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Role of Regulatory Bodies in India

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ABSTRACT

The paper covers the various real life scenarios faced by the investors who had invested in the financial products without understanding the risk and return profile of the product. The paper has covered in detail the recent scams that have affected the Indian capital market. The role of various regulatory bodies has also been discussed in detail. There is many a time over lap of regulations which affect the trust of the investors as ultimately they are not guided. The paper also covers the important incidents like misspelling in ULIP, NSEL scam and other current updates which would make the reader more aware about the working of the securities market.

Introduction

The word "Regulatory Bodies" has become the buzz word with the economy and the politics grappling with the new and complicated laws being enacted by the various regulatory bodies in the country. One has to accept that "No regulation" would mean utter chaos like what happened in the NSEL matter where there was clear "Regulatory Vacuum" and this led to the investors losing Rs. 5500 crores. At the global level also the "Sub Prime Crises" which shook the USA's financial system andultimately led the world into recession is yet another example where the regulations were not properly implemented and this led to exploitation of the loop holes into the system. There is a thin line between too much of regulation and very loosely regulated markets, either of them are dangerous for the financial system and also for the overall economy. The paper tries to give an insight on the role of various regulatory bodies like the SEBI, IRDA and the various practical instances which have shook the economy and the financial system. The recent NSEL scam, the mutual funds industry debacle due to the removal of the entry load, mis-selling of ULIP which has killed the insurance industry has been covered in this paper.

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The paper also covers how the faith of the retail investors could not be brought back as the index is trading at all time high but the retail participation is at the lowest levels. This is really alarming and if corrective steps are not taken then we have just regulations but no investor left to be regulated. At times the regulations framed are with good intention but they tend to damage the working of the intermediaries who act as a bridge between the markets and the investors.

Current Scenario

The Indian Economy has been dealing with mixed Macro Economic data with some indicating that the worst may be over while others indicating that still pain would be there in the economy. The inflation numbers have come and the CPI inflation is has reached 10.09% which is very high. The food inflation has touched 12 % mark which clearly means that RBI would not be in a position to reduce the interest rates. The IIP index for September came at 2 % which is a positive surprise but still economy does not seem to be out of woods yet. The Exports were up 13.5% and Imports down 14.5% which resulted in the October Trade Deficit at $ 10.55 billion which was last year at $ 20.2 billion. This has caused some relief for the Current Account Deficit which is now being projected to be less than $ 60 billion. The Indian Economy at the grass root level is still grappled with non execution of the projects worth Rs 15 lakh crore of industrial projects stalled. The power sector which is the core to the industrial manufacturing has 136 projects worth Rs 7.14 lakh crore stalled.. The main reason for the projects to get stuck up is delay largely due to lack of clearances. The banking sector is also feeling the heat as the Gross NPA of banks have reached Rs. 1,36,970 crore (17.43% of total) from Rs. 12,190 crore (4.66% of total) at end of March 2009 intensifying pressure on banks. The money which has been advanced by the banks has got stuck and this leads to increasing of NPAs. This would put pressure on the whole financial system and economy which is already passing through very rough phase. The stock market is scaling new highs but the retail investor participation is at the lowest level. The US Fed tapering news creates jitters for the markets as there is fear that any unwinding by the US would lead to steep correction in the Indian Markets.

Sensex which is at 20,827 but with inflation adjusted it is real value is 13000. NSE Mid cap is 22% down and small cap is 58 % down. Another major factor affecting Foreign Investors could be FATCA (Foreign Accounts Tax Compliance Act) which aims to track

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down the investment made by US citizens in Indian markets. Foreign investors have invested over Rs 92,250 crore or USD 16.7 billion so far this year. This robust flow will be adversely impacted come January 1 when nearly 40% of the foreign flows will be governed by FATCA - Foreign Account Tax compliance Act. To put it simply, FATCA was enacted by the US government to track down offshore investments and earnings of any US citizen.

The FII (Foreign Institutional Investors) are dictating the markets as our own participation is at the lowest level.

Month (Rs.crore)	Net flows of FII
Jan	22,245
Feb	22,122
March	11,660
April	5,145
May	20,678
June	-10,530
July	- 5,909
August	- 6,200
September	13,158
October	18,013
November	1,843

Source:- Economic Times dated 13th November 2013

NSEL Fiasco

The recent National Spot Exchange Limited (NSEL) fiasco in which Rs. 5500 crores of 13000 investors have been trapped is the clear case of "Regulatory Vacuum" where the so called Spot Exchange was never regulated and it cheated the investors by launching T + 30 day contracts and it was sold as guaranteed product to the retrial investors. The money was actually borrowed by 24 companies out of which 19 have been declared as "defaulters" by the exchange. Most of these companies are shell companies which have paid up capital of Rs 1 lakh but they have borrowed amount worth Rs. 792 crores as in case of Mohan India, a company who had claimed to have sugar worth 1000 tonnes but actually no commodity was found when the raids were conducted. This shows that the warehouse receipts generated were also fake and the entire mechanism was based to cheat the retail investors. On July 15 2013, the Ministry of Food and Consumer affairs wrote a letter to the NSEL stating that they need to stop all the contracts on 31st July. This led to sudden payment crisis as the last lag of money which was in the system got stuck and never came out. In August when the news became public, it was really surprising that neither SEBI nor Ministry of Finance nor FMC was ready to

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take the charge of the situation. Then ultimately Government intervened and then put FMC (Forward Market Commission) which is a commodity regulator under the Ministry of Finance and gave it powers to ensure that the whole matter was sorted out. This shows that there was complete regulatory vacuum as how to control an entity which was private in nature but yet had the status of the Exchange.

Mutual fund Industry

The mutual fund industry has been ruined by SEBI diktat that no entry load would be charged to the investors. This has led to the scenario that Independent Financial Advisors who were the backbone of the industry getting thrown out of the business. This led to the investors not getting serviced and in the last three years more than 10 lakh folios got closed. This has led to financial advisors closing down their offices. The investors are deprived of their services which ultimately makes them redeem their investments since there is no one to guide them and service them. This leads to permanent loss of investors to the market.

ULIP Mis-selling

ULIP which is Unit Linked Insurance Plan was one of the hottest selling product of the insurance industry and also in the financial services segment. In this product, the agent'smis-sold the products by not disclosing the charges which were upto 30 % of the premium paid. The result was when the clients received their statement they would certainly be disappointed as their capital was eroded and as stock markets did not perform, obviously their return was also negative. The widely spread mis-selling followed by many complaints led to SEBI banning the sale of ULIP by insurance companies. This led to bitter battle between the IRDA and SEBI that who controls the insurance investors. Then ultimately FSDC(Financial Stability Development Council) which is a super regulator intervened and gave the insurance jurisdiction to IRDA. This again shows that two regulators fighting for the same set of investors yet the investors suffered huge losses. IRDA has then reduced the commission structure on ULIP products and increased the premium paying period from minimum of 3 years to 5 years. This killed the product and it has resulted into the industry losing faith of the investors. Currently the insurance industry is passing through the worst phase as the clients have lost faith in the insurance products. This has led to the severe loss to whole industry.

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Regulating Intermediaries

In April 2013 SEBI came with the guidelines to regulate the intermediaries, which are so complex that the advisors are shunning away from getting themselves registered. They rather prefer to work as independent advisors since they are able to get the commission and other remuneration from the fund houses.

Conclusion

Regulatory bodies play a vital role in ensuring that the faith of the investors is maintained in the markets. They presence and regulations ensure that no undue advantage is taken by anyone participant and that investor are not taken for a ride. Historically there have been scams where the retail investors have been cheated and they finally get out of the market. But at the same time, one needs to understand that sometimes regulations instead of helping the market participants and investors damage the market confidence. Regulatory bodies need to ensure that there is balance between protecting the investors' interest and at the same time one needs to ensure that market participants also get the level playing field. This would ensure that both the investors and market intermediaries are able to survive and make decent income from the market.

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