

THE MYTH OF SELF-REGULATION OR THE DANGERS OF SECURITIES REGULATION WITHOUT ADMINISTRATION: THE INDIAN EXPERIENCE

ROBERT C. ROSEN *

I. Introduction

1.1. Objectives

This article discusses regulation of the securities industry in India. It culminates a year's study which utilized the resources of the Securities and Exchange Commission (SEC), the Library of Congress and the World Bank [1]. It also involved a six-week stay in India visiting the four largest stock exchanges and personal interviews with over seventy individuals whose vocations cover almost every aspect of the securities industry [2]. Motion pictures were taken and studied of trading on the floors of the Bombay, Calcutta and Madras exchanges. The intention here is not to write a monograph merely describing regulations affecting certain securities-related topics. An attempt is made to identify, describe, discuss and analyze those regulations which affect securities regulation in the narrower sense; that is, with a view towards enforcement. The enforcement programs (or lack thereof) and their effectiveness are also analyzed and certain recommendations made [3]. The author realizes that developing countries in particular must establish a regulatory framework based at least in part upon economic considerations. The paper will not explore such considerations, and to the extent possible they are generally divorced from the discussion herein.

1.2. An overview

In their desire to increase per capita standards of living, developing countries have sought and used various means to hasten economic development. Not all of these have proven successful, however. State and external financing is inefficient and in the long run leads to economic instability. The failures of communism, socialism, and totalitarianism and various combinations of these are well documented. Thus far, the development of a free enterprise system with a strong private sector at its foundation appears to be the most successful means.

The ability to channel savings into long-term equity financing is central to main-

* Mr. Rosen is an Attorney in the Washington Regional Office of the Securities and Exchange Commission and a member of the District of Columbia Bar.

tenance of a free enterprise system. Stock markets and stock exchanges are the mechanisms for such financing. The effectiveness of these mechanisms depends upon the degree to which certain conditions exist: a stable political environment; reasonable and successful fiscal and monetary policies; reliable accounting and financial reporting standards and procedures, and concomitant reliable and timely economic and financial information; a system to allocate savings to entrepreneurs through short- and long-term financial instruments that meet the risk/reward requirements of savers and borrowers; a secondary market for such instruments; and a legislative and regulatory infrastructure that includes the means to administer it through regulatory agencies [4]. The last of these conditions is a major factor in determining the amount of confidence that investors will have in the market system, and therefore it is a major factor in determining the extent to which investors will channel their savings into long-term equity financing. Investor confidence is thus the key to smooth and successful operation of the market system.

Like most countries that have market systems, India has suffered stock market crashes and resultant loss of investor confidence in the system. Usually, it has responded to such crises by appointing a committee to examine the problem and make recommendations; often it has followed such recommendations by enacting corrective legislation. It also has copied, with variations, many of the United Kingdom's laws. For instance, the Indian Companies Act of 1956 was modeled after the United Kingdom's Companies Act of 1948.

Differences are evident, however, in the mode of regulation that India adopted. Unlike the United Kingdom, India does not rely on self-policing by the securities industry; instead, it has laws that, on their face, strictly regulate the issuance and trading of securities and the recognition and operation of stock exchanges. Unfortunately, these laws are ineffectively administered. Consequently, they are worse than useless; they are dangerous because investors unjustifiably rely on them. India's practice of merely monitoring self-regulation has created only an appearance of government control. It has been ineffective in controlling manipulative and insider trading practices, and although the government has powers of oversight and direct intervention, it rarely, if ever, exercises them.

1.3. The Indian market in perspective

India has a long history of stock market activity. The first stock exchange, the Bombay Stock Exchange, was established over 100 years ago. The Bombay Stock Exchange is India's largest and most prominent, with 821 listed companies and 450 members or brokers. Calcutta is next in size with 772 listed companies and 650 members. In total, India has approximately 50,000 companies, of which 8,186 are classified as public [5]. No figures exist on the volume of securities traded. The estimated three million Indian shareholders roughly equal the number of shareholders of American Telephone and Telegraph. Less than one-half of one percent of India's population own securities as compared to over 12 percent of the population

of the United States and over 5 percent of the population of the United Kingdom [6]. Indians have a strong propensity to save. Savings have traditionally taken the form of hoarding jewelry and precious metals, and more recently, the form of short-term bank and post office deposits [7]. Efforts have been made to channel savings into the securities market, most notably with the creation of India's only mutual fund in 1963, the Unit Trust of India [8]. Units are sold by the post offices, salesmen and banks in Rs. 10 denominations [9]. The 770,000 investors holding Rs. 2,554 billion of equity in the Unit Trust annually receive a 9 percent return on their investments [10].

2. Development of financial and securities transactions in India from the joint Hindu family system to the present-day stock exchanges

2.1. *The joint Hindu family and managing agency system*

The concept of limited liability by which modern corporations obtain capital and individuals put their money to work without personal risk is not new to India. Thousands of years before England developed its corporate system, commerce in India was being conducted by Hindu families, the members of which enjoyed limited liability. Under the Hindu joint family system the family was considered distinct from its members and could engage in all aspects of business. Hindu law recognized that only the head of the family remained personally liable; the other members shared in the profits of the enterprise without exposing their personal property to possibility of loss [11].

The introduction of the modern corporate system in India began in 1600 when the East India Company was granted, through a Royal Charter, a monopoly to engage in trade with India. Soon afterwards, other English companies, known as sterling companies because they were capitalized in pounds sterling, began trading in India. These companies were managed in India by Europeans who, because of the great distance and communication problems, were granted almost all the powers of their respective boards sitting in England. By the middle of the nineteenth century, a managing agency system, unique to India, had developed [12].

The managing agency generally consisted of several partners who ran the day-to-day affairs of several large companies [13]. Many such partnerships converted into private and even public companies. Managing agents were responsible for starting industrial units because, based upon their past record of achievement, it was relatively easy for them to obtain capital from investors and banks. Often, agents stood personally liable for loans made by banks to their managed companies [14]. Managing agents developed a system of administrative integration, the forerunner of modern corporate conglomerates. By coordinating the operations of several companies, managing agents were able to achieve lower administrative costs, economies of scale and purchase, and a ready market for one company's products with another [15].

Although the managing agency system aided in India's economic development, inherent in the system was the possibility for great abuses. The agencies passed into hands of relatives who did not necessarily possess the business acumen or initiative of their pioneer predecessors. Agents soon learned to take advantage of their position by commingling the capital of companies under their control, using these funds to aid weaker entities at the expense of unaffiliated stronger companies [16]. Managing agents also used their ability to appoint directors to gain control of a company's board of directors to the detriment of its public shareholders [17].

Abuses in the managing agency system led to statutory restrictions and later to its abolition [18]. The Companies Act of 1913 made no reference to managing agents. However, a 1936 amendment limited the duration of a managing agency to twenty years, allowed the agent to be removed for fraud, insolvency or breach of trust and permitted it to appoint no more than one-third of a company's board of directors [19]. The Companies Act of 1956 placed a limit of ten companies, public or private, which could be managed at one time by a managing agent [20]. Finally, a 1969 amendment decreed that as of April 1, 1970, all existing appointments of managing agents were considered to be expired and no further such appointments were to be made [21].

2.2. The stock markets

2.2.1. Formation

Before 1800, Indian securities transactions were primarily limited to loan instruments of the East India Company. By 1830 bank securities were being traded in Bombay, and shares of cotton presses were being traded in Calcutta. The Companies Act of 1850 formally recognized the concept of limited liability and gave birth to the modern corporation or joint stock company. The advent of the American Civil War in 1861 caused England to look to India for its cotton needs, and between 1861 and 1865, cotton exports to England, mostly from Bombay, doubled. This, coupled with a ten-fold price increase in cotton, caused Rs. 520,000,000 of gold and silver to pour into India. These funds were used to capitalize scores of new ventures which sold their shares to the public. Banks loaned money to purchase shares, and everyone, from menial servants upwards, engaged in speculation. What is referred to as the Share Mania of 1860–65 came to a grinding halt on Black Friday, July 1, 1865, when the end of the Civil War caused the price of cotton to plummet. This precipitated the liquidation of hundreds of companies and widespread disillusionment among the public. Despite this, it is believed that the positive results of the Share Mania were the great expansion of liquid capital and the establishment of a regular market in securities [22]. The number of brokers [23] in Bombay increased from 6 in 1850, to 60 in 1860, to 300 in 1875 [24].

In 1875, 300 brokers formed a Brokers Association. Two years later the Native Stock and Share Brokers' Association, the precursor of the Bombay Stock Exchange, was founded:

to support and protect the character and status of brokers and to further the interests of both brokers and public dealing in Bombay in stocks, shares and like securities and in exchange, to promote honorable practices, to discourage and suppress malpractices [25].

Securities activities in Calcutta somewhat paralleled those in Bombay. At the end of the eighteenth century, several brokers were transacting business, primarily in government issues. In 1864, daily newspapers were reporting stock quotations of ninety-one joint stock companies, the majority being tea, jute and coal concerns. In 1908, the Calcutta Stock Exchange Association was founded by 150 members. In 1923 the Association became incorporated with a membership of 210 firms and 442 individuals [26].

After the Bombay Native Stock and Share Brokers' Association was formed in 1877, Ahmedabad, a city just north of Bombay, developed a large textile industry with capital supplied by floating joint stock companies. A secondary market developed, and in 1894 the Ahmedabad Share and Stock Brokers Association was formed [27]. The first stock exchange in South India was created in Madras in 1920, but went out of business three years later. Even without an exchange, Madras brokers in the 1920s traded scrips in local textile mills. In 1933, Madras was linked to Bombay and Calcutta by telephone. This greatly increased the interest of investors in the north and the south in each others' issues. The Madras Stock Exchange was established in 1937 with five members and thirty-seven listed companies [28].

The increased economic activity due to the Second World War brought unprecedented prosperity to the stock exchanges. Associations of brokers sprang up in most of India's large cities. Stock exchanges were established in Lahore (now part of Pakistan) in 1934, Cawnpore, U.P. in 1940, Hyderabad in 1943, Delhi in 1947, and Bangalore in 1957. There are presently eight stock exchanges recognized under the Securities Contracts (Regulation) Act, 1956 [29].

The beginning of the First World War brought activity and wealth to members of the Bombay and Calcutta Exchanges. The value of a card or seat on the Native Stock and Share Brokers' Association exchange went from Rs. 2,900 in 1914 to Rs. 48,000 in 1921. During this period there were no established trading rules. The public was not prohibited from entering the trading floor, where clients often transacted business among themselves. Beggars, hawkers and pickpockets created an overcrowded and chaotic atmosphere. In 1918-19 several brokers were successful in manipulating the price of two highly traded stocks, Standard Mill and Madhavji Mill. The resultant crash caused forward trading to be halted. Fourteen brokers defaulted, forcing the exchanges to sell off their cards [30]. The public criticism that followed the manipulative practices and the market slump of the early 1920s moved the Bombay Legislative Council to create a committee to look into the activities of the Bombay Exchange. Sir Wilfred Atlay, previous Chairman of the London Stock Exchange, was chosen to head the Committee. In its report the Committee stated:

The most sinister manifestation of speculation in Bombay is the frequent occurrence of corners

in the market, and the policy and practice of the Association with regard to corners appears to us to constitute the head and front of their offending [31].

While the government of Bombay was considering what, if any, action to take based on the Atlay Committee report, the exchange experienced another crash in 1925. Later that year the Securities Contracts Control Act of 1925 was passed which voided all trades unless made in accordance with rules approved by the Bombay government. The exchange submitted a complete set of rules and regulations which gave itself the power to intervene in cases of manipulation and cornering the market. Although these rules were sanctioned by the government in 1927, they were never effectively implemented [32].

Between 1927 and 1937 five serious crises were experienced on the Bombay exchange. In 1933 the failure of one of India's largest public managing agencies, Currimbhoy Ebrahim and Sons Ltd., resulted in the bankruptcy of many textile companies under its management. The exchange responded by suspending forward trading for seven weeks. Forward trading was again suspended in 1936 after the exchange was unwilling or unable to prevent the manipulation of several markets by professional jobbers (specialists) [33]. Once again an inquiry committee was appointed, this time under the chairmanship of W.B. Morrison, a leading London broker. Although many of the committee's recommendations were adopted by the exchange, legislation which would have permitted the government to take over and prevent manipulative and other abuses in situations where the exchange would not act did not materialize [34].

The Second World War, which witnessed an increase in the number of stock exchanges and trading activities, also witnessed a concomitant increase in illegal conduct by brokers. Restrictions preventing forward and options trading forced brokers to leave the exchange for the adjacent streets. It is estimated, for example, that nine out of ten trades in Calcutta in 1945 took place in the "Katai" market, just outside the Calcutta Stock Exchange [35]. Another committee was formed, this time by the Central Government. It was headed by A.D. Gorwala, whose report, submitted in 1951, led to the passage of the Securities Contracts (Regulation) Act of 1956. Although (as will be discussed below) this act gives the Central Government complete control over the recognition and administration of exchanges, it has been unsuccessful in halting the history of manipulative abuses and in restoring investor confidence to the market place.

3. The regulatory framework

Three legislative enactments primarily deal with the regulation of securities in India. The Companies Act of 1956 regulates the incorporation of companies and their periodic financial and other reporting requirements. The Capital Issues (Control) Act of 1947 strictly controls the issuance of securities. The Securities Con-

tracts (Regulation) Act of 1956 regulates the stock exchanges and the trading of securities. To a lesser extent, other laws also affect the regulation of securities: the Foreign Exchange Regulation Act of 1973; the Banking Regulation Act of 1949; the Unit Trust of India Act of 1963; Indian Trusts Act of 1882; Reserve Bank of India Act of 1934; the Income Tax Act of 1961; the Estate Duty Act of 1953; Wealth Tax Act of 1957; Gift Tax Act of 1958; Public Debt Act of 1942; and the Indian Stamp Act of 1899.

3.1. The Companies Act and the Companies Law Board

The Companies Act became effective April 1, 1956, and since then has been amended fourteen times. It presently consists of 658 sections dealing with matters generally found in the federal and state securities laws and the state corporate codes of the United States. The basic objectives of the Companies Act were to:

provide a minimum standard of good behaviour and business honesty in company promotion and management; due recognition of the legitimate interest of shareholders and creditors and of the duty of management not to prejudice or jeopardize those interests; provision for greater and effective control over and voice in the management for shareholders; a fair and true disclosure of the affairs of companies in their annual published balance sheet and profit and loss accounts; a higher standard of accounting and auditing; recognition of the rights of shareholders to receive reasonable information and facilities for exercising an intelligent judgement with reference to the management; a ceiling on the share of profits payable to the management as remuneration for services rendered; a check on their transactions where there was a possibility of conflict of duty and interest; a provision for investigation into the affairs of any company managed in a manner oppressive to a minority of the shareholders or prejudicial to the interests of the company as a whole; enforcement of the performance of their duties by those engaged in the management of public companies or of private companies which were subsidiaries of public companies by providing sanctions in the case of breach and subjecting the latter also to the more restrictive provisions of law applicable to public companies [36].

Two amendments to the Companies Act are noteworthy. The first created the Companies Law Board ("Board") in 1963, vesting it with certain powers of the Central Government and of the Courts. In 1974 a further amendment substantially strengthened those powers. Through its benches, the Board receives, examines, and processes various applications and petitions. It also orders investigations and through the regional directors and registrars of companies pursues matters civilly in the courts and/or refers matters criminally to the police or the Central Bureau of Investigations.

3.1.1. Classifications of companies

All corporations whether public or private must be registered under the Companies Act and must file audited financial statements with the appropriate registrar [37]. The Companies Act classifies companies in three ways: liability structure, government/nongovernment, and foreign/domestic. With respect to liability, the

three types of companies recognized under the Companies Act are companies limited by shares, companies limited by guarantee, and unlimited companies. In companies limited by shares, the shareholders' liability is limited to the amount which is left unpaid to purchase such shares. Clearly the most prevalent type of company, this classification includes 48,434 nongovernment companies limited by shares, of which 40,548 are private and 7,886 are public [38]. Where shareholders have agreed to contribute certain amounts to the assets of the company, the company is registered as a guarantee company or an association not for profit [39]. As of March 31, 1978, there were 1,381 such companies registered [40]. Unlimited liability companies with no personal liability limits on shareholders are generally private investment companies [41]. Of the forty-seven such companies registered on March 31, 1978, thirty-two were from Goa, a former Portuguese colony taken over by India in 1961 [42].

Government companies, as defined in Section 617 of the Companies Act, can be public or private as well as limited in liability by stock or otherwise. As of March 31, 1978, there were 745 government companies registered of which 300 were public limited companies and 445 were private limited companies [43].

Because of the new ownership requirements under the Foreign Exchange Regulation Act, India has recently been experiencing the sale of tremendous amounts of stock to Indian nationals by foreign companies. With certain exceptions, foreign-owned companies have been forced to divest their equity to 40 percent or leave India altogether. Coca Cola and IBM are two multinational corporations that have chosen the latter course. As of March 31, 1978, there were 473 foreign corporations doing business in India [44]. During 1977-78 four foreign corporations established a place of business in India, and three closed down their operations [45].

Under the Companies Act, private companies are less restricted than public companies. Two incorporators must sign the memorandum of association instead of the seven required for a public company [46]. Two rather than three directors are the minimum permitted [47], and these directors can be elected or appointed without the disclosure and scrutiny required for public company directors [48]. A private company does not have to file a registration statement when allotting its shares [49]. Of most topical importance is the absence of controls on managing and full-time directors of private companies, particularly with respect to remuneration [50]. A recent survey revealed that the average total remuneration, inclusive of salary, commission and perquisites, for the top executive of a private company is Rs. 223,000 per year as compared to only Rs 83,740 per year for his public company counterpart [51].

A private company may become a "deemed" public company if its annual sales volume exceeds Rs. 10,000,000 or if it owns 25 percent of, or is owned 25 percent by, a public company [52]. The legislative intent was to confine the activities of private companies to running small businesses. The Sachar Committee recommends that further restrictions be placed on private companies, particularly in the area of

raising capital. Under the proposal, private companies would be prohibited from borrowing money or accepting public deposits and from borrowing long-term loans in excess of Rs. 10,000 for more than three years from public financial institutions [53].

3.1.2. Prospectus

Before shares can be publicly offered, a prospectus must be filed with the Registrar of Companies and furnished to prospective investors. The information required in the prospectus is quite detailed and includes a history of the company, considerable biographical data on the directors, and financial statements [54].

3.1.3. Shareholder protection

An individual shareholder's statutory rights as enumerated in the Companies Act include the following: the right to apply to the Central Government for the calling of an annual shareholders' meeting if the company refuses to call such a meeting [55]; to insist that a shareholders' meeting not be held unless at least twenty-one days written notice has been given [56]; to petition for a compulsory winding up of the company [57]; to make representations to the courts where the company seeks the sanction of the courts to a scheme of transfer of shares [58], and to object to compulsory transfer of his shares [59]. Shareholders' rights may also be exercised when the minimum required number of shareholders band together. These rights include the right to apply for an investigation of the affairs of the company [60] and to apply to the courts for relief of oppression and mismanagement [61].

The Sachar Committee has recommended that the Companies Act be amended to allow the statutory recognition of regional shareholders associations [62]. These associations would be recognized under the same criteria utilized for the stock exchanges. They would be entitled to purchase one or more shares in every public company listed on the various stock exchanges and would have the right to make application to the courts and Central Government in order to protect shareholders [63].

3.1.4. Books, records and auditors

The Companies Act prescribes how financial and other information will be disclosed [64]. Presently, companies are permitted to maintain their books on a cash basis [65]. However, the Sachar Committee recommends that all companies be required to use the mercantile or accrual basis [66]. The Sachar Committee also recommends the adoption of a provision similar to Section 16 of the United Kingdom's Companies Act of 1967 concerning the resignation of auditors. Upon resignation, based on management impropriety or other reasons, the auditor would be entitled to call upon the directors of a company to hold an extraordinary meeting of the shareholders and to request the company to circulate a written statement from the auditors to its shareholders [67].

Since 1975 the Central Government has required that a company's auditors must

make positive statements in the annual report with respect to fifteen items. These items include, *inter alia*, that the company has maintained proper records to show full particulars, that none of the fixed assets have been revalued during the year, that there are adequate internal control procedures, and that the company has complied with certain provisions regarding deposits accepted from the public [68].

3.1.5. *Trading on inside information*

Trading on information that is not disclosed to the public appears to be quite prevalent and may very well be one of the leading factors causing a lack of general investor confidence. Under the Companies Act, every company is required to keep a register showing, with respect to each director, information concerning his holding stock or debentures of the company [69]. Also, each director is required to give notice of all stock and debenture transactions in order that the company can keep such a ledger [70]. The Sachar Committee has recommended that each director, statutory auditor, cost auditor, financial accountant, financial controller, cost accountant, tax and management consultant or adviser and full-time legal adviser or solicitor, or any spouse or dependent children of the aforementioned persons be required to notify the board of directors fifteen days prior to any company stock or debenture transaction. If the board does not object within fifteen days, then the transaction may be consummated [71]. The committee further recommends a complete prohibition on trading by these insiders for a two-month period before and after the close of the accounting year [72]. The Sachar Committee's recommendation includes a provision that would impose civil liability against the insider in favor of a party who was taken advantage of due to the misuse of confidential information. In addition, the insider would be held accountable to the company for his "unjustly made" profits [73].

3.1.6. *The Company Law Board*

The Board is a quasijudicial body within the Department of Law, Justice and Company Affairs, part of the Ministry of Law, Justice and Company Affairs. The Department of Law, Justice and Company Affairs administers the Companies Act of 1956, the Monopolies and Restrictive Trade Practices Act of 1969 ("MRTP Act"), the Chartered Accountants Act of 1949, and the Cost and Work Accountants Act of 1959. It also exercises supervisory control over the Institute of Company Secretaries formed under the Companies Act [74]. The Board discharges those powers and functions conferred on the Central Government under the Companies Act or under other laws as may be delegated to it by the Central Government [75]. The Central Government is empowered to delegate any of its powers to the Board [76]. In 1972 the Central Government delegated, with certain exceptions, all of its powers and functions under the Companies Act to the Board [77]. Under a 1974 Amendment to the Companies Act, the Board was statutorily vested with certain additional powers that previously had been reserved for the High Courts [78]. With the approval of the Central Government the Board has passed the Com-

pany Law Board Procedural Rules of 1974 and the Company Law Bench Rules of 1975.

The present Board consists of a chairman and six members. The chairman is the secretary of the Department of Law, Justice and Company Affairs, and four of the six members are joint secretaries in the same department. A bench which consists of two or more members hears and decides those matters which come before it. The Board benches generally meet in the various offices of the Registrar of Companies. For the fiscal year ending March 31, 1978, the Board, through its benches, met thirty times [79].

A matter generally comes before the Board in the form of an application/petition. The most prevalent matter heard by the Board for the fiscal year ending March 31, 1978, concerned companies appointing and/or continuing the appointment of a sole selling or buying agent [80]. The Companies Act requires the approval of the Board where a company with paid-up capital greater than Rs. 5,000,000 intends to appoint a sole selling or buying agent or where a smaller company intends to appoint a sole selling agent who directly and through his relatives holds either Rs. 5,000 or 5 percent of the paid-up capital [81]. The Board heard 137 such cases [82]. Loans by a company to its directors or their relatives are not permitted without Board approval [83]. Of the forty-three such applications made, only fifteen were approved [84]. A similar provision in the Companies Act obligates a company with paid-up share capital of Rs. 10,000,000 or more to seek prior approval of the Board where it intends to enter into a contract with a director, his relative or business associate involving the purchase or supply of any goods, materials or services or for underwriting the subscriptions of any shares in, or debenture of the company [85]. Of the 139 such applications considered for fiscal year ending March 31, 1978, seventy-two were approved, one rejected, three withdrawn and sixty-three left pending at the end of the year [86]. Other matters considered by the Board include the acquisition by an individual or group of persons owning 25 percent of the equity shares of a company registered under MRTTP Act [87]; declaration and payment of dividends when the company does not make a profit [88]; and use of a form other than Schedule IV to report annual financials [89].

3.2. The Capital Issues (Control) Act and the Comptroller of Capital Issues

As its name implies, the Capital Issues (Control) Act of 1947 ("Capital Issues Act") controls the raising of capital and issuance of securities [90]. Its jurisdiction extends to any company, foreign or domestic, which issues capital in India; offers its securities to the public in India; or renews or postpones the date of maturity or repayment of any security maturing for payment in India [91]. Jurisdiction is also extended to the issuance of capital outside India by a domestic company [92]. The purpose of the Act is wholly economic, *i.e.* to ensure that corporate investments are compatible with India's Five-Year Plans; to prevent investments in unproductive

areas; to further the growth of sound companies; and to space the timing of public offerings [93].

The Comptroller of Capital Issues within the Ministry of Finance administers the Capital Issues Act. With exceptions, no securities are to be issued or offered for public sale without the "consent" of the Comptroller of Capital Issues. The exceptions are to be found in the Capital Issues (Exemption) Order of 1969, last amended on April 1, 1976 ("Exemption Order"). Only "acknowledgment" by the Comptroller of Capital Issues is required when public companies or private companies registered under the MRTP Act are involved, *inter alia*, in the following types of transactions: the issuance of securities when the value of the consideration involved, together with the value of any previous issue of securities within twelve months, does not exceed Rs. 5,000,000 [94]; the issuance of securities in stock splits or consolidations when the paid-up capital does not change [95]; the issuance and acceptance of securities, other than debentures, in the ordinary course of business to a banking institution for loans, overdrafts or guarantees [96]; and third party guarantees with respect to the above [97].

The Exemption Order also provides that only the "acknowledgement" of the Comptroller of Capital Issues is required when a public company (not registered under the MRTP Act) issues securities (less than Rs. 5,000,000 of debentures) and where certain conditions are fulfilled including, *inter alia*: as a result of the proposed issue, the equity of the company will not be less than half its debt; the total paid-up preference share capital will not be more than one-third of the total paid-up equity share capital; if the securities are issued to acquire a business or asset, they are to be acquired at book value; when a public company is formed to acquire a proprietorship, partnership or association of persons, the acquisition is at book value; no securities are issued as consideration for revalued, intangible or fictitious assets; only par value is to be paid for such securities; all securities are to be fully paid for within five years; if it is the first public offering, the value of equity capital subscribed to previously by promoters, directors and their friends shall not be less than 15 percent if the total does not exceed Rs. 10,000,000, 12.5 percent if the total does not exceed Rs. 20,000,000, and 10 percent if the total is in excess of this amount; if the shares are offered publicly, then no reservation can be made in favor of any person or class without the approval of the Comptroller of Capital Issues; and the timing of the proposed issuance is in conformity with Central Government guidelines [98].

With exceptions, certain categories of companies do not require the consent or acknowledgement of the Comptroller of Capital Issues regardless of the amount of consideration involved, namely: private companies (not registered under the MRTP Act); government companies not issuing securities to the public; banking and insurance companies; and incorporated provident societies [99].

Issuers seeking acknowledgement from the Comptroller of Capital Issues file a "Statement of Capital Issue Proposal" [100]. Within approximately two weeks the issuer receives a letter stating that the Comptroller of Capital Issues acknowledges

receipt of the proposal [101]. Issuers seeking a consent from the Comptroller of Capital Issues file an "Application Form for Issue of Securities (Other than Bonus Shares)". Although not as detailed as the requirements of a full registration under Section 5 of the U.S. Securities Act of 1933, the "Application" is quite extensive and requires the enclosure of copies of such items as licenses, foreign collaboration agreements and memorandum and articles of association [102]. If the application is complete in all respects, the issuer receives a letter of consent from the Comptroller of Capital Issues within six weeks [103].

The Central Government is empowered to modify in the public interest proposals made under the Exemption Order [104] and to qualify any consent with such conditions as it deems appropriate [105]. The conditions imposed generally concern the timing of the issue, the period of validity of the acknowledgement or consent, and the submission of periodic statistical reports [106]. Failure to comply with the conditions or any section of the Capital Issues Act is punishable by a fine and/or a maximum of one year in jail [107].

Acknowledgements and consents are valid for a period of one year unless otherwise qualified [108]. For the year in which the capital issue is fully subscribed, the issuer is required to file with the Comptroller of Capital Issues an audited balance sheet and profit and loss statement. Unless otherwise qualified, no further reports are required [109]. As previously discussed, companies have a continuing obligation to file audited financial statements with the registrar of companies.

An analysis of how companies finance their projects shows that raising capital through the sale of equity shares amounts to only 26.1 percent of the total costs [110]. The largest percentage, 61.7 percent, of the total project costs were supplied by public financial institutions and banks. Companies' reserve surpluses accounted for 10.1 percent, while debentures accounted for only 0.7 percent of total project costs [111].

The total amount raised by nonfinancial and nongovernment companies through the sale of equity shares amounted to Rs. 717.1 million, which was up significantly from Rs. 343 million raised the previous fiscal year. The Rs. 717.1 million were raised by forty new public companies, fourteen existing public companies, and twenty-six private companies entering the capital market for the first time [112]. Rs. 529 million or 92.6 percent were underwritten; 83.2 percent of the total was offered to the public, and the balance was earmarked for promoters, directors, friends, existing shareholders, employees of the company, financial institutions, banks and state governments [113]. Of the total offered, 53.9 percent was subscribed to by the public and 43.7 percent was taken by underwriters—9.8 percent in their capacity as investors, 33.9 percent as part of their underwriting obligations—and 2.4 percent was left unsubscribed [114]. A further breakdown of the amount underwritten (Rs. 529 million) shows that 45.6 percent was underwritten by public financial institutions including the Industrial Development Bank of India and the Industrial Credit and Investment Corporation of India, 19.9 percent by banks, 11.9 percent by the General Insurance Corporation of India, 2.9 percent by state

financial and industrial development corporations, and only 18.0 percent by brokers [115]. From the above analysis, it can be seen that public financial institutions as direct lenders and participating underwriters play a much larger role than brokers in the acquisition of capital for India's corporations.

3.3. *The Securities Contracts (Regulation) Act and the stock exchanges*

In 1950 the new Constitution of India made stock exchanges and futures markets the exclusive jurisdiction of the Central Government [116]. Subsequently, the Securities Contracts (Regulation) Act of 1956 ("Securities Regulation Act") and the Securities Contracts (Regulation) Rules of 1957 ("Securities Regulation Rules") became law. The preamble to the Securities Regulation Act states that it is "an act to prevent undesirable transactions in securities by regulating the business of dealing therein, by prohibiting options and by providing for certain other matters connected therewith". This Act provides for the direct and indirect control of virtually all aspects of securities trading and the running of the stock exchanges. The Act makes every transaction in securities in any notified state or area illegal and punishable by fine and/or imprisonment if it is not entered into between or with members of a recognized stock exchange in that state or area [117]. It also makes every such securities contract void [118].

The Act prohibits the existence of other than recognized stock exchanges [119] and provides the mechanism for recognizing stock exchanges [120]. Applications to the Central Government for recognition must include a copy of the rules relating in general to the constitution of the stock exchange and in particular to, among other things: the admission into the stock exchange of various classes of members; the exclusion, suspension, expulsion and re-admission of members; and the procedure for registration of partnerships as members [121]. In determining whether to grant recognition, the Central Government may make whatever inquiry is necessary and impose in the rules and by-laws of the stock exchanges whatever conditions are required to ensure "fair dealing" and to "protect investors" [122]. These conditions concern, *inter alia*: the qualifications for members; the manner in which contracts are to be entered into and enforced; the representation of not more than three Central Government nominees on the board of the stock exchange; and the maintenance of books and records by members and their audit by chartered accountants [123]. The Central Government has the power to impose further conditions, other than in the rules and by-laws, such as limiting the number of members [124]. Finally, the Central Government has the power unilaterally to withdraw recognition.

Presently, of the eight stock exchanges recognized under the Securities Regulation Act, only the Bombay Stock Exchange has been recognized on a permanent basis. The other exchanges have been recognized for five-year renewable terms. How an exchange is organized is not a factor in determining recognition. Thus, the stock exchanges at Bombay, Ahmedabad and Indore are voluntary non profit-

making associations; those at Calcutta, Delhi and Bangalore are joint stock companies limited by shares; and those at Madras and Hyderabad are companies limited by guarantee [125].

After it recognizes a stock exchange, the Central Government exerts regulatory control over it. Periodic reports are furnished to the Central Government [126], and certain books and records are maintained for a period of five years [127]. The Central Government may make an inquiry itself, or through an appointed third party, into the affairs of a stock exchange or any of its members [128]. All officers, directors, members, and others who have had dealings in the matter under inquiry are required to produce requested documents, statements, or information [129].

The Central Government retains control over the stock exchange's by-laws and its rule amendments. A stock exchange, subject to previous Central Government approval, has the authority to make by-laws for the regulation and control of contracts and the regulation of trading. Similarly, no rule amendments have effect until they are approved by the Central Government [130]. The Central Government, furthermore, has the power to direct a stock exchange to amend its rules; and if it fails to do so, the government may directly amend such rules [131].

The Securities Regulation Act grants the Central Government power to suspend business and to supersede the governing body of a recognized exchange. The suspension of business may be complete or subject to conditions [132]. Suspensions may not last more than seven days initially but may be extended from time to time [133]. The Central Government may supersede the governing body of any exchange by declaration and then appoint any person or group of persons to exercise and perform all the powers and duties of the governing body [134].

Other powers granted to the Central Government include the ability to stop further trading in specified securities for the purpose of preventing undesirable speculation [135], and the power to compel a public company "in the interest of the trade or in the public interest" to list its securities on any of the recognized exchanges [136].

A dichotomy exists between the broad powers granted the Central Government, as described above, and the implementation of these powers. This dichotomy seems to have been built into the history of the Securities Regulation Act. The Gorwala Committee, upon whose draft the broad and powerful provisions of the Act were based, stated in its 1951 report:

Ordinarily, it should not be necessary for Government to interfere in the internal working of the exchange. Within its own sphere, the exchange should have a large measure of autonomy, and Government's role should be limited to keeping in touch with happenings on the exchange and ensuring that it enforces its bye-laws properly [137].

The Securities Regulation Rules specifically prescribe the qualifications necessary for membership on an exchange [138]. No person can be eligible for membership if he is less than twenty-one years of age, is not a citizen of India, has been

adjudicated bankrupt, or has been convicted of an offense involving fraud or dishonesty [139]. Only individuals and partnerships are permitted to be members. No companies, as defined under the Companies Act, may be admitted [140]. Once admitted, a member may not engage either as principal or as an employee in any business other than that of securities, except as a broker or agent not involving any personal financial liability [141].

The Securities Regulation Rules further prescribe the requirements with respect to listing securities on a recognized exchange [142]. The requirements are quite stringent. Besides requiring copies of memoranda and articles of association, prospectuses, offering literature, financials, etc. [143], the Rules compel such detailed production to the exchange that every letter or other document which has been part of or referred to in any securities offering in the last five years must be supplied in certified copy form [144]. It is doubtful that such production is meaningful since the exchanges, with the possible exception of the Bombay Exchange, do not have the personnel or expertise necessary to evaluate and analyze this information. Furthermore, it is believed that the majority of the exchanges do not have adequate filing systems so that all the documents of a specific company can be located or notice given if the required listing or follow-up information is not provided.

The Rules require a company, as a condition precedent to listing its securities, to forward to the stock exchange copies of statutory annual reports, annual returns and audited accounts as soon as issued [145], and to notify the exchange of a number of important events including a change in the general character or nature of the company's business [146], or any alteration of capital [147].

A stock exchange has the power to suspend or permanently revoke listing privileges based on breach or noncompliance with any of the conditions of admission, or for any other reason which it records in writing. A company may appeal such action to the Central Government [148].

It is evident that the Central Government has devoted very little manpower to implementation of the Act. The office of the Comptroller of Capital Issues within the Ministry of Finance has been delegated the authority to administer and enforce the Act. The Stock Exchange Division is one of three divisions with the office of the Comptroller of Capital Issues. Aside from clerical help, it has only five employees: namely, a joint director, two deputy directors, an assistant director, and a section officer [149]. Members of the Stock Exchange Division as well as a representative of the Company Law Board sit as government representatives on the governing body of each of the eight recognized exchanges. In practice, actual administration of the provisions of the Securities Regulation Act and of its Rules is thus left to the exchanges themselves.

The exchanges act through their governing bodies which generally consist of elected members, government representatives and an administrator. The 650 members of the Calcutta Stock Exchange, for example, choose fifteen members to serve on the board of directors, known as the Committee. The Committee selects a six-

teenth member, the Central Government appoints three representatives, and the executive director rounds out the twenty-man Committee [150]. The seventeen-man board of directors of the Delhi Stock Exchange consists of twelve members, three government representatives, one representative of the public, and the executive director [151]. It is, however, the leadership of individual personalities which, more than any other factor, determines the extent to which the laws, rules and regulations are adhered to by the members of the exchanges. Perhaps the best known such personality, about whom much has been written, was A.D. Schroff (1899–1965), former President of the Bombay Stock Exchanges. Mr. Schroff was looked upon as a financial visionary whose ideas and leadership virtually shaped India's economic development for nearly half a century. The present Chairman of the Bombay Stock Exchange, P.J. Jeejeebhoy, is following in Mr. Schroff's footsteps. He is well respected throughout India and in other parts of Asia where the Bombay Stock Exchange is the largest exchange west of Tokyo.

The Executive Director of the Delhi Stock Exchange, Colonel H.C. Verma, exerts great control over the day-to-day activities of this exchange. Colonel Verma feels it is up to him to set a strong standard of compliance, even in areas where the present regulations may not reach. Thus, in the situation where a company is exempt from the requirements of the Capital Control Act because its paid-up capital is below Rs. 500,000, Colonel Verma, in order to protect the public, has forced the company to comply with certain provisions of the Act before he will list its securities [152]. Similarly, S.L. Bardhan, President of the Calcutta Stock Exchange, and E.R. Krishnamurti, Executive Director of the Madras Stock Exchange, exert strong leadership.

3.4. Enforcement

India suffers from the absence of an overall coordinated securities enforcement program. The existing system lacks proper procedures, manpower, technical ability and a developed body of common law. The two primary entities that enforce securities regulations are the stock exchanges and the Department of Company Affairs.

3.4.1. Enforcement under the Capital Issues Control and Securities Regulation Acts

The Comptroller of Capital Issues within the Ministry of Finance administers the Capital Issues Control Act and the Securities Regulation Act and is empowered to conduct investigations and bring legal action, but has no manpower with which to do this. The relevant enforcement arm within the Ministry of Finance, the Directorate of Enforcement, deals only with problems that arise under the Foreign Exchange Regulation Act. The Comptroller of Capital Issues views his office as being wholly policy oriented and interested only in raising capital [153].

The Capital Issues Act provides that the Comptroller of Capital Issues can require a company or any of its officers to furnish him with accounts, books and documents for the purpose of determining whether the company has complied with

conditions imposed on its issuing capital [154]. The Act prohibits making material false statements in connection with furnishing the required accounts, books, and documents [155]. Violations of the Act or any order issued by the Comptroller of Capital Issues are punishable by fine and/or imprisonment for not more than one year [156]. The Act contains an interesting provision which, in the situation where the company has been found guilty, makes every director, manager, secretary and other officer also guilty unless they can prove that the offense was committed without their knowledge or that they exercised all due diligence to prevent its commission [157]. The Act further permits a good faith defense to all suits, prosecutions and other legal proceedings brought against the company or other persons [158].

The Securities Regulation Act, which provides for regulation of the stock exchanges and the trading of securities, arms the Comptroller of Capital Issues with more enforcement weapons than the Capital Issues Control Act. The books, records and documents of the stock exchanges and of member brokers are subject to inspection at all reasonable times by the Comptroller of Capital Issues [159]. Furthermore, the exchanges and their members may be required to furnish in writing any information or explanations concerning their affairs [160]. If the matter under inquiry is serious enough, a special investigator may be appointed with powers to compel the production of documents and the giving of statements, not only by exchange and brokerage personnel, but also by any person who directly or indirectly may be involved in the matter under inquiry [161]. Fine and/or imprisonment for not more than one year can be imposed for violation of a major provision; a fine can be imposed for violation of the mandatory listing requirements or dealing with a customer on a principal basis without the written consent of that customer [162]. When a company has committed an offense, every person who was in charge of and responsible for the conduct of its business shall also be deemed guilty unless he can prove that the offense was committed without his knowledge or that he exercised all due diligence to prevent its commission [163]. The Act further provides that if a violation by a company was due to the gross negligence of any director, manager, secretary or other officer, such person shall also be deemed guilty [164]. Under the Securities Contracts Rules the Central Government, after receiving the special investigator's report, may direct the governing body of the applicable stock exchange to take certain disciplinary action against the offending member including fine, suspension and expulsion [165]. These provisions under the Capital Issues Act and the Securities Regulation Act with respect to investigations and actions which can be taken against exchanges, their member brokers and others have never been invoked [166].

All the exchanges have bye-laws and regulations which govern the activities of the exchanges and their members. The misconduct described in the bye-laws for which a penalty may be imposed on a member include, *inter alia*: the conviction or commission of a fraudulent offense; conduct which is dishonorable, disgraceful, disorderly, improper or which willfully obstructs the business of the exchange; fail-

ure to submit books or records or to give testimony to the board of the exchange or other authorized person; conducting business through nominees or creating fictitious transactions; failure to carry out business with customers; offering to trade or actually trading in the streets; advertising to other than a broker's own customers; and failing to provide the proper margin deposits [167]. Penalties which may be imposed by the board of directors of an exchange for such misconduct are expulsion, suspension, withdrawal of all or any membership rights, imposition of a fine, censure, reprimand or warning [168].

Although an exchange may conduct an examination of the books and records of its members, it does not have the staff or technical ability to do so. A partner in one of the large brokerage firms in Calcutta stated that to his knowledge the exchange has never examined his firm's records [169]. The President of the Calcutta Stock Exchange did, however, state that on occasion employees of the exchange will examine a member's books to determine whether he is overextended or is trading beyond his working capital capacity. These are not full examinations and merely comprise a review of the member's position in various stocks and the amount of working capital he has available [170].

The most effective means of control the exchanges exert over their members is in the area of deposit requirements. Members must deposit with their respective exchanges a certain amount of money or securities, such as Rs. 20,000 cash or Rs. 22,000 of securities as required by the Calcutta Stock Exchange [171]. These deposits guarantee that members will fulfill their obligations to their customers and to each other. Furthermore, if the exchange finds evidence of or suspects that one of its members is involved in manipulating, cornering or taking a large position in a stock, it requires the payment of an additional deposit from the member, thus forcing him to liquidate his position [172]. Such action is intended only to prevent the manipulation of the market; no penalty or long-term preventative measures are taken.

Most of the officials at the various exchanges stated that action is very rarely if ever taken against its members. Officials of the Delhi Stock Exchange recalled that on two occasions members were expelled because they failed to pay their customers once the stock was delivered. One of these brokers appealed to the Delhi High Court, which upheld the expulsion [173].

3.4.2. Enforcement under the Companies Act

The Company Law Board, the regional directors, the registrars and the courts enforce the provisions of the Companies Act. The registrar is empowered to conduct limited investigations. If the registrar, upon reviewing documents required to be filed, is of the opinion that further information or explanation is necessary, he may order, in writing, such production from the company submitting the document and from the officers of that company [174]. The registrar may also call upon the company to provide any information or explanation pursuant to allegations brought to his attention that the company is defrauding its creditors or others it

deals with or is engaging in other unlawful practices [175]. Only an interested party can make such allegations. Allegations by third parties such as competitors will not be acted upon [176]. Failure to comply with the registrars's order is punishable in the courts by a fine up to Rs. 500, and for continuing offenses, Rs. 50 per day [177]. In certain circumstances the registrar is empowered to seize books and records of a company and its managing director. If the registrar has reasonable grounds to believe that such books and records may be destroyed, mutilated, falsified or secreted he may apply to the magistrate for an order permitting him to search for and seize such books and records [178]. The registrar conducts his limited investigation without visiting the company (with the rare exception of seizing books and records). Upon completion, he prepares a report which is reviewed by the regional director and submitted to the Company Law Board [179].

Under the Companies Act, the Board, in certain situations, has discretionary authority to appoint an inspector[s] to investigate the affairs of a company. In other circumstances the Board must appoint such an investigator. The Board may exercise its discretion in four circumstances: first, when the registrar has submitted his report and recommends a full investigation; secondly, on the application of not less than 200 members or at least 10 percent of the voting shares of a stock company; thirdly, when the company does not have share capital, on the application of at least 20 percent of its members [180]; and fourthly, when the Board is of the opinion that there are circumstances suggesting that the company has not made full disclosure to its shareholders, or that the company is defrauding its creditors or others it deals with or that the officers, directors or promoters of the company are guilty of fraud or misfeasance [181]. The Board must appoint an investigator if the company in question passes a special resolution or if a court, by order, declares that the affairs of the company ought to be investigated [182].

Since investigations are rarely undertaken [183] and are considered a serious matter which alone may have a material adverse impact [184]. Many companies challenge in court the right of the Board to order an investigation [185]. Such challenges are based on an abuse of discretion by the Board in ordering the investigation pursuant to item number four above. The Supreme Court of India has held that when challenged, the burden is on the Board to prove it has based its decision to order the investigation upon actual materials that are in existence and not upon materials it thinks exist [186]. Courts generally will not challenge the sufficiency or adequacy of the materials reviewed by the Board, but at least some *prima facie* showing must be made by the Board that such materials exist [187].

The inspector appointed by the Board to conduct the investigation can be drawn from the regional director's office or from the Inspection Wing within the Department of Company Affairs in New Delhi. An outside chartered accountant, attorney or other qualified individual may also be appointed as the inspector [188]. However, a provision in the Companies Act which prohibits the appointment of a firm, body, corporation or association [189] was specifically intended to prevent a firm of chartered accountants (as opposed to an individual) from conducting the investigation [190].

The inspector is empowered to investigate the affairs of the company in question and the affairs of related and affiliated companies [191]. In certain situations where the inspector seeks to look into the affairs of another company which is or was managed or directly controlled by the primary company, prior approval of the Board is required [192].

The first business of the inspector is to write to the company notifying it of the nature of the investigation and requesting full assistance. The inspector then visits the company. If he is from a regional director's office, he generally is assisted by a stenographer. At the initial stages the investigation is more in the nature of an audit. Minutes of meetings of the board of directors are examined to determine who is empowered to sign checks. An examination of the company's books and records for the past three years is then made. Where problems are found, a letter is sent to the company requesting it to clarify them. When satisfactory explanations are not forthcoming, the inspector takes the testimony of, or obtains signed statements from, relevant persons [193].

The Companies Act specifies the sanctions to be imposed by the courts for failing to cooperate with the inspector [194]. If any person without reasonable cause refuses to produce books and records, testify under oath, answer any question once put under oath, or sign the written notes of his examination once read by or to him, he may be imprisoned for up to six months and/or fined up to Rs. 2,000. A fine of up to Rs. 200 per day for continuing such obstructive conduct may also be imposed [195]. Inspectors, under the same circumstances as registrars, may search for and seize the books and records of a company and its manager or managing director [196].

In a challenge to the authority of an investigator to require the production of documents and oral testimony under oath, the Supreme Court of India has held that a person cannot refuse to do so based upon a right not to be compelled to give self-incriminating evidence pursuant to Article 20(3) [197] of the Constitution of India [198]. The Court reasoned that the right against self-incrimination attaches only at the time a person is accused of a crime and that an investigation authorized under the Companies Act is no more than a fact-finding commission, involving neither an accuser nor an accused [199].

The inspector, upon completion of the investigation, prepares a final report of his findings. He may also have prepared an interim report if so directed by the Board. Inspectors' reports contain only findings; they do not recommend specific actions [200]. The Board has authority to provide copies to interested parties and to publish such reports [201]. Inspectors' reports, as opposed to a registrar's report, are admissible in any legal proceeding as evidence of the opinion of the inspector in relation to any matter contained in the report [202].

The Board reviews the inspector's report and determines what, if any, action should be taken. Where serious offenses are indicated, the Board may refer the matter for criminal prosecution to the police or the Central Bureau of Investigations [203]. Where lesser offenses punishable by a fine are indicated, the Board refers the

matter to the regional director who oversees the prosecution of the case in magistrate's court. These cases are handled by prosecutors who are under the control of the registrar of companies [204]. The Board also has the option to authorize the filing of a civil suit for recovery of damages or property. Such suits are brought in the name of the company which benefits from any recovery. The company is entitled to receive indemnity from the government for any costs it may have incurred in connection with the suit [205].

The investigative procedure described above is similar to that of the SEC. The staff of the SEC conducts a preliminary investigation, gathering facts and evidence with the voluntary cooperation of individuals and companies. If it feels a broader investigation is warranted, the staff submits a memorandum to the Commissioners seeking their authority to issue subpoenas and take the testimony of witnesses under oath. If at the conclusion of the investigation it feels enforcement action is warranted, the staff recommends in a memorandum that the Commissioners authorize it to refer the matter for criminal prosecution, file a civil action in federal district court seeking to enjoin violative conduct, initiate an administrative action seeking to sanction those entities who are registered with the Commission, or issue a report disclosing the results of the investigation. Such possible dispositions are not mutually exclusive. The Board, however, does not have the option of bringing a civil injunctive action and is therefore precluded from immediately preventing continuing violations and from utilizing the threat of criminal contempt against those who repeatedly violate the law.

The Sachar Committee has made broad recommendations concerning structural changes in the existing administrative working of the Board and in the area of prosecutions and penalties. The Board, as presently constituted, is made up of a chairman and members who are the secretary and joint secretaries of the Department of Company Affairs. With respect to the same company, these individuals may be in the conflicting position of exercising their administrative duties based on political or economic concerns and also hearing and deciding matters in their judicial capacity [206]. The Sachar Committee recommends that the Board be made a quasi-judicial tribunal, independent of the executive authority of the Central Government, thereby ensuring that the Companies Act will be administered in such a manner that decisions can be made without the possible influence of executive considerations [207]. The proposal would establish a tribunal similar to the Income-tax Appellate Tribunal as provided under Section 252 of the Income Tax Act, 1961 [208].

The Sachar Committee recognized that the present scheme of prosecution under the Companies Act suffers from certain defects, primary among which is the necessity of initiating an entire legal proceeding every time a company defaults in its statutory filing obligations [209]. The regional directors and registrars are authorized to file complaints without prior consultation with the Board in certain situations [210]. Company prosecutors, assigned to each registrar's office, represent the registrar or the regional director in court. Most prosecutions are brought against small

private companies [211]. Of the 7,649 prosecutions initiated for the fiscal year ending March 31, 1978, 7,455 or 97.5 percent were for failure to file and/or give to shareholders annual financial and other reports and for failure to hold annual shareholders' meetings [212]. These types of violations are easy to prove and the conviction rate is approximately 98 percent [213]. The penalties imposed by the courts are almost always in the form of a fine and are so abnormally low that prosecution does not provide an adequate deterrent [214]. The Sachar Committee recommends that the registrars and the Board be clothed with the powers of a court to impose certain penalties. Administratively, under the proposal, a registrar or the Board would issue a notice to any person or company to show cause why the penalty listed in the notice should not be levied for violating certain specified provisions. Fines would be levied for every day of noncompliance. Officers and directors of the company would only be prosecuted in court to secure their imprisonment when the fines imposed are not paid and compliance has not been achieved. Appeal would be from the registrar to the Board and finally to the high courts [215]. In the United States, when a company fails to file required documents with the states in which they are incorporated, their corporate charter is revoked, but neither criminal nor civil actions are pursued. Even in the case of public companies, the SEC selectively brings civil actions to obtain compliance. Hundreds of public companies, whose stocks are thinly traded over-the-counter, escape from complying with the filing requirements under the Securities Exchange Act of 1934 [216].

3.4.3. Private rights of action

Private rights of action as an adjunct to securities regulation are virtually nonexistent in India. The Companies Act provides that directors, promoters and experts may be held civilly liable for misstatements in the prospectus [217]. No such liability is imposed for selling unregistered securities or for misstatements appearing in subsequent filings. An attorney who signs the prospectus stating that the company has complied with all relevant laws may be sued as an expert [218]. However, liability may be avoided by proving that there was reasonable ground to believe that the statements in the prospectus were true [219]. Civil liability may also be imposed under the India common law theories of tort, contract, fraud, breach of trust and loss caused to the corporation by misfeasance, malfeasance or nonfeasance [220]. Civil liability cases under the Companies Act are rarely pursued in the courts [221]. By nature, Indians seem to be antiligious and do not generally perceive court action as the means to rectify wrongs [222]. Also, the courts discourage private damage actions by keeping recovery amounts low [223].

4. The brokerage community and problem trading practices

The brokerage community is primarily made up of one- and two-man firms. Each member of the firm must also be a member of the exchange; however,

exchange deposit requirements are reduced for additional members of the same family. Many brokers do not have offices separate from their facilities at the exchange. Around the floor and open balcony of the Delhi Stock Exchange, for example, there are located many small rooms. These rooms, perhaps no more than eight feet by ten feet at most, serve as the brokers' offices. Many of these rooms have beds or cots, a desk, file cabinets and eating utensils. Several people are usually crowded into these rooms, busily engaged in business activities.

The largest brokerage firms in India are small in comparison to firms in the United States. The largest firm in India in terms of volume is Bhupendra Champakal Devidas of Bombay, a successor to a firm started in 1920. It presently has thirty employees, six of whom are professional brokers. The firm acts as the managing underwriter of twelve to fifteen issues and participates in fifty to sixty additional underwritings per year. It maintains a correspondent relationship with Stewart & Co., one of Calcutta's largest brokers. Devidas plans to enter the investment advisory business in Bombay [224], where only two such firms can presently be found [225].

The rules and bye-laws of the exchanges do not recognize distinctions between brokers. Over the years, however, brokers have developed expertise in certain areas of trading. These functional specialists are generally referred to as: commission brokers; floor brokers; taravniwallas or specialists; odd-lot dealers; budliwallas or financiers; arbitrageurs; and security dealers. The commission broker executes transactions on the floor of an exchange as agent for his customer. The floor broker executes trades on the floor for other brokers, splitting the commissions. Taravniwallas or jobbers are somewhat akin to the specialists on the floor of the several exchanges in the United States. Most trades are transacted through the taravniwallas. Odd-lot dealers trade as principals in transactions involving less than the customary trading units. Budliwallas lend money or stock to other brokers who wish to carry over or to prevent a transaction from clearing at the end of the settlement period. The budliwalla's fees are equal to the difference between the price at the time of the loan and the price that would be paid at settlement, plus interest. Arbitrageurs generally specialize in trading in the same stock on different markets. Brokers, hampered by the rule that they may only be members of one exchange, have established correspondent relationships with brokers of other exchanges. Security dealers specialize in trading as principal in gilt-edged securities issued by the Central and state governments and other statutory public bodies.

An analysis of the trading practices of the taravniwallas reveals a continual pattern of open and blatant abuses [226]. Unlike specialists operating on the floors of exchanges in the United States, the taravniwallas are not regulated. They are not subject to any special capital or other requirements, and are not required to quote two-way markets. They are not limited to acting as dealers. Many execute trades for their customers, partners or others for which they receive a fee, thus acting as principal and agent on the same transaction [227]. The taravniwallas do not accumulate a "book" of limit orders. They may walk away from (and generally do and refuse

to take) a long position in a declining market. There is a general feeling among brokers that many taravniwallas are not trustworthy [228].

Although the exchanges have the ability to report transactions on a timely basis, they fail to see the necessity for doing so. Only a modicum of such information is obtained and broadcast. When a trade is consummated between brokers, each makes a note of the particulars in his trading book. No official record is kept. When the price is different from the last trade a floor official is notified. He makes arrangements to have this price placed on the board listing the stocks and their last trade price. No data is accumulated on the size of individual trades or, more importantly, on the total daily volume of trades in each security. It is not possible to determine the total daily exchange volume or to develop meaningful indexes. Failure to report such vital data means that investment decisions are being made on less than a fully informed basis. Moreover, such data is an indispensable tool in an overall surveillance program. Unfortunately, none of the exchanges have what appears to be even a semblance of such a program.

The exchange regulation that establishes a maximum brokerage commission scale places brokers in potentially compromising situations. Exchanges have set the maximum fee at 1 percent on stock transactions and 0.5 percent on transactions involving government and statutory body securities, debentures or loans [229]. Oftentimes, brokers are forced to reduce their fees even lower in order to remain competitive. It has been suggested that brokers must be able to make an adequate living in order to maintain proper standards among members of the exchange and to provide adequate services to their customers [230]. Many brokers, being unable to maintain a minimum income based on brokerage commissions, are forced to trade for their own account [231]. They tend to borrow from the budliwallas in amounts beyond their means and many times either lose money, engage in manipulative conduct, or both. The practice of setting maximum brokerage fees in what is generally recognized as a low turnover market prevents brokers from attracting and training qualified professionals. More often than not, brokerage firms follow the Indian custom of using family members to staff and ultimately succeed in the ownership of the business. Also, without adequate control and professional staff, brokers are prevented from performing the necessary functions of underwriters: providing liquidity for the secondary market; conducting basic market research and dissemination of market information and advice. The brokers' role in underwriting has decreased dramatically over the last ten years and will continue to do so, primarily because they have been prevented from accumulating a capital base and experienced professional staff. Once a market has developed to the point where its very existence, or at least its stability, is no longer threatened by an undercapitalized and unprofessional broker community, the brokerage fees should best be left to market competition. India is far from this situation, and consonant with other measures which should be taken with respect to its brokers, should allow them to earn an adequate minimum brokerage commission [232].

5. Conclusion and recommendations

5.1. Supporting factors

A strong correlation exists between an effective enforcement program and an effective market system. However, factors other than regulation impact upon the efficiency of a market system. The opportunity and incentive to invest freely in a multitude of instruments where individual risk/reward priorities can be satisfied, high liquidity, and a prosperous broker-dealer community aid in the implementation of an overall enforcement program. It is therefore important to consider recommendations with respect to these other factors in conjunction with specific enforcement recommendations.

In countries developing a securities market system, it has been suggested that promotional measures are as important as regulatory ones. A securities commission or similar agency should serve the dual role of promotor and regulator [233]. Although India has a developed securities market system, only 0.4 percent of the population participate. It therefore must engage in an active campaign to educate potential investors to the advantages of securities ownership. Concomitant with this is the necessity to coordinate various government programs in order to decrease or eliminate the disincentives to trading and to increase or create the proper incentives. With respect to education, India has certain advantages over other developing countries. It has well-established college, university and specialty school programs. It also has well-respected accounting and legal professions.

Education, however, must first begin with the securities industry by training and qualifying individuals in the fields of corporate finance, investment banking, securities analysis, merchandising, and advising. A professional staff of government regulators, including market specialists, analysts, accountants and attorneys should be organized and a training program developed. To a rudimentary degree, some of this is already being done. For the past two years, E.R. Krishnamurti, Executive Director of the Madras Stock Exchange, has taught a post-graduate course on portfolio management at Madras University [234]. The Bombay Stock Exchange has plans to establish a training school for future brokers and exchange personnel [235].

A full commitment should be made by the government and the securities industry to making the public aware of the existence of the exchanges and the benefits of equity ownership. The public must also be educated on the use of available financial and other data in making investment decisions. The general attitude that only those with an "inside tip" dare trade in securities must be overcome. Rules preventing brokers from advertising and making recommendations stand as a barrier to informed investors. In an attempt to reach and properly service a greater number of potential investors, brokers should open branches in cities and locations that do not have an exchange. Presently, all brokers have offices at or within the vicinity of the exchanges.

The Central Government should realize the necessity of coordinating its pro-

grams to encourage investment in the stock market. Taxes on income, wealth and capital gains should be re-evaluated to determine their overall impact on investment decisions [236]. The restrictions and practices preventing foreign ownership of stock under the Foreign Exchange Regulation Act, 1973, should be examined in light of India's positive balance of foreign payments position. Limitations by the Central Government on dividends and interest on ordinary and convertible debentures (recently set at 11 percent by the Comptroller of Capital Issues) dampens investor interest, particularly in the more speculative companies.

The stock market suffers from lack of a proper mix of investment instruments to meet the risk/reward requirements of investors. There is also an insufficient number of tradable securities. India has been called "very primitive" because it limits its securities instruments to common and preferred stocks, corporate debentures and government and quasi-government loan instruments [237]. Efforts should be made to introduce additional instruments such as income bonds (a favorite of railroads in the United States), participation certificates whereby lenders participate in a number of loans (popular in Mexico), secondary market instruments in home loans from the newly created Housing Development Finance Corporation, and second trust instruments.

Certain measures could be taken to increase the number of shares on the market. Of the 745 government companies, only 300, or 40 percent, are public. However, only 8.5 percent of the aggregate paid-up capital of all government companies belong to these public companies [238]. Many state-owned trading companies are earning a 25 percent return on equity. These factors indicate that many government private companies no longer need the protection and other benefits their special positions permit and are in a good position to and should offer their shares to the public [239].

India's economic development program is largely conducted through loan and equity investments made by public financial institutions and state financial and industrial development corporations. For fiscal year ending March 31, 1978, these institutions were responsible for purchasing 15.6 percent of all underwritings [240]. Brokers bitterly complain that these institutions regularly hold onto their shares longer than necessary, thus locking up large blocks of stock. The same complaint is made against the General Insurance Corporation, the Life Insurance Corporation, and the Unit Trust of India, all of which deal more in the secondary market.

The government's banking policy seems to ignore the existence of the equity market. Banks are required to deposit 6 percent of their cash with the Reserve Bank of India and use an additional 33.3 percent of it to purchase government securities. Banks have been forced to increase their deposits with the Reserve Bank because of a recent abundance of savings deposits. This presently leaves the banks with less than 51 percent of their deposits to lend to the public. Coupled with the requirement that they lend according to government priorities, banks have no money available for equity investors or for brokers to loan to their customers. Also, the requirement of the Security Act of 1928, forcing provident funds to invest in government

securities, postal savings deposits (maximum of 30 percent) and national banks (maximum of 10 percent), artificially depresses demand in the equity market.

5.2. Trading practices

Although it is always easy to recommend that a committee be appointed and a study made, such an undertaking might be particularly meaningful in the area of market trading practices. The author is not aware of any such comprehensive study having been conducted during the last thirty years in India. Such a study could take the form of a management-type evaluation conducted by a team of experts from foreign exchanges and regulatory bodies.

As indicated by previous discussions, certain steps should be taken to correct trading practice abuses. The taravniwallas or jobbers must be better regulated. Special rules should be adopted to control their trading activities to ensure the maintenance of a fair and orderly market, *i.e.* maintaining price continuity with reasonable depth and minimizing the effects of a temporary disparity between supply and demand. Other reforms might include changing the trading rules to compel brokers to yield priority to public orders to prevent them from competing with their customers. Certain measures should be taken to truly eradicate forward trading and to increase the maximum brokers' commission rate.

5.3. Overcoming the myth of self-regulation

Indian investors are being deceived by the myth of self-regulation. From appearances it seems that the exchanges are regulating their member-brokers and overseeing a corporate disclosure program, and that the Central Government is a participant and big brother to all of this. The Indians have not realized that a properly carried out program of self-regulation is invaluable. In the United States a special Congressional study on securities markets found that:

Regulation in the area of securities should . . . be a cooperative effort, with government fostering maximum self-regulatory responsibilities, overseeing its exercise, and standing ready to regulate directly where and as circumstances may require [241].

The fact is that the Central Government does not oversee self-regulatory responsibilities and, despite the power and need to do so, has never regulated directly. The same three government individuals sit as members of the governing bodies of the eight exchanges. Along with their other duties, they do not have the time to properly monitor exchange activities. Examinations of the exchanges and the broker community have never been conducted. Likewise, no proceedings have been brought directly by the Central Government against the exchanges or any of their members.

India needs an overall coordinated securities enforcement program. It is essential

that such a program begin with the Central Government. Professional staff in the areas of corporate finance, market regulation and enforcement must be assembled. A stock exchange and broker-dealer examination program should be developed and implemented. Examinations should be conducted on site and on a surprise and causes basis. The quality of examinations by exchanges of their members would be checked by government oversight examinations of some of these same brokers. Where indicated, enforcement action should be taken by the exchanges *and* by the Central Government. Surveillance programs would be a necessary component of an overall enforcement program. At the exchange level it would be necessary to monitor corporate filings and to take quick action against delinquent companies. Better exchange records should be maintained to identify the exact time, amount of stock, price and brokers involved in every transaction. At the government level, the surveillance program would monitor the effectiveness of the exchanges' programs and refer matters for inquiry and possible enforcement action.

When asked why there have been no prosecutions for stock manipulation or insider trading violations, exchange and government personnel stated that such practices, although prevalent, are almost impossible to prove. In the United States such prosecutions are based on circumstantial evidence (absent an admission). India, because of the lack of proper record-keeping by exchanges, brokers, companies and the government, is not even in a position to accumulate circumstantial evidence [242].

Presently, proceedings under the Companies Act result in imprisonment or fine, usually the latter. A particularly effective means of preventing ongoing violations from continuing is through the use of a restraining order or injunction. This remedy is singularly important in the securities field where fraudulent schemes and the dissemination of false information can mean the ruin of many investors. Injunctions can also be effectively utilized under the Capital Issues Control and Securities Contracts Regulation Acts.

The use of civil suits as an adjunct to the overall enforcement program should be encouraged.

Provision for civil liability relieves the administrative agency of much of the enforcement burden and at the same time may actually be a more effective deterrent against violation of the law than any fear of administrative action by a harried and understaffed government agency. Moreover, where it is not feasible to provide adequate enforcement by means of inspections of the offices of brokerage and investment firms, or by other continuous supervisory methods, it may be possible to encourage members of the public to complain of misconduct to the government. A relatively small staff of investigators could follow up those complaints that appear to have merit [243].

In India, civil liability is provided by statute for violations of the various acts. In practice, however, few such suits are brought. One result of a strong enforcement program would be a flow of follow-up civil suits. Thought should be given to encouraging such litigation by developing an interest in securities law through bar

associations, making a defendant liable to pay the plaintiff's attorneys' fees if he loses, and doubling or tripling the amount of recovery.

5.4. *The future*

The past few years have seen a tremendous shift in global financial activity to the Middle and Far East. India, being the world's largest democracy and sitting at the crossroads of this phenomenon, has the resources to become the financial and industrial center of Asia. Already, several of the Arab countries, particularly Saudi Arabia and Kuwait, have made large investments in India. Presently, India is exporting the technology and labor force to Arab and African nations. India's ability to develop internally and as an industrial and financial leader depends in no small way on the stability and viability of its securities market system. Realizing that the cornerstone of such a system is investor confidence, India must now concentrate on achieving this goal by developing and implementing an overall securities enforcement program.

Appendix A

Individuals who were personally interviewed in the United States

Indian Embassy: N.A. Palkhivala, Ambassador to the United States and former Bombay corporate and tax attorney (Washington, October 23, 1978); R.L. Misra, Minister Economic (Washington, October 23, 1978); Satish Chandra, First Secretary (Economic) (Washington, June 6, 1978).

World Bank: V.M. Narasimham, Executive Director, former Governor of the Reserve Bank of India, former Secretary, Department of Banking, and former Additional Secretary, Department of Economic Affairs (Washington, May 23, 1978); P.M. Mathew, Deputy Director, Capital Markets Department (Washington, June 13, 1978); Promodh Malhotra, Investment Officer, Capital Markets Department (Washington, June 13, 1978); Eugene Rotberg, Treasurer (Washington, May 1, 1979); P.T. Tan, Senior Counsel — India and Sri Lanka, Office of the General Counsel, former Secretary of the Securities Industry Counsel — Singapore, and author of an unpublished manuscript, *Securities Regulation in Singapore and Malaysia — a Primer on the Laws of the Stock Exchange* (Washington, April 13, 1979); V.V. Bhatt, Division Chief, Public Finance Division (Washington, October 23, 1978).

Securities and Exchange Commission: Irving M. Pollack, Commissioner (Washington, December 1978–January 1979); Yeiichi Kuwayama, Special Assistant, International Capital Markets, Directorate of Economic and Policy Research (May 22, 1978); Carl T. Bodolus, Office of International Corporate Finance, Division of Corporation Finance (Washington, May 16, 1978); Martin Moskowitz, Counsel to Office of the Director, Division of Market Regulation, author of *Preliminary Survey*

of the Securities Markets of Korea (1965) (Washington, June 8, 1978); Terrence C. Reilly, Senior Legal Advisor for International Securities, Division of Market Regulation, former Director of International Policy (May 23, 1978).

Miscellaneous: Louis Loss, Professor, Harvard Law School (Cambridge, July 28, 1978); J.L. Bajaj, Resident Director, Indian Investment Center — New York (Washington, June 6, 1978); David Silver, President, Investment Company Institute and Co-author of *Regulation of Indian Stock Markets: A Preliminary Survey* (1965) (Washington, June 8, 1978).

Appendix B

Individuals who were personally interviewed in India

Justices: B.P. Sinha, Chief Justice (retired), Supreme Court of India (Punjab, November 8–11, 1978); A. Kalasam, Justice, Supreme Court of India (New Delhi, December 8, 1978); R. Ramprasadrao, Chief Justice, Tamil Nadu High Court (Madras, December 5, 1978); S. Mohan, Justice, Tamil Nadu High Court (Madras, December 5, 1978).

Ministry of Finance: A.V. Ganesa, Controller of Capital Issues (New Delhi, November 17, 1978, December 7, 1978); M.R. Miyya, Joint Director, Stock Exchange Division, Office of the Controller of Capital Issues (New Delhi, November 17, 1978, December 7, 1978).

Department of Company Affairs, Ministry of Law, Justice and Company Affairs: M.K. Kukreja, Joint Secretary, member of the Company Law Board and Secretary to the High Powered Expert Committee on Companies and MRTP Acts, 1977–8 (New Delhi, November 17, 1978); N. Neelakatan, Joint Secretary, member of the Company Law Board, and Chief of the Inspection Wing (New Delhi, November 17, 1978); Shadi Lal, Senior Research Officer (New Delhi, December 7, 1978); J.P. Mukherjee, Regional Director (Calcutta, November 23, 1978); A.G. Sirsi, Regional Director (Bombay, November 27, 1978); K.N. Ramachandran, Official Liquidator (Madras, December 5, 1978).

Stock exchanges: joint interview with Col. H.C. Verma, Executive Director, and Béhari Lal Chowdhary, President, Delhi Stock Exchange (Delhi, November 16, 1978); joint interview with officials of the Calcutta Stock Exchange, S.L. Bardhan, President, Dr. B.B. Ghosh, Executive Director, B. Majumdar, Secretary, P.K. De, Deputy Secretary (Calcutta, November 20–21, 1978); joint interview with officials of the Madras Stock Exchange, E.R. Krishnamurti, Executive Director, V.K. Sundaram, President, and S. Narayanswami, past president (Madras, December 4, 1978); interviews with officials of the Bombay Stock Exchange, P.J. Jeejeebhoy, Chairman (Bombay, November 27, 30, 1978); R.R. Nair, Chief Statistician (November 26, 1978); Rabinder Nath, editor, *The Stock Exchange Official Directory* (November 30, 1978).

Reserve Bank of India: joint interview, V.B. Kadam, Adviser and Officer-in-Charge, Economic Department, and N.A. Mujamdar, Advisor to the Governor, Economic Department (Bombay, December 1, 1978); joint interview, A. Hasib, Secretary, B. Ray, Deputy Secretary, and A. Gogate, Director of Banking Division, Economic Department (Bombay, December 1, 1978); joint interview, N.V. Sundaram, Chief Legal Adviser, and M.A. Batki, Legal Officer (Bombay, December 1, 1978) R. Janakiraman, Joint Chief Accountant (Bombay, December 1, 1978).

State Bank of India: S.V. Shanmugavadivelu, General Manager, Merchant Banking Division (Calcutta, November 22, 1978, and Bombay, November 27, 1978); R.S. Bhatt, Adviser, Merchant Banking Division, also founder and chairman of the Indian Investment Center, founder and former chairman of the United Nations Commission on Transnational Corporations, and director of over ten of India's largest corporations (Bombay, November 28, 1978).

Industrial Credit and Investment Corporation of India: James Ray, nonexecutive Chairman, former Vice President of the World Bank (Bombay, November 30, 1978); S. Kumarasundaram, Wholetime Director (Bombay, November 30, 1978); and K. Ramachandran, Manager — Calcutta (Calcutta, November 23, 1978).

Brokers: Bhupen C. Dalal, majority partner in Bhupendra Champaklal Devidas, largest brokerage firm in India (Bombay, November 27–28, 1978); Rasikal Maneklal (Bombay, November 29, 1978); joint interview with Manaj Dhupelia and S.A. Shah of the Calcutta brokerage firm, Stewart & Co. (Calcutta, November 21, 1978); joint interview with E.V. Rajagopalan and V. Sri Ram of the Madras brokerage firm, Paterson & Co. (Madras, December 4, 1978); S. Narayanswami of the Madras brokerage firm, Chitra & Co. (Madras, December 5, 1978); joint interview with V.K. Sundaram, V.K. Padmanabhan and V.J. Rajagopalan of the Madras brokerage firm, V.S. Krishnaswami (Madras, December 5, 1978).

Attorneys: B.P. Ray, senior partner in the Calcutta law firm, Orr, Dignam & Co., largest in India (Calcutta, November 23, 1978); J.P. Thacker of the Bombay law firm, Mulla & Mulla & Craigie Blunt & Caroe (Bombay, December 1, 1978); joint interview with C. Doraswami and Dulip Singh of the Madras law firm, King & Partridge (Madras, December 5, 1978); and Lalit Bhasin of the New Delhi law firm Bhasin & Bhasin (New Delhi, December 7, 1978).

Accountants: V.B. Harihbakti, President, Indian Merchants Chamber, past President, Institute of Chartered Accountants of India, of the national accounting firm, Harihbakti & Co.; joint interview with C.C. Chokshi, past President of the Indian Merchants Chamber and Institute of Chartered Accountants of India and N.V. Iyer of the Bombay accounting firm, C.C. Chokshi & Co (Bombay, November 27, 1978).

Miscellaneous: Joint interview with G.S. Patel, Chairman, H.C. Bhatt, Director of Investment-Underwriting, K.N. Atmaramani, Joint Director (Investment), and Dr.M. Sharma, Research Officer, of the Unit Trust of India (Bombay, December 2, 1978); C.R. Thakore, Chief (Investment), Life Insurance Corporation of India (Bombay, November 29, 1978); H.T. Parakh, founder and Honorary Chairman,

Housing Development Finance Corporation (Bombay, November 29, 1978); G.N. Sinha, Company Secretary, Hindustan Milkfood Manufacturers Limited (Delhi, November 16, 1978); A.K. Ghosh, Managing Director in the Calcutta investment banking and management consulting firm of Robson Black & Ghosh (Calcutta, November 21, 1978).

Notes

- [1] See Appendix A for a list of individuals who were interviewed in the United States.
- [2] See Appendix B for a list of individuals who were interviewed in India. This list includes government regulators, exchange personnel, brokers, underwriters, bankers, justices, attorneys, accountants and corporate directors and secretaries.
- [3] The author, an attorney in the SEC's Division of Enforcement for over seven years and being responsible for investigating and litigating securities violations, realizes that he brings a certain bias to this project. To counter this, an attempt has been made to include in the equation the experiences of securities enforcement schemes of other countries.
- [4] Gill, *Domestic Financial Systems and External Financial Policies*, paper presented at the Conference on External Financial Policy, Santiago, Chile (1977).
- [5] Department of Company Affairs, Ministry of Law, Justice and Company Affairs, *The Twenty-Second Annual Report on the Working and Administration of the Companies Act, 1956* (1978) at 24, 30 [hereinafter cited as *Twenty-Second Annual Report*].
- [6] The New York Stock Exchange, 1978 Fact Book (1978) at 37. The Stock Exchange Bombay, *The Stock Market in India* (1977) at 21.
- [7] There is a post office in most of India's 600,000 villages. Also, the State Bank of India, the largest bank in the world in terms of number of branches, has located its branches within reach of most Indians.
- [8] Unit Trust of India Act, 1963.
- [9] There are approximately 8 Rupees (Rs.) to the dollar.
- [10] *Unit Trust of India Annual Report 1977-1978* (1978) at 5-7.
- [11] See Indian Investment Centre, *India Company Law* (1975) at 1.
- [12] Arokiaswami, *The Modern Economic History of India* (1949) at 149.
- [13] At the height of its power, Andrew Yale & Co. managed 54 companies, some of them being the largest jute, tea and coal companies in India. *Id.* at 150.
- [14] Desai, *Economic History of India Under the British* (1968) at 89.
- [15] Arokiaswami, *supra* n. 12 at 150-151.
- [16] Desai, *supra* n. 14 at 89-90.
- [17] Arokiaswami, *supra* n. 12 at 151-152.
- [18] The managing agency system is still quite prevalent in Pakistan.
- [19] Arokiaswami, *supra* n. 12 at 152.
- [20] Indian Investment Centre, *supra* n. 11 at 4.
- [21] The Companies (Amendment) Act, 1969 (1177 of 1969).
- [22] The Bombay Stock Exchange, *History, Regulation and Organization of the Stock Market in India*, (1978) at 2-3 [hereinafter cited as *History, Regulation and Organization*].
- [23] The term "broker" or "share broker" as used in this paper and in India equates with the term broker-dealer as used in the United States.
- [24] Garg, *Stock Exchanges in India* (1948) at 17-18.
- [25] Thomas, *Report on the Regulation of the Stock Market in India* (1948) at 1.
- [26] Garg, *supra* n. 24 at 17-18.
- [27] Thomas, *supra* n. 25 at 2.
- [28] *History, Regulation and Organization*, *supra* n. 22 at 9-10.
- [29] *Id.* at 11-12; Garg, *supra* n. 24 at 21-23. The stock exchanges are located at: Ahmedabad, Bangalore, Bombay, Calcutta, Delhi, Hyderabad, Indore and Madras.
- [30] Arokiaswami, *supra* n. 12 at 19.
- [31] *Id.* at 29.
- [32] Thomas, *supra* n. 25 at 3.

- [33] *Id.* at 4–5.
- [34] Garg, *supra* n. 24 at 32–38.
- [35] Thomas, *supra* n. 25 at 6.
- [36] *Report of the High-Powered Expert Committee on Companies and MRTP Acts* (August, 1978) at 2 [popularly referred to and hereinafter cited as *Sachar Committee Report*, named after its Chairman, Justice Rajindar Sachar]. The Sachar Committee was established by the Indian Parliament on June 23, 1977 to consider and report on what changes (with particular emphasis on form and structure) are necessary in the Companies Act, 1956, and the Monopolies and Restrictive Trade Practices Act, 1969.
- [37] Companies Act §220.
- [38] *Twenty-Second Annual Report*, *supra* n. 5 at 29.
- [39] Companies Act §25.
- [40] *Twenty-Second Annual Report*, *supra* n. 5 at 31.
- [41] Companies Act §12 (2).
- [42] *Twenty-Second Annual Report*, *supra* n. 5 at 30.
- [43] *Id.* at 24.
- [44] *Id.* at 25.
- [45] *Id.*
- [46] Companies Act §12 (1). See §3 (1) (iii) for the definition of a private company.
- [47] *Id.*, §252.
- [48] *Id.*, §266.
- [49] *Id.*, §70.
- [50] *Id.*, §§44, 198, 309.
- [51] *Sachar Committee Report*, *supra* n. 36 at 306.
- [52] Companies Act §43A.
- [53] *Sachar Committee Report*, *supra* n. 36 at 22.
- [54] Companies Act §56.
- [55] *Id.*, §167.
- [56] *Id.*, §171.
- [57] *Id.*, §439.
- [58] *Id.*, §391–394.
- [59] *Id.*, §395.
- [60] *Id.*, §235.
- [61] *Id.*, §399.
- [62] *Sachar Committee Report*, *supra* n. 36 at 54–55, 62–63.
- [63] Shareholders Associations, under the *Sachar Committee Report's* recommendations, would be entitled to avail themselves of the rights prescribed in §§399–409 of the Companies Act dealing with oppression and mismanagement. At least one noted commentary has criticized this recommendation because the Sachar Committee did not suggest practical means to implement its recommendation. J.P. Thacker, a Bombay corporate solicitor, in a November 11, 1978, speech to the Indian Merchants' Chamber, pointed out that the recommendation fails to address such questions as: What views will be put forward by the Association and how will they be attained? How will enough funds be raised, particularly from shareholders holding small numbers of shares in various parts of India, to purchase the requisite number of shares and to staff and maintain an office?
- [64] Companies Act §§209–233B and Schedule VI.
- [65] *Id.*, §209.
- [66] *Sachar Committee Report*, *supra* n. 36 at 64.
- [67] *Id.* at 71–72.
- [68] Companies Act §227.

[69] *Id.*, § 307.

[70] *Id.*, § 308.

[71] *Sachar Committee Report, supra* n. 36 at 69–70.

[72] *Id.* at 69. It has been pointed out that this restriction may not be particularly effective because it does not prohibit trading from the third to the sixth months of the accounting year, the end of the six months being when financial statements are required to be filed and thereby made public. Interview with C.C. Chokshi and N.V. Iyer of the Bombay accounting firm, C.C. Chokshi & Co. (November 27, 1978); interview with J.P. Thacker, of the Bombay law firm, Mulla & Mulla & Craigie Blunt & Caroe (Bombay, December 1, 1978).

[73] *Sachar Committee Report, supra* n. 36 at 79.

[74] Companies Act § 227 (4A).

[75] *Id.*, § 10E.

[76] *Id.*, § 637.

[77] These powers were delegated pursuant to the requirements of § 637 of the Companies Act, namely, notice in the October 18, 1972 issue of *The Official Gazette*.

[78] These powers concern amendments to a memorandum of association (§ 17, 18 and 19), the sanctioning of shares issued at a discount (§ 79), granting an extension of time for filling of particulars or for registration of certain charges (§ 141), and the power to order a general shareholders meeting other than the annual meeting (§ 186).

[79] *Twenty-Second Annual Report, supra* n. 5 at 3.

[80] *Id.*, at 105–106.

[81] Companies Act, § 294(A).

[82] *Twenty-Second Annual Report, supra* n. 5 at 61–62.

[83] Companies Act, § 295.

[84] *Twenty-Second Annual Report, supra* n. 5 at 63.

[85] Companies Act, § 297 (1).

[86] *Twenty-Second Annual Report, supra* n. 5 at 63.

[87] Companies Act §§ 108A, 108B and 108C.

[88] *Id.*, § 205A (3).

[89] *Id.*, § 211.

[90] A security is defined under the Act as any share, stock, bond, debenture, mortgage deed, instrument of power, pledge of hypothecation, any other instruments creating or evidencing a charge or lien on the assets of the company, instruments acknowledging loan to or indebtedness of the company and guaranteed by a third party or entered into jointly with a third party. Capital Issues (Control) Act § 2 (1) (e).

[91] The Capital Issues (Control) Act of 1947, § 3 (2) [hereinafter cited as Capital Issues Act].

[92] *Id.*, § 3 (1).

[93] Bombay Stock Exchange, Capital Issues Control (1978) at 1 [hereinafter cited as Capital Issues Control]; interview with A.V. Ganesa, Comptroller of Capital Issues, and M.R. Miya, Joint Director (Stock Exchange) Office of the Comptroller of Capital Issues (New Delhi, November 17, 1978, and December 7, 1978).

[94] The Capital Issues (Exemption) Order, 1969, amended up to April 1, 1976, Clause 4(i) [hereinafter cited as Exemption Order].

[95] *Id.*, Clause 4(ii).

[96] *Id.*, Clause 4(vi).

[97] *Id.*, Clause 4(ix) (b).

[98] *Id.*, Clause 5.

[99] *Id.*, Clause 3.

[100] Capital Issues Control, *supra* n. 93 at 17.

[101] *Id.* at 28.

- [102] The Capital Issues (Application for Consent) Rules, 1966, Schedule A.
- [103] Capital Issues Control. *supra*, n. 93 at 17.
- [104] Exemption Order, *supra* n. 94, Clause 8(ii).
- [105] Capital Issues Act, § 3 (4).
- [106] Capital Issues Control, *supra* n. 93 at 16.
- [107] Capital Issues Act, § 13.
- [108] Capital Issues Control, *supra* n. 93 at 16–17.
- [109] *Id.* at 17.
- [110] *Twenty-Second Annual Report*, *supra* n. 5 at 37. Unless otherwise noted, all figures pertain to fiscal year ending March 31, 1978, the latest year for which figures are available.
- [111] *Id.*
- [112] *Id.* at 33–34.
- [113] *Id.* at 34.
- [114] *Id.* at 38.
- [115] *Id.* at 42.
- [116] Item 48 of the Union List.
- [117] Securities Regulation Act, § §13 and 23 (1) (b).
- [118] *Id.*, § 14 (1).
- [119] *Id.*, § 19.
- [120] *Id.*, § §3 and 4.
- [121] *Id.*, § 3 (2).
- [122] *Id.*, § 4 (1) (a).
- [123] *Id.*, § 4 (2).
- [124] *Id.*, § 4 (1) (b).
- [125] History, Regulation and Organization, *supra* n. 22 at 6.
- [126] Securities Regulation Act § §6 (1) and 7.
- [127] *Id.*, § 6 (2).
- [128] *Id.*, § 6 (3).
- [129] *Id.*, § 6 (4).
- [130] *Id.*, § 7 (A) (2).
- [131] *Id.*, § 8.
- [132] *Id.*, § 11.
- [133] *Id.*, § 12.
- [134] *Id.*, § 11.
- [135] *Id.*, § 16.
- [136] *Id.*, § 21.
- [137] Poser and Silver, Regulation of the Indian Stock Market: A Preliminary Survey, at 58 (1965) (unpublished report prepared for the United States Agency for International Development) [hereinafter cited as Regulation of the Indian Stock Market: A Preliminary Survey].
- [138] Securities Regulation Rules, Rule 8.
- [139] *Id.*, Rule 8 (1) (a), (b), (c) and (e).
- [140] *Id.*, Rule 8 (4).
- [141] *Id.*, Rule 8 (3) (f).
- [142] *Id.*, Rule 19.
- [143] *Id.*, Rule 19 (1) (a)–(d).
- [144] Rules 19 (n) (g)–(h) of the Companies Act provide that the following shall be supplied to the exchanges:

certified copies of agreements or other documents relating to arrangements with or between:

- (i) vendors and/or promoters;
- (ii) underwriters and sub-underwriters;

(iii) brokers and sub-brokers.

and

a certified copy of every letter, report, balance sheet, valuation, contract, court order, or other document, part of which is reproduced or referred to in any prospectus, offer for sale, circular or advertisement offering securities for subscription or sale, during the last five years.

[145] *Id.*, Rule 19 (3) (j) and (p).

[146] *Id.*, Rule 19 (3) (h).

[147] *Id.*, Rule 19 (3) (n).

[148] *Id.*, Rule 19 (5).

[149] Interview with M.R. Miya, *supra* n. 93.

[150] Interview with officers of the Calcutta Stock Exchange, S.L. Bardhan, President; Dr. B.B. Ghosh, Executive Director; B.H. Khandelwal, Vice President; B. Majumdar, Secretary; and P.K. De, Deputy Secretary (Calcutta, November 20–21, 1978).

[151] Interview with officials of the Delhi Stock Exchange, H.C. Verma, Executive Director, and Behari Lal Chowdhary, President (Delhi, November 16, 1978).

[152] *Id.*

[153] Interview with A.V. Ganesa, *supra* n. 93.

[154] Capital Issues Control Act, § 7.

[155] *Id.*, § 8.

[156] *Id.*, § 13 (1).

[157] *Id.*, § 13 (2).

[158] *Id.*, § 15.

[159] Securities Regulation Act, § 6 (2).

[160] *Id.*, § 6 (3).

[161] *Id.*, § 6 (3) (b) and 6 (4). Rule 16b of the Securities Regulation Rules prescribes the manner in which such inquiries are to be undertaken.

[162] *Id.*, § 23.

[163] *Id.*, § 24 (1).

[164] *Id.*, § 24 (2).

[165] Securities Regulation Rules, Rule 11.

[166] Interview with A.V. Ganesa, *supra* n. 93.

[167] *Bye-Laws and Regulations of the Delhi Stock Exchange*, at 90–96.

[168] *Id.*, at 90.

[169] Interview with S.A. Shah, partner in Stewart & Co., Calcutta share broker (Calcutta, November 21, 1978). Mr. Shah also stated that the books and records of his 80-year old firm had never been examined by any government agency.

[170] Interview with officers of the Calcutta Stock Exchange, *supra* n. 150.

[171] *Id.*

[172] The Madras Stock Exchange, which requires a Rs. 10,000 deposit per member, would impose a one rupee deposit per share for each two rupees in price fluctuation caused by the purchase of a large block of stock. Interview with officials of the Madras Stock Exchange, E.R. Krishnamurti, Executive Director; V.K. Sundaram, President; and S. Narayanswami, past President (Madras, December 4, 1978).

[173] Interview with officials of the Delhi Stock Exchange, *supra* n. 151.

[174] Companies Act § 234 (1)–(3A).

[175] *Id.*, § 234 (7).

[176] Ramaya, A Guide to the Companies Act 405 (1971).

[177] Companies Act § 234 (4). See *Coimbatore Spinning & Weaving Mills Ltd. v. M.S.*

Scrīnivasan, (1969) Comp. Cas. 97, A.I.R. 1959 Mad. 229, for a detailed discussion of the powers of the registrar under §234 of the Companies Act.

[178] Companies Act, §234-A.

[179] Interview with J.K. Hajra, Deputy Director Inspection, Regional Directors Office (Calcutta, November 23, 1978).

[180] Companies Act, §235 (c).

[181] *Id.*, §234 (b). The Board may also utilize a seldom used provision of the Companies Act (§247) and appoint an inspector to investigate and determine the true persons who are or have been financially interested in the success or failure of the company and who are or have been able to control or materially influence the policies of the company. Such an investigation may be instituted merely because it appears to the Board that there is good reason to do so. Where the Board determines it is unnecessary to appoint an inspector to determine ownership and influence of individuals, it may request such information directly from the company. See Companies Act, §148.

[182] *Id.*, §237 (a).

[183] For year ending March 31, 1978, the Board exercised its discretion and ordered investigations in 32 of the 45 cases considered. *The Twenty-Second Annual Report, supra* n. 5 at 71.

[184] The names of companies under investigation are published in the annual reports on the workings and administration of the Companies Act.

[185] Fifteen writ petitions were filed in the various High Courts for year ending March 31, 1978, seeking to enjoin investigations. *Twenty-Second Annual Report, supra* n. 5 at 71-72.

[186] *Barium Chemical Ltd. v. Company Law Board*, A.I.R. 1966 S.C. 295, 36 Comp. Cas. 639.

[187] *Sahu Jain Ltd.*, (1969) 1 Comp. L.J. 213, 73 C.W.N. 446, 40 Comp. Cas. 83.

[188] Interview with J.P. Mukherjee, Regional Director, Company Law Board (Calcutta, November 23, 1978).

[189] Companies Act §238.

[190] A Guide to the Companies Act, *supra* n. 176 at 409.

[191] Companies Act, §239.

[192] *Id.*, §239 (d).

[193] Interviews with Hajra, *supra* n. 179 and Mukherjee, *supra* n. 188.

[194] Officers and agents of the company under investigation are specifically required "to give to the inspector all assistance in connection with the investigation which they are reasonably able to give". Companies Act §240 (1) (b).

[195] Companies Act §240 (3); *Re Gaumont British Picture Corporation*, (1980) 2 All.E.R. 415.

[196] Companies Act, §240-A. The right to search for and seize books and records under the Companies Act is coordinated with procedures outlined under the Code of Criminal Procedure of 1898 §103, which provides that:

(a) at least two respectable witnesses of the locality shall be asked to be present; (b) the search shall be conducted in their presence and the list of things seized should be signed by the witnesses; (c) the occupant of the place or his representative shall be allowed to attend during the search and a copy of the seizure list signed by the witnesses shall be given to him and (d) when any person in or about such places is reasonably suspected of concealing about his person any article for which search is being made such person may be searched under §102 (3) of the Code of Criminal Procedure, 1898, and a copy of the list of things taken possession of shall be given to him.

[197] Article 20 (3) states that "no person accused of any offence shall be compelled to be a witness against himself".

[198] *Raja Narayanlal Bansilal v. Maneck Phiroz Mistry, et al.*, A.I.R. 1961 S.C. 29 at 90.

[199] *Id.*, at 39.

[200] Interview with Mukherjee, *supra* n. 188.

[201] Companies Act, §241.

[202] *Id.*, §236.

[203] *Id.*, §242; interview with Mukherjee, *supra* n. 188.

[204] Interview with Mukherjee, *supra* n. 188.

[205] Companies Act §233. The Board also has the option under §§247 and 248 to freeze the transfer and voting rights of an individual in a company for a period up to three years while it ascertains the true ownership of such shares and the influence such individuals exercise over the affairs of the company. *See* Companies Act, §250.

[206] Interview with M.K. Kukreja, Joint Secretary in the Department of Company Affairs, member of the Board, and Secretary to the Sachar Committee (Delhi, November 17, 1978); interview with A. Neelakatan, Joint Secretary, member of the Board, and Chief of the Inspection Wing in the Department of Company Affairs (Delhi, November 17, 1978).

[207] *Sachar Committee Report*, *supra* n. 36 at 148.

[208] *Id.*

[209] *Id.*, at 149–178.

[210] *Id.*, at 149.

[211] *Id.*, at 150.

[212] Prosecutions for such defaults were brought under the following sections of the Companies Act: 159, 162, 165 (9), 166, 168, 209, 210 (5), 220 (3), 551 and 614A. *Twenty-Second Annual Report*, *supra* n. 5 at 74–75.

[213] Interview with Neelakatan, *supra* n. 206.

[214] The penalty for failing to file an annual report with the registrar as required under §159 is Rs. 50 per day.

[215] *Sachar Committee Report*, *supra* n. 36 at 150–151.

[216] Under the SEC's delinquent filing program, priorities have been established so that action is first taken against New York Stock Exchange listed companies, other exchange listed companies, NASDAQ listed companies, high volume over-the-counter traded companies and, lastly, thinly traded over-the-counter traded companies.

[217] Companies Act, §62.

[218] Interview with B.P. Ray, senior partner in the Calcutta law firm of Orr, Dignam & Co. (Calcutta, November 23, 1978).

[219] Compare with the "reasonable grounds to believe" after "reasonable investigation" standard under Section 11 (b) (3) of the Securities Act of 1933.

[220] Interview with J.P. Thacker, *supra* n. 72.

[221] Two Supreme Court and two High Court justices stated that they were not aware of any private civil court actions involving a false prospectus, manipulation of the market, or insider trading. Interviews with Chief Justice B.P. Sinha (retired), Supreme Court of India (Punjab, November 8–11, 1978); Justice Kalasam, Supreme Court of India (Delhi, December 8, 1978); Chief Justice Ramprasad, Tamil Nadu High Court (Madras, December 5, 1978) and Justice S. Mohan, Tamil Nadu High Court (Madras, December 5, 1978).

[222] As Hindus, the great majority of Indians accept misfortunes as being part of their destiny or karma.

[223] Interview with Lalit Bhasin of the New Delhi law firm of Bhasin and Bhasin (December 7, 1978).

[224] Interview with Bhupendra C. Dalal, majority partner, Bhupendra Chamapklal Davidas (Bombay, November 27–28, 1978).

[225] No separate regulations control investment advisors.

[226] On the Bombay, Calcutta and Delhi exchanges, stocks are generally traded at specific

floor locations. When activity is slow, transactions may be consummated wherever the taravniwalla happens to be. On the Bombay exchange, where activity seems always to be brisk, many times involving physical contact, the taravniwallas stand on raised ledges with one arm looped around a large leather strap rivetted to the wall behind them. This prevents them from being pulled into the crowd of anxious bidding brokers below. Should a taravniwalla step down into the crowd, he is subject to having his head forcibly turned one way and another by brokers attempting to get his attention. Although loud yelling appears to be a necessary ingredient in trading on most exchanges, it is doubtful the Indians can be outdone in this respect.

[227] *Cf.* Rules of the New York Stock Exchange, Rule 104:

No specialist shall effect on the Exchange purchases or sales of any security in which such specialist is registered, for any account in which he, his member organization or any other member, allied member, or approved person, in such organization or officer or employee thereof is directly interested, unless such dealings are reasonably necessary to permit such specialist to maintain a fair and orderly market, or to act as an oddlot dealer in such security.

[228] One commentary has likened taravniwallas to parasites:

Some members, so-called brokers and miscalled jobbers, carry on what is known as tarawaniwalas business which is entirely of a parasitic nature. They rush in to buy or sell according as they find bonafide brokers trying to execute buying or selling orders. Their operations necessarily result in price movements almost always to the detriment of clients' buying or selling. These tarawaniwalas hardly keep any outstanding business overnight and they continuously go on buying and selling at a small range of fluctuations. Their actions are nothing but gambling in differences. This leads to consequent overtrading which at times has resulted in disaster and crisis. Garg, *supra* n. 24 at 160.

[229] Bye-Laws of the Delhi and Madras Stock Exchanges, Appendix A to Regulation 14 (Regulation 14.1), Official Scale of Brokerage.

[230] The *Gorwala Committee* stated in its report:

There is an unfortunate tendency to continuously reducing scales of brokerage in order to obtain large speculative business. Reasonable scales of brokerage are essential both for enabling efficient service to be given to the public and for the maintenance of proper standards among members of the stock exchange. Reduction by individual members below the minimum to attract business merits the severe displeasure of the governing authorities.

Regulation of the Indian Stock Market: A Preliminary Survey, *supra* n. 137 at 20.

[231] It is estimated that 90 percent of trading is done by brokers speculating for their own or, to a limited extent, their customers' accounts. *See id.* at 11.

[232] Minimum brokerage commissions were eliminated as late as 1975 in the United States.

[233] Gill, *Securities Commissions as Developmental Agencies*, paper presented at the Third Inter-American Conference of the Securities Commissions of America, Buenos Aires, Argentina (1977).

[234] The Madras Exchange subsidizes 50 percent of the tuition costs of this course. Interview with officials of the Madras Stock Exchange, *supra* n. 172.

[235] Interview with officials of the Bombay Stock Exchange (Bombay, Nov. 26–30, 1978).

[236] To some extent certain measures have already been taken. An investor is presently permitted to deduct from taxable income 50 percent (up to Rs. 10,000) of his purchase of

shares in newly underwritten companies. Also, up to Rs. 150,000 of investments in newly underwritten companies are exempt from the wealth tax. Dividends of new companies are exempt from income tax for a number of years. And, the capital gains holding period has been reduced from five to three years; however, if the entire proceeds from the sale of stock is used to purchase shares of a new company, or units of the Unit Trust of India or bank deposits, then no capital gains tax is imposed.

[237] Interview with James S. Raj, nonexecutive Chairman, Industrial Credit and Investment Corporation of India (Bombay, November 29, 1978).

[238] *Twenty-Second Annual Report*, *supra* n. 5 at 24.

[239] It has been suggested that forcing a government company to go public would create a positive control mechanism whereby company officials for the first time would be accountable to shareholders. Interview with James S. Raj, *supra* n. 237.

[240] *Twenty-Second Annual Report*, *supra* no. 5 at 42.

[241] Special Study of Securities Markets, H.R. Doc. No. 95, pt. 4, 88th Cong., 1st Sess. 694 (1963).

[242] Compare with the Soundness Rule in Japan which avoids the need of proving that the purpose of the defendant in engaging in certain securities transactions was to manipulate the market:

a series of sales or purchases or entrustment thereof which is likely to create an artificial market price deviating from the actual market, or the act of being entrusted with a series of sales or purchases with the knowledge that an artificial market price deviating from the actual market is likely to be created.

Securities Exchange Law, 1948, Art. 1, Item 3, *cited in* Tatsuta, *Securities Regulation in Japan* (1970) at 87–88.

[243] Poser, *Securities Regulation in Developing Countries: The Brazilian Experience*, 52 Va. L. Rev. 1283 (1966) at 1297.

Robert C. Rosen (b. 1945) is a graduate of the University of Minnesota (B.S. 1967), Duquesne University School of Law (J.D. 1970), and Harvard Law School (LL.M. 1979). He was a research fellow at the Fletcher School of Law and Diplomacy and an Assistant Attorney General in the Justice Department of the Commonwealth of Pennsylvania. Mr. Rosen joined the Securities and Exchange Commission in 1973 as a trial attorney. He is presently an attorney in the Commission's Washington Regional office. He is a member of the Pennsylvania, District of Columbia, and California Bars and is the author of *Law and Population Growth in Jamaica*, Monograph Series No. 10 (The Fletcher School of Law and Diplomacy, Tufts University, Medford, Massachusetts, 1973).

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