be probing such actions under securities laws.

56. SEBI has also sought information from other securities commissions in other jurisdictions under the Multilateral Memorandum of Understanding [21] ("**MMOU**") to which members of the International Organisation of Securities Commissions[22] ("**IOSCO**") are parties. SEBI has submitted to the Committee that the IOSCO MMOU requires justification of reasons for seeking information. It appears that SEBI has drawn a blank from regulators in Cayman Islands, Malta, Curaçao, British Virgin Islands and Bermuda. Without more information (which can only be available after it is provided by these other agencies), it is apparent that SEBI is unable to make out a case for seeking information. SEBI has stated that it is now working on initiating a process of seeking amendments to the IOSCO MMOU in order to get better inputs from overseas regulators in the future.

57. The response of the ED and of the CBDT are quite similar in content to the requirements cited under the IOSCO MMOU. Besides, from the plain reading of Rule

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9 of the PMLA Rules, it is apparent that there is an incumbent declaration of who the beneficial owners are, by each of the FPIs, which would make them compliant with PMLA.

58. In a nutshell, SEBI's contention is that it needs information from these other agencies to be able to demonstrate a link to a potential violation. Without such information SEBI is unable to satisfy itself that its suspicion that has been aroused can be put to rest. The securities market regulator suspects wrongdoing, but also finds compliance with various stipulations in attendant regulations. Therefore, the record reveals a chicken-and-egg situation.

59. It is noteworthy that SEBI, in its legislative capacity, did away with the prohibition against any FPI having an "opaque structure" on the premise that declarations of the beneficial owner flows from Rule 9 of the PMLA Rules and that such a stipulation is sufficient for its regulatory purposes. Such compliance having been effected by the FPIs, coupled with the repeal of the provisions on "opaque structure", the chicken-and-egg situation of hoping to get evidence, can become a perpetual one.

60. Therefore, it appears that the legislative policy stance of SEBI on the ownership structure of FPIs has moved in one direction while the enforcement by SEBI is moving in the opposite direction.

61. It would be open to SEBI to amend the FPI Regulations to stipulate what level of economic interest should be declared by the FPIs in respect of those who own any stipulated proportion of the FPI. These are matters of legislative policy choice.

Committee's Conclusions:

62. At this stage, based on all the information provided by SEBI, it is apparent to the Committee that:-

a. SEBI has been suspecting 13 overseas entities of having links to the promoters of the Adani Group and thereby suspecting that the shareholding in the listed Adani stocks in the hands of these 13 overseas entities need not qualify as public shareholding;

b. If such holding is not public shareholding, the listed Adani companies would have violated Rule 19A of the SCRR;

c. At this stage, each of the 13 overseas entities have provided the details of the beneficial owners to the respective reporting entities and to SEBI in compliance with Rule 9 of the PMLA Rules;

d. According to SEBI, there is no demonstration that the persons declared to be beneficial owners are not "beneficial owners" for purposes of Rule 9 of the PMLA Rules;

e. Both the Adani promoters and the FPI's beneficial owners appear to have affirmed on oath that the FPI investments are not funded by the Adani Group;

f. In the instant case, it appears that SEBI is not able to make out a case, and such a position of the case not being made out is presented as a *prima facie* position, which cannot be confirmed unless more investigation is done. In any prosecution of proceedings, whether civil or criminal, the presentation of a "*prima facie*" case is the responsibility of the plaintiff or the prosecutor. Once a *prima facie* case is made out, the burden shifts to the accused;

g. The inversion of the process of proving a charge, leaves the matter in the realm of suspicion. It is trite law that suspicion, however strong, cannot replace proof. However, the publication of the Hindenburg Report has reinforced SEBI's suspicion that perhaps there is something amiss and it desires to probe this further, and is seeking time;

h. Even the fundamental rules of evidence would require a conclusion of whether an allegation is "proved", "disproved" or "not proved". At this stage, the factual matrix appears to place the matter in the realm of "not proved" – the regulator has not been able to prove that its suspicion can be translated into a firm case of prosecuting an allegation of violation.

Related Party Transactions

March of the Law:

63. The SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 [23] ("**LODR Regulations**") came into force on December 22, 2015.

64. These regulations defined a "related party transaction" in Regulation 2(1)(zb) as a transaction involving a transfer of resources between a listed entity and a "related party", regardless of whether a price is charged.

65. The term "related party", in Regulation 2(1)(zc) had the same meaning ascribed to it under Section 2(76) of the Companies Act, 2013 or under the accounting standards.

[23]

66. The definition of the term "related party" was amended to take effect on April 1, 2019, to provide that any person or entity belonging to the "promoter" or "promoter group" of the listed entity and held 20% of more of the shareholding in the listed entity shall be deemed to be a related party.

67. This amendment was based on recommendations of a Committee on Corporate Governance which made a report dated October 5, 2017 containing various recommendations on corporate governance. The recommendations were put out for public debate and after detailed deliberations these changes were made.

68. Subsequent amendments made in 2018, 2019, 2020, 2021 and 2022 changed the provisions that imposed regulatory obligations on related party transactions, but the definitions of "related party" and "related party transaction" were left unchanged.

69. On November 21, 2021, the regulations underwent substantial amendments yet again, but the amendments took care to ensure that amendments took prospective effect and that too from a deferred date. Most of these amendments took effect on April 1, 2022, but some specific amendments made in this round were given an even further deferred date to take effect (April 1, 2023).

70. In these amendments, the definition of "related party" was amended to include persons holding 20% or more in the listed company whether directly or indirectly or on a beneficial interest basis under Section 89 of the Companies Act, 2013 within the ambit of the term. With effect from April 1, 2023, the deemed inclusion would bring within the scope of the term "related party" persons who so hold 10% or more of the listed company.

71. The term "related party transaction" was also amended with a similar deferred prospective effect to expand its scope to cover transactions between a listed entity or any of its subsidiaries on the one hand, and a related party of either the listed company or its subsidiaries on the other. So also, to further the spirit of the regulatory coverage, the term was amended to include transactions between a listed company or its subsidiary on the one hand, and any other person (even if not a related party), if the purpose and effect of the transaction is to benefit a related party.

72. These amendments were necessitated to address the mischief or contrivance of effecting a transaction involving a transfer of resources between a listed company and a third party which is not a related party, only to technically escape the rigors of compliance applicable to a related party transaction, to thereafter transfer the resources from the unrelated party to a related party.

73. Suitable exceptions were made for transactions that have a uniform effect for all shareholders on a pari passu basis in proportion to their shareholding – transactions such as dividend, bonus issue, rights issue, buyback etc., which are offered to all shareholders in proportion to their shareholding.

74. The aforesaid summary describes the key to understanding the scope of the terms "related party" and "related party transactions". A comprehensive extract of the provisions defining these two terms that would show the movement of the various amendments is set out at **Annexure B** to this Report.

Allegations on Related Party Transactions:

75. The Committee asked SEBI to comment on each of the transactions referred to in the Hindenburg Report to enable the Committee to carry out its remit. After a detailed initial presentation made on April 2, 2023, SEBI made a more detailed presentation on these transactions on April 26, 2023.

76. The Hindenburg Report refers to over 6,000 related party transactions, and questions their appropriateness. That apart, ten transactions have been assailed as related party transactions that have not been disclosed but allegedly ought to have been disclosed.

77. SEBI has submitted that the transactions assailed in the Hindenburg Report could be classified into five types of structures. These are:-

a) **Two Step Structures**: Structures where the "second leg" of a transaction involves a listed entity and is disclosed, but the "first leg" of the transaction is between two private unlisted related parties. The two legs could be proximate or distant in time. The two legs are however, alleged to be connected to each other, on the premise that such connection makes the two legs of the transactions combine into a composite related party transaction.

b) **Indirect / Intermediated Structures**: Structures where the first leg of the transaction is between a listed entity and an unrelated party, and therefore not disclosed. The second leg would be between such third party and an entity that is a related party to the listed entity. The two legs could be proximate or distant in time. Neither leg is disclosed, each of it falling outside the definition of related party transactions.

c) **Associated Party Vs Related Party Structures**: Structures where the transaction is between a listed entity and a third party that is "closely

associated" with the promoter. However, such third party is not a "related party" as defined in the regulations, and therefore transactions with such party are not disclosed specially as a related party transaction.

d) **Subsidiary Company Structures**: Structures where the transactions are between a subsidiary of the listed entity and a related party. Such transactions not strictly involving the listed entity on the one side, are not treated as a related party transaction.

e) **Allegedly Questionable RPTs which have been reported**: Structures that already come under the ambit of RPTs under SEBI Regulations and have been disclosed, but where their appropriateness is questionable.

78. As regards transactions that are reported as related party transactions (covered by sub-para (e) above), it would necessarily follow that questioning their appropriateness by the market could be based on an opinion on business judgement but cannot be based on alleged violation of law. Put differently, if a listed entity is compliant with the law, the scope for discussing a violation of the law stands eroded. The appropriateness of the transaction may be subject matter of comment by the market. Competing and conflicting opinions would

inform price discovery of the securities issued by such listed entity. Whether the comments are fair or unfair, appropriate or inappropriate, are all matters covered by free speech and expression, subject to the reasonable restriction imposed by validly made regulations on the obligation to speak the truth and not misrepresent the truth.

79. The focus should then shift to the transactions that are not disclosed on the premise that they are not related party transactions (covered by sub-paras (a) to (d) above) and to then consider if they are related party transactions masquerading as transactions with unrelated third parties.

80. As seen above, the regulations defining "related party" and "related party transactions" have been constantly amended to expand their scope and bring within its sweep the transaction structures referred to above.

81. One regulatory approach would have been to test such structures on the strength of the regulations as they existed at the time the LODR Regulations were first notified. Section 12A of the SEBI Act, 1992 outlaws contrivances and devices that are structured to circumvent the law – in effect, a framework against anti-avoidance.

82. However, another regulatory approach is to make amendments to spell out what would be covered by the legal requirements. With related party transactions, over the years, SEBI, in its legislative capacity, has consistently and consciously chosen this path. The march of the law governing related party transactions is articulated in the section above.

83. The Constitution of India lays down a fundamental principle – all actions of human ingenuity are deemed to be permitted, unless validly made law makes an intervention and restricts it. Such interventions need to withstand the test of being intelligible, being reasoned and not being arbitrary, in order to be constitutionally valid. The rule of law is not that unless explicitly permitted, human action is prohibited, but that unless explicitly prohibited, human action is permitted.

84. SEBI submitted that no matter what the regulations stipulate, there will always be a structural vulnerability or an intrinsic opportunity to structure transactions in a way as to comply with the letter of the law while not necessarily abiding the spirit of the law. While SEBI submitted to the Committee that the Committee ought to recommend introduction of provisions akin to the general anti-avoidance rules that are now in vogue in tax laws, the fact remains that Section 12A of the SEBI Act, 1992 is but a provision enabling anti-avoidance

action, and has been in force right since October 29, 2002.

85. For ease of reference, the provisions of Section 12A of the SEBI Act are extracted below:-

> *12A.* ***No person shall directly or indirectly***—
>
> *(a)* ***use or employ****, in connection with the issue, purchase or sale of any securities listed or proposed to be listed on a recognized stock exchange,* ***any manipulative or deceptive device or contrivance in contravention of the provisions*** *of this Act or the rules or the regulations made thereunder;*
>
> *(b)* ***employ any device, scheme or artifice to defraud*** *in connection with issue or dealing in securities which are listed or proposed to be listed on a recognised stock exchange;*
>
> *(c)* ***engage in any act, practice, course of business which operates or would operate as fraud or deceit*** *upon any person, in connection with the issue, dealing in securities which are listed or proposed to be listed on a recognised stock exchange, in contravention of the provisions of this Act or the rules or the regulations made thereunder;*
>
> *(d) engage in insider trading;*
>
> *(e) deal in securities while in possession of material or non-public information or communicate such material or non-public information to any other person, in a manner*

which is in contravention of the provisions of this Act or the rules or the regulations made thereunder;

(f) acquire control of any company or securities more than the percentage of equity share capital of a company whose securities are listed or proposed to be listed on a recognised stock exchange in contravention of the regulations made under this Act.

[Emphasis Supplied]

86. As seen above, the approach adopted by SEBI has been to explicitly stipulate with a deferred prospective effect from April 1, 2022, that transactions involving a subsidiary of a listed company would be deemed to be a transaction with the listed entity. Likewise, SEBI has explicitly stipulated with effect from April 1, 2023 that transactions with an unrelated third party would be regarded as a transaction with a related party, if the purpose and intent of the transaction is to benefit a related party. The provision of a deferred prospective effect has enabled listed entities to rearrange their affairs in a manner that is not violative of the law. Such a "glide path" is a matter of good practice in economic legislation, where disruptive changes do not hurt the ease of appreciating what is expected of members of society, to be compliant and to ensure compliance.

87. Having adopted the path of making explicit stipulations prospectively, the path of testing the principles

underlying the regulations governing related party transactions has been abandoned. That being so, it would be legally infeasible to attack past transactions on the standards that have later been made applicable with prospective effect.

88. The Committee does not intend to criticize SEBI for having adopted the approach of explicitly stipulating requirements with prospective effect, in preference to the approach of testing the existing law on a principles-based approach. Such an adoption of choice is SEBI's prerogative in its legislative capacity, and an expression of its best judgement of what is appropriate policy. So long as there is nothing unreasonable or subversive in choosing one path over the other, there is no scope for an adverse comment on the approach or to arrive at a finding of a "regulatory failure".

89. However, the Committee believes that once an approach is adopted, it must be implemented and adhered to, in accordance with law. Predictability and certainty are vital elements of regulation since a majority of society would desire to be compliant and therefore would wish to know what it ought to do, to remain compliant. If past transactions were compliant with the law as was applicable when they were transacted, and more so, if changes have been made subsequently to outlaw a repetition of such past transactions, it would follow that there can neither be a repetition of the same structures

in future nor can there be an attack on the validity of the past transactions.

90. As regards the principle of introducing "long business association" as rendering a business counterparty to be a "related party", some caution would be in order. Certainty and consistency in servicing a business relationship is a virtue and unless there is a strong benefit associated with burdening an arms-length business relationship as being a "related party transaction" for no reason other than having been a long-standing relationship, the measure may lead to an imbalance between the costs of the measure and the benefits from the measure. If the terms of contract with such a party were to be forced by law to be made public, it would impose a burden on such a counterparty that his competitors would not face. The appropriateness of such an approach is an important dimension and must be handled with great care.

91. SEBI has submitted that long association has been the basis of impacting the independence of an independent director (with the law imposing a term limit) and the basis of auditor rotation (term limit on serving as statutory auditor). The role of independent director is one of overseeing governance while the role of an auditor is one of being a check and balance and auditing compliance. Such relationships have an element of fiduciary accountability and a prolonged association

could erode the independence and fairness expected from a person playing that role.

92. SEBI has also repeatedly submitted to the Committee that the transactions may be technically compliant with the letter of the law and it may be difficult to prove a violation in a court of law but the spirit and purpose of the law may have been violated. At this stage, the Committee does not desire to express any view on merits, since its remit is not to conduct a parallel probe and express an opinion on individual transactions, particularly, when SEBI is expressing a desire for more time to investigate and return findings more firm than *prima facie* findings.

93. However, the remit of the Committee clearly is to examine if there is any regulatory failure in the wake of the allegations made. Towards this end, purely for purposes of a flavour of the facts on hand, the detailed presentations made by SEBI in respect of each of the 12 suspicious transactions are annexed in the Compilation of Submissions.

94. A few big-picture facets that are *ex facie* evident, are worth spelling out, with specific regard to the regulatory framework governing related party transactions:-

a. The allegation of non-disclosure is not sustainable since by the application of the legal definition of "related party" none of the counter-parties were

related parties in the eyes of the law at the time of the transactions;

b. SEBI's pursuit of investigations is based on the premise that it is pursuing the "spirit of the law", which flies in the teeth of the prospective amendments with deferred effect that SEBI has made on the legislative side;

c. Some transactions relate to the period of nearly a decade ago, which predate the LODR Regulations, when the listing agreement was the instrument of law that was applicable;

d. Several transactions are evidently transactions with parties that do not fit the definition of "related party", but other transactions between such unrelated parties and related parties have led to the allegation of the spirit being violated; and

e. Some transactions are transactions between the subsidiary of the listed entity and the related party, which SEBI has brought under coverage of the law governing related party transactions only with effect from April 1, 2022 and that too with deferred prospective effect.

95. The Committee notes that predictability of the law is an important touchstone for economic legislation. SEBI

has been actively learning from developments in the market and has consistently been reacting to such learning by regular amendments to the regulatory framework.

96. A key question that would then emerge is whether a commercial business can be accused of violating the law when the law at the relevant time did not not exist or did exist but in a manner and form materially different from how it is formulated later.

97. Therefore, arguably, when the LODR Regulations make a reference to the listed entity, it could be argued that such reference included in its sweep, an inclusion of its subsidiaries. A person alleging a violation could argue that what is prohibited from being done or is regulated in how it can be done, cannot be effected indirectly through a subsidiary, without being hit by the prohibition of the regulation.

98. However, in the eyes of the law, the picture completely changes when the regulations are positively amended with specific regard to preventing the possibility of such an interpretation. Even amendments to the law could be of two types – clarificatory amendments and substantive amendments. It is trite law that substantive amendments can take prospective effect while clarificatory amendments would clarify the

existing provisions and therefore would relate to how the regulations must be interpreted.

99. In the instant case, on November 21, 2021, the LODR Regulations were amended (for the sixth time that year) and that too with a two deferred effective dates of April 1, 2022 and April 1, 2023, to expand the scope of "related party transactions". A contrivance or a device would have to be proven that a transaction purporting to be a transaction with an unrelated party is actually a related party transaction masquerading as a normal transaction. But such a framework would take effect from April 1, 2022, and therefore transactions prior to such date cannot be accused of being violative.

100. Since the amendments were not only given prospective deferred effect, but also were given an effective date that would start with the next financial year, it is evident that the legislative intervention was a substantive one, taking care to provide listed entities with time to re-arrange their affairs to remain compliant. Therefore, it would not be legally tenable to assail transactions that were evidently effected when the newly envisaged substantive law did not exist, on the premise that they violated the law.

101. SEBI is still investigating the matter and is examining old transactions to arrive at a view on whether there was any fraud in the underlying facts and their depiction.

The Committee is therefore anxious not to comment on the merits of any fact under investigation, and has therefore restricted itself to the law and its application.

102. The Committee is equally cognizant of the fact that the allegations in the Hindenburg Report are substantially based on publicly available information. However, the manner in which it has extrapolated the information and presented it, has led to a serious nose-dive in the prices of Adani stocks. The prices have undergone a correction and have improved but not to the level as existing prior to January 24, 2023, the date of publication of the Hindenburg Report.

103. This points to a simple thesis – the market has factored in the seriousness of the allegations on the commercial facets of the transactions in question. Regardless of whether the law is violated, the market has decided to re-price the Adani stocks. There has been an infliction of a price erosion and a subsequent mitigation. Every action that is legally compliant need not be an action that is considered desirable. If the market feels the actions taken in the past were not entirely desirable, it would re-price the stocks, but that by no means can be extrapolated to inexorably conclude that a violation of law has been made out in the facts of the case.

Committee's Conclusions:

104. The Committee therefore returns the following conclusions:-

a. The Committee would like to reiterate that it is only setting out the position in the law, with the specific regard to whether there has been a regulatory failure;

b. In the facts of the case, it is evident that SEBI has been getting feedback about such transactions from the market and has responded by amending the regulations. Therefore, it would be difficult to arrive at a finding of a regulatory failure on the legislative side, when SEBI has been intervening to regularly raise the bar in its stipulation of desirable conduct;

c. However, while the legislative policy has proceeded in one direction, enforcement policy cannot move in a diametrically opposite direction. The manner of enforcement ought to be consistent, coherent and decisive, in consonance with publicly declared law;

d. Once SEBI has taken the legislative position (in November 2021) that transactions between related parties and subsidiaries of listed companies would come within the coverage of related party

transactions only with a deferred prospective effect (with effect from April 1, 2022), it cannot assail past transactions effected even before November 2021 as being violative of law that has been stated by it as not being in force when the transactions were effected;

e. Likewise, once SEBI has made a legislative stipulation (in November 2021) that transactions with unrelated parties would fall within the scope of related party transactions if it can be shown that the intent and purpose of the transaction is to benefit a related party, with deferred prospective effect (with effect from April 1, 2023), it cannot assail transactions effected in the past as being in violation of law that has been stated by it as not being in force when the transactions were effected;

f. Invoking the spirit of the law would not suffice to pursue a credible means of investigation into the matter, keeping a cloud over the transactions;

g. Assuming the law to have been applicable when the transactions were effected, it must be noted that the Hon'ble Supreme Court has repeatedly held in matters relating to securities law that enforcement must be taken up with promptitude and reasonable

proximity of time with the occurrence of the events suspected to be violative[24];

h. SEBI has been probing the matter since October 23, 2020 after receipt of complaints in June 2020 and July 2020. The amendments to the definitions of the terms "related party" and "related party transactions" were made in November 2021 and took effect on April 1, 2022 and April 1, 2023, with material and substantive changes being made;

105. The Committee believes there is a need for an effective enforcement policy that is coherent and consistent with the legislative position adopted by SEBI, so that precious regulatory resources are not expended on regulatory action that is infirm on the ground of applying the law retrospectively.

Price Manipulation in Adani Scrips

106. In dealing with the remit of assessing if there has been regulatory failure, one of the points on which SEBI is to apprise the Committee is whether there has been price manipulation in the Adani stocks.

107. The Committee called for a briefing from SEBI on the historical price movements in the Adani stocks and what SEBI's approach had been as part of its

[24] Adjudicating Officer, SEBI vs. Bhavesh Pabari. See

surveillance of the market. The Committee also asked the invitees to comment on the subject.

108. SEBI pointed out that it has in place automated surveillance systems to monitor trading activity and price movements to point to detection of potential price or volume manipulation and other market abuse. From the data generated in the course of trading, alerts are generated by the algorithm that mines the data, after which the alerts lead to analysis based on set criteria including:-

a. Concentration of net buyers/ net sellers in the scrip;

b. Contribution of net buyers to the increase in Last Traded Price ("**LTP**") during a price rise period and contribution of net sellers during price fall period;

c. Whether any group of entities traded among themselves, which might have led to increase/ decrease in the price of the scrip;

d. Whether delivery was taken by the entities in a scrip and what proportion of deliveries were taken vis-a-vis their trading volume in that particular scrip;

e. Trading behavior of the top LTP contributors in a particular scrip vis-a-vis their trading behavior across all other scrips;

f. Category of entities appearing in the top net buyers, net sellers and net LTP contributors e.g. Sovereign Wealth Funds, Mutual Funds, brokers, individuals, etc.;

g. Whether the trading entities profited or incurred losses from the trades;

h. Concurrent corporate announcements or news flows about the company, triggering positive or negative sentiment in the scrip;

109. Factoring in the above factors, if the trading pattern appears to be suspicious the alerts are considered for further detailed examination. If the trading pattern does not arouse suspicion, then the alerts are closed.

110. SEBI submitted that based on the aforesaid factors, the price movement in the Adani stocks had been considered by the stock exchanges on four occasions and they had submitted a report to SEBI. Two of these were well prior to the Hindenburg Report and two were after January 24, 2023. The following table summarises the position:

Report No.	Period of Examination	Date of submission of report to SEBI
Pre- Hindenburg report		
1	October 01, 2019 to September 18, 2020	September 28, 2020
2	October 01, 2019 to April 30, 2021	May 10, 2021
Post-Hindenburg Report		
3	May 01, 2021 to December 31, 2022	March 20, 2023
4	October 24, 2022 to February 10, 2023	March 14, 2023

111. In all the above four reports, the Stock Exchanges considered the factors mentioned above, and *prima facie*, found no evidence of any artificiality to the price rise and did not find material to attribute the rise to any single entity or group of connected entities.

112. From the first report mentioned above, SEBI submits that it observed that a set of common FPIs were having shareholding across the Adani Group companies, which led to a further detailed examination. It appears that the report received in September 2020 coincided with the complaints received by SEBI in June 2020 and July 2020 and eventually led to the formal investigation that commenced on October 23, 2020.

113. The investigation then was not into any alleged price manipulation, considering that there was no evidence of

the FPIs having manipulated the stocks (they were net sellers as will be seen later) but investigations into potential violation of minimum public shareholding as a result of the FPIs was underway.

114. Likewise, there was also a reference to common FPIs found in the second report received in May 2021. SEBI submits that pending investigation triggered by the earlier report, SEBI undertook a review of the ASM framework in June 2021 and some added criteria were added.

115. SEBI also submitted that the Adani Group scrips have been were subjected to various surveillance measures under the ASM framework. Data relating to such surveillance is summarised in the table below. It is evident that trading in each of the seven stocks has been scrutinised and kept under watch.

S. No.	**Scrip Name**	**Date on which ASM got triggered first (A)**	**Total No. of days since (A) till March 25, 2023**	**Total No. of days for which ASM was applicable**
1.	Adani Green Energy Ltd.	October 14, 2019	1257	567
2.	Adani Power Ltd.	December 15, 2020	829	530
3.	Adani Transmission Ltd.	August 30, 2018	1667	555
4.	Adani Total Gas Ltd.	December 20, 2020	824	540

S. No.	Scrip Name	Date on which ASM got triggered first (A)	Total No. of days since (A) till March 25, 2023	Total No. of days for which ASM was applicable
5.	Adani Wilmar Ltd.#	April 28, 2022	330	159
6.	Adani Enterprises Ltd.*	February 03, 2023	49	41
7.	Adani Ports and Special Economic Zone Ltd.*	February 03, 2023	49	10

 # Adani Wilmar was listed on February 08, 2022.

** These scrips are part of F&O segment, on which only short term ASM is applicable. Further, short term ASM became applicable in F&O segment from April 28, 2022.*

116. A study of the table above would show that the Adani stocks had indeed been under watch by SEBI. The application of ASM measures (discussed in Chapter Three) would mean that investors were alerted and cautioned about the price rise. It is a matter of record that SEBI has stated it did not find any evidence of "wash trades" (where connected parties transact in a stock continually with one another without any intention to actually transfer ownership of the stock).

117. If none of the attendant factors that warrant a deeper and further probe was found, and indeed SEBI kept a watch in light of its concurrent probe into the suspicion about the minimum public shareholding, it stands to reason that one cannot return a finding of a regulatory failure.

118. SEBI submitted comparative data about other stocks from other parts of the world with sharp price movements. The Committee does not intend to compare price rise trends across stocks across industries since the Committee's remit is not to examine whether the price rise was justified, whereas its remit is to ascertain if there was a regulatory failure. Whether what a reasonable regulator ought to do when faced with such trends was done, is the question to ask, and it is apparent that SEBI was actively engaged with developments and price movements in the market. All the submissions of SEBI in this regard are contained in the accompanying Compilation of Submissions.

119. SEBI also submitted that it examined whether there has been any unusual trading pattern proximate to the release of the Hindenburg Report, i.e. during the period January 18, 2023 to January 31, 2023. While there was no adverse observation with respect to Adani scrips in the cash segment, suspicious trading has been observed on the part of six entities. These are four FPIs (not from among the 12 FPIs suspected in relation to minimum public shareholding), one body corporate and one individual.

120. The trading pattern here is suspicious because of the build up of short positions by these entities in the Adani scrips prior to the Hindenburg Report, and substantial profits earned by them by squaring off their short positions after publication of the Hindenburg report on January 24, 2023.

121. A detailed investigation is being carried out in respect of the trading of the aforesaid six entities. These being matters under investigation, and the factual findings at this stage being *prima facie* in nature, the Committee is not delving into the details and names of these persons, or commenting upon the quality of the *prima facie* evidence. The Committee wishes to ensure that the position of the respective parties, including SEBI, is not compromised either way when investigations are pending.

122. As regards the trading period between April 1, 2018 and December 31, 2022 (the calendar month prior to the publication of the Hindenburg Report), the Committee learnt that a total of 849 alerts had been received from the automated system in respect of Adani group scrips. These include online alerts, complaints and references, and were examined by Stock Exchanges, applying the factors listed at the start of this sub-chapter.

123. The examination has not been entirely passive since intrusive efforts such as examination of promoter pledge, KYC details of the investors, bank statements of investors taken from brokers, and the like, have been studied.

124. These regulatory interventions have led to the Stock Exchanges submitted three examination reports to SEBI, on which work is in progress. Details of these examination reports are summarised below:

S. No.	Scrip covered	Period of Examination	Date of receipt of report
1.	Adani Green Energy Ltd	Mar 01, 2021 to Jun 30, 2021	June 02, 2022
2.	Adani Power limited	Feb 01, 2022 to Apr 30, 2022	December 20, 2022
3.	Adani Green Energy Ltd	Feb 21, 2022 to Apr 20, 2022	January 03, 2023

125. SEBI has submitted that out of the total 849 alerts, 603 alerts were related to price volume movements, while the remaining 246 alerts were related to suspected insider trading. The 603 alerts were closed after processing the same as per approved the standard operating procedures, and the 246 alerts were processed from the perspective of suspected insider trading and have led to the aforesaid three reports submitted to SEBI.

126. Upon queries from the Committee for more granular information on how SEBI has handled the alerts and the journey between the alerts and the eventual views taken on them, SEBI presented at the submission made on April 26, 2023, a detailed tabular grid, taking trading in shares of Adani Enterprises Ltd as an illustration.

127. The charts presented in this regard are part of the Compilation of Submissions, and specifics are not being elaborated in this report. However, in a nutshell:-

a. The price of AEL shares, between March 01, 2020 and December 31, 2022 increased from Rs. 219 to Rs. 3,859;

b. The period has been divided into four "patches" on the basis of the price movement, and trading in these patches has been analysed;

c. In Patch 1 (March 01, 2020 to August 31, 2020), the FPIs suspected as linked to Adani Group were net buyers for around 1.25 crore shares but this was a small proportion of the total delivery quantity in this patch, at 11.73 crore shares;

d. Analysis of the buyers responsible for the highest contribution to the LTP showed that these FPIs did not figure amount them. In this patch, the purchases by these FPIs could be said to have contributed to an increase from the LTP by less than 0.1% - meaning thereby, it cannot be reasonably alleged that these FPIs were indulging in artificial price rise since the purchases appears to be almost at prevailing market price;

e. The top 25 net LTP contributors, collectively contributed only around 15.26% to the LTP, with no single entity contributing more than 5%;

f. As regards Patch 2 (September 01, 2020 to September 30, 2020) Life Insurance Corporation

was the largest net seller, having sold 50 lakh shares of the stock. Large and well-known FPIs and mutual funds were net buyers in this patch;

g. The top 25 net LTP contributors, collectively contributed 14.82% to the LTP with no single entity contributing significantly more than 5%;

h. The next segment i.e. Patch 3 (October 1, 2020 to March 31, 2021) saw the price rise from around Rs. 300 to Rs. 1,031;

i. The top net buyers were large and well known FPIs and Mutual Funds and they bought around 1 crore shares;

j. FPIs from among those suspected of being linked to Adani too purchased in this patch, but a minuscule component. The top 25 net LTP contributors, collectively contributed only around 14.14% to the LTP with no single entity contributing more than 5%;

k. Finally, in Patch 4 (April 1, 2021 to December 31, 2022), in which the price shot up from around Rs. 1,031 to Rs. 3,859, the largest net buyer was LIC, buying around 4.8 crore shares;

l. The FPIs under watch were actually among the top net sellers, having sold around 8.6 crore shares

during this patch where the price rose, rendering it impossible to conclude that they had a hand in the price rise;

m. The top 25 net LTP contributors, collectively contributed only around 13.89% to the LTP with no single entity contributing more than 5%;

n. Though, no single entity had contributed significantly to LTP across the patches, one entity appeared across the different patches amongst the top 25 net LTP contributors. Therefore, the trading activity of the said entity in the Adani stocks as compared with trading across all other stocks in these periods, was analysed. The trading concentration in Adani stocks ranged from 1.24% to 3.08% of its total trading, which is insignificant and not unusual.

128. As a result, it was submitted by SEBI that while the price rise of shares of AEL rose as discussed above, no evident pattern of manipulative contribution to price rise could be attributed to any single entity or group of connected entities.

129. The Committee has asked SEBI to prepare similar charts with data across all the Adani stocks and present the same for analysis. This can be work in progress as indeed is the intended probe into those who build short

positions just ahead of the publication of the Hindenburg Report and profited from the price crash upon publication on January 24, 2023.

Committee's Conclusions:

130. As stated earlier, the Committee's remit is not to examine whether the price rise was justified, whereas its remit is to ascertain if there was a regulatory failure. It is apparent that SEBI was actively engaged with developments and price movements in the market.

131. The Committee notes that all such investigations must be completed in a time-bound manner. At this stage, taking into account the explanations provided by SEBI, supported by empirical data, *prima facie*, it would not be possible for the Committee to conclude that there has been a regulatory failure around the allegation of price manipulation.

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CHAPTER FIVE

REGULATORY FRAMEWORK AND COMPLIANCE – STRENGTHENING MEASURES

Introduction:

1. In the preceding chapters, we have dealt with the nature and scope of the alleged violations and discussed whether it can be said that there has been a regulatory failure in dealing with the alleged violations.

2. In this Chapter we deal with the subject of what measures we would suggest in order to strengthen the statutory and regulatory framework, and to secure compliance with the existing statutory and regulatory framework for investor protection.

Existing Framework:

3. Before suggesting measures to improve the statutory and regulatory framework, it is important to have an overview of key elements of the existing framework. The regulatory framework for the securities market is overseen by SEBI as the specialised regulator, with wide powers conferred on SEBI by Parliament under the SEBI

Act, 1992, to discharge its twin mandate of orderly development of the securities market as well as protection of interests of investors in the securities market.

4. SEBI has been vested, by law with the entire gamut of powers of the State – legislative, executive and judicial – all rolled into one organisation. The scale and scope of this power can be seen from just a plain reading of Section 11(1) of the SEBI Act, which provides as follows: -

> *"Subject to the provisions of this Act,* ***it shall be the duty of the Board***[25] *to protect the interests of investors in securities and to promote the development of, and to regulate the securities market, by such measures as it thinks fit."*

5. An illustrative list of the "measures" is set out in Section 11(2) and that is without prejudice to the generality of Section 11(1). Indeed, SEBI has the power to make subordinate legislation[26]; investigate violations of such legislation[27], with statutory powers at its command; and quasi-judicially adjudicate[28] the alleged violations – all on its own. Using the power to legislate, extensive subordinate legislation in the form of regulations have been made. Such regulations deal with market abuse,

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[25] Securities and Exchange Board of India
[26] Section 30, read with Section 11 of the SEBI Act
[27] Section 11C of the SEBI Act
[28] Issuance of directions under Sections 11 and 11B of the SEBI Act, and impose monetary penalties under Chapter VI-A of the SEBI Act

and do not just cover market intermediaries over whom SEBI has licensing powers [29] but also market participants who do not need a certificate of registration from SEBI – such as companies that issue securities, traders who trade in securities and employees and directors of organisations that are connected to the securities market. The jurisdiction of SEBI extends not only to "market intermediaries" [30] but also "persons associated with the securities market"[31].

6. Adjudication of criminal prosecution alone is kept out of SEBI's hands, where SEBI has to satisfy an independent judge in the criminal justice system, about its allegations of a violation having occurred[32]. All the other powers of regulatory intervention comport to the civil standard and the judicial authority for determination of findings of fact and law, are vested in officers of SEBI.

7. There is another facet of the matter. Criminal prosecution entails demonstrating the charges alleged, beyond reasonable doubt (the criminal standard of proof) while the civil prosecution for issuance of directions and imposition of penalties entails adopting the standard of preponderance of probability (the civil standard of proof). Preponderance of probability entails

[29] Various activities in the securities market can only be conducted by stipulated market intermediaries who necessarily have to obtain a certificate of registration from SEBI under Section 12 of the SEBI Act
[30] Those who require a certificate of registration under Section 12
[31] A term that has been judicially interpreted to include any person who has ever invested in any security
[32] Section 24 of the SEBI Act

drawing a reasonable conclusion as to which of the competing versions of what likely happened would seem more plausible and reasonable to a reasonable mind (not a fanciful mind – the sharp distinction being between "possibilities" and "probabilities").

8. That apart, since the doctrine of separation of powers is not strictly followed in regulatory design for any financial sector regulators, as a matter of legal requirement, such regulators are not mandated by law to segregate and separate these powers of the State – an element that is judicially recognised as a basic feature of the Constitution of India. Indeed, of their own accord or by necessary practice, organisations like SEBI have to separate these powers at least in form, by creating separate departments in making the legislation and its working conform to constitutionality.

9. However, the legal framework is lacking in mandating such separation as matter of the law governing the structural design of regulators. Human resources of the regulator are fungible within the regulatory organisation, with officers serving the executive side and the quasi-judicial side being capable of transfers without legal stipulations such as prohibition of communication and correspondence between the quasi-judicial department and the enforcement department, or any mandatory cooling-off period before an enforcement

official can take up a quasi-judicial role in the organisation.

10. Section 11C confers robust powers on SEBI to investigate any matter where it has formed a reasonable ground to believe that an investigation is warranted. Powers of a civil court empowering issuance of summons, calling for information or for attendance of persons and examining them on oath are conferred upon SEBI. The power to investigate is also embellished with a statutory duty cast on any person from whom SEBI seeks information to provide the same.

11. These provisions constitute the basis on which SEBI has wide access to call data records and meta data about communication among persons being investigated – data that would enable determining even the physical location of persons who are communicating; the number of times they have communicated; even access to CCTV camera footage held by banks and market participants. SEBI has put such powers to effective use and examined market abuse with a degree of sophistication in its investigative powers.

12. Besides, failure to respond to SEBI can be visited with both monetary penalties as well as criminal prosecution. Powers to search premises[33], to impound amounts equivalent to suspected value of illegal transactions[34]

[33] Section 11C(9) of the SEBI Act
[34] Section 11(4)(d) of the SEBI Act

and to disgorge amounts equal to wrongful gains made or loss averted[35] have been conferred. SEBI is also empowered to issue *ex parte ad interim* restraints on individuals suspected of wrongdoing from trading in securities, or accessing the market, or indeed from doing any specific type of activity as the situation demands [36] – the economic variation of preventive detention or bar on assembly of persons who are likely to disturb public order and peace.

13. The check and balance against SEBI's actions in its civil proceedings is a post-facto post-decisional appellate review in the form of a first appeal before the Securities Appellate Tribunal ("**SAT**") – any "order" passed by SEBI is subject to such appellate review[37]. Appeals from the decisions of the SAT lie in the Supreme Court of India and that too only on questions of law[38].

14. In short, the current statutory framework in which SEBI functions is a robust one, empowering SEBI with strong statutory powers at its disposal. It cannot be said that SEBI lacks powers to act and intervene in the case of wrongdoing in the securities market.

15. Therefore, the key question that the Committee had to examine is how to make the regulatory framework more effective. Towards this end, the Committee benefitted

[35] Section 11B(1) of the SEBI Act
[36] Sections 11(4) and 11B of the SEBI Act
[37] Section 15T of the SEBI Act
[38] Section 15Z of the SEBI Act

immensely from much of the seminal work that has been done by the Financial Sector Legislative Reform Commission, chaired by Justice (Retd.) B.N. Srikrishna, which, after extensive public deliberations, drafted the Indian Financial Code, with a robust framework on regulatory design and the law governing law-making.

16. Some of the reform recommendations of the FSLRC – in particular, those aimed at reforming regulatory organisational structure, investor grievance redressal and systemic risk – lend themselves to reiteration, in the context of the work done by this Committee within its remit.

Structural Reform:

17. SEBI performs multiple complex functions in its regulatory role. It ranges from a licensing role (by registering market intermediaries and stipulating quantitative norms such as minimum capital requirements and qualitative norms such as composition of those in governance of market intermediaries) to a policy-making and legislative role, to an investigative role, to an adjudicatory role (quasi-judicial determination of questions of fact and law).

18. Yet, investor protection is an abiding one that permeates SEBI's functions across these roles. Every measure of SEBI can be referable to the mantra of investor

protection including prudential regulation (such as stipulating networth requirements), resolution of failing market intermediaries (taking measures to deal with defaults and failures of market participants), corporate governance for listed companies (listing regulations) and development and orderly growth of the securities market (advocacy role).

19. For these functions to be appropriately performed, the regulator must be well structured and its own governance must be well thought through. Effective measures to ensure better regulatory governance would lead to greater transparency in law-making, greater societal involvement in contributing to the law, and consequently greater acceptance and compliance with the regulations. Provisions that bring out better regulatory governance would essentially involve stipulation of legal obligations for government and for regulators, that would lead to a more empowered, autonomous and effectively functioning regulator.

Suggested Measures:

20. Based on deliberations of the Committee and review of the rich material that is available in the field of capital markets regulatory policy, and keeping in mind the remit of the Committee, with a view to strengthen the existing statutory and regulatory framework, and to secure better compliance with the existing framework,

the Committee suggests implementation of the measures set out in the following paragraphs.

Effective Enforcement Policy:

21. A clear view that emerged in the Committee's deliberations is that there is a need to develop a proper enforcement policy that would optimise the utilisation of precious regulatory resources on the field.

22. Proceedings initiated by SEBI in 2021-22 have sky-rocketed to 7,195 cases as compared with 562 cases in 2020-21 and 249 cases in 2019-20. The sheer increase in the proceedings initiated begs the need to analyse if the settlement option is a viable alternative. Every case initiated entails an adjudicating official committing time, energy and resources to it and adjudicating if the executive arm of SEBI has a case to make out that can be upheld on the quasi-judicial side. Every adverse order then has two layers of appeal as a check and balance – first, to the SAT, and then to the Hon'ble Supreme Court, each of which would also expend energy and resources on each appeal. Statistics from the SAT on the institution, disposal and pendency of appeals and miscellaneous applications are set out in the accompanying Compilation.

23. An effective enforcement policy would mean laying down criteria on the basis of which SEBI may choose from the wide-ranging scope of measures available to it. For instance, the criteria by which SEBI must choose whether to initiate proceedings to impose monetary penalty; as opposed to proceedings to issue remedial directions; or indeed launch criminal prosecution, should all be clear, reasoned and non-arbitrary.

24. The cost inflicted with an issuance of direction not to deal in securities cannot be quantified easily, and further complexity would be added by the period for which such directions are issued. Therefore, it is even more vital that the criteria on which choice of regulatory weapon can be made, is clearly spelt out.

25. There is also the element of the approach to enforcement having to be consistent with the legislation and policy stance of SEBI. SEBI must not seek to prosecute old facts with an allegation of violating the ingredients of new law that has emerged from its own amendments. If the existing regulation does not adequately address a desired regulatory objective, and amendments are made, care should be taken to enforce the changed law prospectively.

Judicial Discipline:

26. Besides, different Adjudicating Officers and different Whole Time Members must not take conflicting positions on the same issue. Once SEBI has ruled on an issue in a particular way, judicial discipline would require that subsequent quasi-judicial iterations must adopt the same ratio, unless the ratio has been upset or re-stated in appeal, in which case the ratio would apply with its modification by the courts.

27. If a ruling by SEBI is set aside, unless the appellate order is stayed by the Hon'ble Supreme Court or a writ court, adjudication by SEBI must abide by the law declared by the appellate order. That the statutory right to appeal has been filed is no ground to ignore the law declared in the order appealed against. If this principle is not followed, it would be akin to a person SEBI has acted against, repeating his violation on the premise that he has appealed SEBI's order and claiming that SEBI's order is not binding on him.

Robust Settlement Policy:

28. Data presented by SEBI with statistics on settlement points to the fact that the approach to settlement of proceedings is still not robust. There is an unstated perception of reluctance to settle potential proceedings arising from causes of action identified. SEBI has formulated objective criteria in regulations governing settlement of proceedings and therefore there should be

very little scope to not be objective about the terms of settlement.

29. To effect settlements, SEBI has proposals of settlement filed by noticees vetted by an "Internal Committee" which puts up its recommendations to a "High Powered Advisory Committee". The HPAC gives its recommendation which is dealt with by a panel of Whole Time Members of SEBI. The Committee sought data on settlement proceedings and the information available at this stage does not lend itself a high quality of empirical analysis.

30. Some trends are however visible. Data submitted by SEBI shows that for the years 2019-20, 2020-21 and 2021-22, SEBI has not differed with the HPAC in a single case – a break-down of the recommendation being one of accepting a settlement or rejecting a settlement is not available. Likewise, data from SEBI does not throw any light on the percentages of cases in which the Internal Committee recommends acceptance and rejection, and in how many of those, the HPAC takes a different view. So also, data on cases disposed in a year includes disposal of cases pending from previous years. While this will not indicate the percentage clearance of cases, it points to cases remaining pending across years. A time-bound disposal must be embedded in the law.

31. All of this needs a deeper empirical study. If SEBI desires to initiate enforcement in over 7,000 cases in a year, it must put in place a coherent policy on settlement of proceedings, whereby financial injury commensurate with the alleged violation may be inflicted on the party and yet precious resources need not be expended where a settlement is possible, achieving a remediation that subserves regulatory objectives. This is a universal principle for securities regulations worldwide and there need be no exception for India. In the heightened initiation of enforcement, while the absolute number of settlements attempted has gone up in absolute terms, the percentage of settlement proposals has crashed to 4.79% from 42.52% in the previous year.

Necessary Timelines:

32. Adopting a firm timeline for initiation of investigations, completion of investigations, initiation of proceedings, disposal of settlement, and disposal of proceedings, is a must. This must be embedded into the law. Needless to say, elements of such a timeline may be directory and other elements may be mandatory (as with any economic legislation) but the complete absence of timelines in this regard is a stark feature that needs correction.

33. It must also be remembered that the burden of making a *prima facie* case first lies on the prosecuting party and

there would have to be a time limit for continuing with proceedings on the premise that the absence of a finding of violation is only *prima facie* in nature. Indeed, initiating a prosecution, even of civil proceedings and bringing home a charge and defending it in appeal, is not a light matter and with capacity constraints, SEBI has done an admirable job so far. However, the very same principle makes it vital to have a clear policy on which battles to pick.

34. There is yet another reason why an enforcement policy is necessary. The regulatory objective of SEBI may be better served by timely and sharp action in a few large and complex cases as compared with frittering energy and resources in thousands of tiny cases. Indeed, every single case has a consequence but for a regulator to achieve its objective, it has to be strategic on how best it can prosecute cases of serious significance.

35. The Committee noted the practices of the Competition Commission of India ("**CCI**"), which has a segregation of its investigating arm from its quasi-judicial arm. The CCI passes an order containing a *prima facie* need to investigate and gives the Director General of Investigations ("**DG**") a period of 60 days to investigate. Indeed, investigations may not conclude in 60 days, but the DG has to provide a status report and seek an extension of time to investigate. By this process, the investigation and its status and progress is overseen.

Likewise, the legislation contains firm timelines for dealing with applications seeking approval of combinations and these are embedded into the law. It would be important for SEBI to study such practices and adopt such a framework into subordinate legislation governing SEBI's enforcement. Such self-discipline provisions do not need an amendment by Parliament, to the SEBI Act.

Surveillance and Market Administration Measures:

36. As regards surveillance actions and the improvements being contemplated to the surveillance mechanism, the Committee notes with appreciation, the regulatory reaction to events and learnings from the market. The Committee would suggest that the element of human discretion should be done away with as far as possible.

37. Even with introduction of stock-specific derivatives, the human element for making a choice on whether to provide such an avenue should be nearly absent. Unless there are extraordinary circumstances that would not have been factored by the algorithm by which a stock's qualification for inclusion in the derivatives segment is assessed, the inclusion of stock-specific derivatives must be automatic and machine-based.

38. On the matter of disclosures, the Committee has made its observations in Chapter Three. To perfect the ability of the market to read and study the data that is

generated by compliance with disclosure obligations, it should be ensured that all provision of data should be in machine readable format and is inter-operable across electronic platforms. Without such a framework, regulatory compliance would only lead to piling up of data in silos of databases that do not talk to one another, rendering the big picture incapable of being discerned. It is noteworthy that a strong feedback on the Hindenburg Report is that it contained no new data but was substantially a collection of inferences from data in the public domain.

Structural Reform:

39. There are some wider structural changes that are apt and which have already been recommended by working groups and committees in the past. This Committee does not intend to elaborate upon and repeat the merits of these. Such recommendations have already been well articulated with serious intellectual resources having been expended in recommending such changes. Some of these that need specific attention are:-

    a. The creation of a Financial Redress Agency that handles investor grievances across sectors. This could be a first step to an eventual unified regulator, but at the least, it is vital to implement a central redress agency that can focus on investor grievance redressal across sectors. Malpractices such as mis-selling and pushing of inappropriate

financial products can occur across sectors – say in stock broking, insurance and in banking. At the enterprise level, the service providers of these respective services could be one and the same; and at the consumer level, the investor at the receiving end of the mis-selling could be the same individual. However, grievance redressal is split across regulators working in silos.

b. Likewise, as seen in Chapter Three, the process for recovering unclaimed private property is spread across agencies such as IEPFA and DEAF. The same successor in title to the same deceased would have to engage with multiple agencies to recover the asset as a matter of right. This anomaly has to be addressed on a war footing. The Committee recommends that either through the aegis of the Financial Stability and Development Council or even by appropriate legislation, this problem must necessarily be addressed with a sense of urgency.

c. Equally, in complex enforcement matters, where the skill-set and expertise of multiple regulatory and enforcement agencies would have to be brought to bear, it would be vital to have a framework by which a multi-agency committee ("**Investigating Committee**") with a temporary shelf life (just what is required for investigating that particular case) may be set up by the

Government of India. At the end of the investigation, with the initiation of appropriate proceedings such a committee must be disbanded. The Committee does not see merit in creating yet another enforcement agency but sees merit in bringing to bear the capacities available to the Republic across agencies to investigate the complex case. The framework being suggested must stipulate criteria by which a case may be referred to such an Investigating Committee, by designating it as a "systemically important investigation". The Government must be able to resort to such a framework only when the case involved has serious cross-sectoral repercussions and would need multi-disciplinary skill sets to be brought to bear in a coordinated manner.

d. Within SEBI (as indeed any other regulator), the doctrine of separation of powers must be followed in letter and spirit. The quasi-judicial arm of the regulator has to be necessarily ring-fenced so that it is truly a check and balance on the executive arm of the regulator. If performance of the quasi-judicial officers is appraised by the executive arm, the very foundation of separation of powers would be nullified. The FSLRC recommendations in this regard must be implemented.

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THIS REPORT HAS BEEN SIGNED BY THE MEMBERS

THIS 6TH DAY OF MAY 2023

Justice Abhay Manohar Sapre (Retd.), Head of the Committee	**Justice J.P. Devadhar (Retd.)** Member
K.V. Kamath, Member	**O.P. Bhatt**, Member
Nandan Nilekani, Member	**Somasekhar Sundaresan**, Member

ANNEXURE A

RULE 19A OF SCRR

"[39][*Continuous Listing Requirement.*

19A. *(1)* ***Every listed company [40][other than public sector company] shall maintain public shareholding of at least twenty five per cent.:***

[41][42][Provided that every listed public sector company which has public shareholding below twenty-five per cent. on the commencement of the Securities Contracts (Regulation) (Second Amendment) Rules, 2018, shall increase its public shareholding to at least twenty-five per cent, within a period of [43][three years] from the date of such commencement, in the manner specified by the Securities and Exchange Board of India.]

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[39] Inserted by the Securities Contracts (Regulations) (Amendment) Rules, 2010, w.e.f. 04.06.2010

[40] Inserted by the Securities Contracts (Regulations) (Second Amendment) Rules, 2010, w.e.f. 09.08.2010.

[41] Substituted, ibid. Prior to substitution, provisos, read as under:

"Provided that any listed company which has public shareholding below twenty five per cent on the commencement of the Securities Contracts (Regulation) (Amendment) Rules, 2010, shall bring the public shareholding to the level of atleast twenty five per cent by increasing its public shareholding to the extent of at least five per cent per annum beginning from the date of such commencement, in the manner specified by the Securities and Exchange Board of India:

Provided further that the company may increase its public shareholding by less than five per cent in a year if such increase brings its public shareholding to the level of twenty five per cent in that year."

[42] Substituted vide Securities Contract (Regulation)(Second Amendment) Rules, 2018, w.e.f. 03.08.2018. Prior to substitution, proviso, read as under:

"Provided that any listed company which has public shareholding below twenty five per cent, on the commencement of the Securities Contracts (Regulation) (Amendment) Rules, 2014, shall increase its public shareholding to at least twenty five per cent, within a period of [49][four] years from the date of such commencement, in the manner specified by the Securities and Exchange Board of India"."

[43] Substituted for "two years" by the Securities Contracts (Regulation) (Second Amendment) Rules, 2020, w.e.f. 31.07.2020

Explanation: For the purposes of this sub-rule, a company whose securities has been listed pursuant to an offer and allotment made to public in terms of [44][***] clause (b) of sub-rule (2) of rule 19, shall maintain minimum twenty five per cent, public shareholding from the date on which the public shareholding in the company reaches the level of twenty five percent in terms of said sub-clause.]

(2) Where the public shareholding in a listed company falls below twenty five per cent. at any time, such company shall bring the public shareholding to twenty five per cent. within a maximum period of twelve months from the date of such fall in the manner specified by the Securities and Exchange Board of India.]

[45][Provided that every listed public sector company whose public shareholding falls below twenty five per-cent. at any time after the commencement of the Securities Contracts (Regulation) (Second Amendment) Rules, 2018, shall increase its public shareholding to at least twenty five per-cent, within a period of two years from such fall, in the manner specified by the Securities and Exchange Board of India.]

(3) [46][***]

[47][(4) Where the public shareholding in a listed company falls below twenty-five per cent. in consequence to the Securities Contracts (Regulation) (Amendment) Rules, 2015, such company shall increase its public shareholding to at least twenty-five per cent. in

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[44] Words "sub-clause (ii) of" omitted by the Securities Contracts (Regulation) Third Amendment Rules, 2014, w.e.f. 19-11-2014.

[45] Inserted vide Securities Contract (Regulation) (Second Amendment) Rules, 2018 w.e.f. 03.08.2018.

[46] Sub-rule (3) omitted by the Securities Contracts (Regulation) (Second Amendment) Rules, 2014, w.e.f. 22-8-2014. Prior to its omission, said sub-rule, as inserted by the Securities Contracts (Regulation) (Second Amendment) Rules, 2010, w.e.f. 9-8-2010, read as under :

"(3) Notwithstanding anything contained in this rule, every listed public sector company shall maintain public shareholding of at least ten per cent :"

[47] Inserted by the Securities Contracts (Regulation) (Amendment) Rules, 2015, w.e.f. 25.02.2015.

the manner specified by the Securities and Exchange Board of India within a period of three years, as the case may be, from the date of notification of:

(a) the Depository Receipts Scheme, 2014 in cases where the public shareholding falls below twenty five per cent. as a result of such scheme;

(b) the Securities and Exchange Board of India (Share Based Employee Benefits) Regulations, 2014 in cases where the public shareholding falls below twenty-five per cent., as a result of such regulations.]

[48][(5) Where the public shareholding in a listed company falls below twenty-five per cent, as a result of implementation of the resolution plan approved under section 31 of the Insolvency and Bankruptcy Code, 2016 (31 of 2016), such company shall bring the public shareholding to twenty-five per cent within a maximum period of three years from the date of such fall, in the manner specified by the Securities and Exchange Board of India:

Provided that, if the public shareholding falls below ten per cent, the same shall be increased to at least ten per cent, within a maximum period of [49][twelve] months from the date of such fall, in the manner specified by the Securities and Exchange Board of India.]

[50][Provided further that, every listed company shall maintain public shareholding of at least five per cent as a result of implementation of the resolution plan approved under section 31 of the Insolvency and Bankruptcy Code, 2016.]

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[48] Inserted by the Securities Contract (Regulation) (Amendment) Rules, 2018, w.e.f. 24.27.2018.
[49] Substituted for "eighteen" by the Securities Contracts (Regulation) (Amendment) Rules, 2021, w.e.f. 18.06.2021.
[50] Inserted by the Securities Contracts (Regulation) (Amendment) Rules, 2021, w.e.f. 18.06.2021.

[51][52][(6) Notwithstanding anything contained in sub-rules (1) to (5), the Central Government may, in public interest, exempt any listed entity in which the Central Government or State Government or public sector company, either individually or in any combination with other, hold directly or indirectly, majority of the shares or voting rights or control of such listed entity, from any or all of the provisions of this rule.

***Explanation**. -- For the purposes of this rule, the exemption shall continue to be valid for the period specified therein, irrespective of any change in control of such listed entity subsequent to issuance of such exemption.]]"*

[51] Inserted by the Securities Contracts (Regulation) (Second Amendment) Rules, 2021, w.e.f. 30.07.2021.

[52] Substituted by the Securities Contracts (Regulation) Amendment Rules, 2022, w.e.f. 02.01.2023. Prior to substitution, sub-rule (6) read as follows:

"(6) Notwithstanding anything contained in sub-rules (1) to (5), the Central Government may, in the public interest, exempt any listed public sector company from any or all of the provisions of this rule."

ANNEXURE B

PROVISIONS FROM LODR REGULATIONS

ON RELATED PARTY TRANSACTIONS

(zb) "related party" means a related party as defined under sub-section (76) of section 2 of the Companies Act, 2013 or under the applicable accounting standards

[17][Provided that:

(a) *any person or entity forming a part of the promoter or promoter group of the listed entity; or*

(b) *any person or any entity, holding equity shares:*

(i) *of twenty per cent or more; or*

(ii) *of ten per cent or more, with effect from April 1, 2023;*

in the listed entity either directly or on a beneficial interest basis as provided under section 89 of the Companies Act, 2013, at any time, during the immediate preceding financial year;

shall be deemed to be a related party:]

Provided [18][further] that this definition shall not be applicable for the units issued by mutual funds which are listed on a recognised stock exchange(s);

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[17]Substituted by the SEBI (Listing Obligations and Disclosure Requirements) (Sixth Amendment) Regulations, 2021, w.e.f. 1.4.2022. Prior to the substitution, the provision was inserted by the SEBI (Listing Obligations and Disclosure Requirements) (Amendment) Regulations, 2018, w.e.f. 1.4.2019 and read as under:
"Provided that any person or entity belonging to the promoter or promoter group of the listed entity and holding 20% or more of shareholding in the listed entity shall be deemed to be a related party."

[18] Inserted by the SEBI (Listing Obligations and Disclosure Requirements) (Amendment) Regulations, 2018, w.e.f. 1.4.2019.

(zc) [19][“related party transaction” means a transaction involving a transfer of resources, services or obligations between:

(i) *a listed entity or any of its subsidiaries on one hand and a related party of the listed entity or any of its subsidiaries on the other hand; or*

(ii) *a listed entity or any of its subsidiaries on one hand, and any other person or entity on the other hand, the purpose and effect of which is to benefit a related party of the listed entity or any of its subsidiaries, with effect from April 1, 2023;*

regardless of whether a price is charged and a “transaction” with a related party shall be construed to include a single transaction or a group of transactions in a contract:

Provided that the following shall not be a related party transaction:

(a) *the issue of specified securities on a preferential basis, subject to compliance of the requirements under the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018;*

(b) *the following corporate actions by the listed entity which are uniformly applicable/offered to all shareholders in proportion to their shareholding:*

i. *payment of dividend;*

ii. *subdivision or consolidation of securities;*

iii. *issuance of securities by way of a rights issue or a bonus issue; and*

iv. *buy-back of securities.*

(c) *acceptance of fixed deposits by banks/Non-Banking Finance Companies at the terms uniformly applicable/offered to all shareholders/public, subject to disclosure of the same along with the disclosure of related party transactions every six months to the stock exchange(s), in the format as specified by the Board:*

Provided further that this definition shall not be applicable for the units issued by mutual funds which are listed on a recognised stock exchange(s);]

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