The Protection of Minority Investors and the Compensation of Their Losses: A Case Study of India

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ABSTRACT:

Any legal system may potentially deploy two separate but related models to ensure the accuracy of disclosure in the capital markets. First, it may possess legal institutions in the form of regulatory bodies with power to make regulations regarding disclosures and to enforce those regulations through powers of sanction conferred upon them. Second, it may adopt the model that relies upon the courts to grant remedies to investors who are victims of inaccurate or misleading disclosures thereby suffering losses.

This paper tests the efficacy of the two models in their application to India. The exploration of India is interesting and helpful because India’s capital markets have witnessed exponential growth in the last two decades. At first blush, it might be simple to attribute this to India’s legal system through civil liability and its enforcement through the judiciary. Counterintuitively, though, India’s common law legal system operating through the judiciary has not played a vital role in the development of the capital markets through a rigorous civil liability regime. Delays in proceedings due to alarming pendency levels in litigation before Indian courts and skyrocketing costs in initiating litigation are some of the factors that have disincentivized investors from relying upon the civil liability regime for enforcing their compensation claims.

At the same time, other factors have been at play. India’s capital markets regulator, the Securities and Exchange Board of India (SEBI) has been instrumental in formulating policies and regulations governing capital markets, and its actions have been rapid and dynamic to suit the needs of the changing markets, by operating through the power of sanctioning various market players.

The paper concludes with the finding that while the general approach in most common law markets is for courts to play a significant role in the development of the capital markets through the process of compensating investors for losses, the success of India’s capital markets growth has hinged upon the regulatory process rather than the courts.

Key words: minority investors, shareholder litigation, securities regulation, compensation of losses, India
I. INTRODUCTION

There exists a strong correlation between the level of protection conferred upon minority investors through the instrumentality of the law and the state of the equity capital markets in a given economy. More specifically, the role of the law and the legal system is to ensure parity of information through disclosures so that investors pay the right price to acquire securities, whether in the primary market or the secondary market. Viewed in this light, law acquires the status of an “information forcing” mechanism that compels issuer companies to make appropriate disclosures. Greater robustness in the legal system therefore leads to better quality of disclosure enabling issuers to raise capital from investors at a fair price.

The legal system may potentially deploy two separate but related models to ensure the accuracy of disclosures in the capital markets. First, the legal system may possess legal institutions in the form of regulatory bodies with powers to make regulations regarding disclosures and also to enforce those regulations through powers of sanction conferred upon them. In case of non-compliance with the disclosure regulations, the appropriate regulatory body would have the power to impose sanctions on the perpetrators so as to act as a preventive measure against non-compliance. Such a regulatory mechanism provides flexibility and adaptability as it is implemented by a country’s securities market regulator, which is not only intended to be independent but also possesses some level of domain

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3 Information-forcing rules are default rules that compel parties with superior information to divulge that information to other parties they deal with so that the problem of information asymmetry is obviated, or at least reduced. See Yair Listokin, Learning Through Policy Variation, 118 Yale L.J. 480, 501-02 (2008).

4 Although these two models are treated separately, there may potentially be some amount of overlap between the two in their impact on securities markets. In other words, the two models may even complement each other.

5 Black, supra note 2 at 1576-77.
expertise. Moreover, the focus of such a regulatory approach tends to target issuer companies and intermediaries involved in the capital markets so as to deter wrongdoing. The regulatory mechanism is aimed much less, if at all, at compensating investor losses, although deterring errant issuers and intermediaries will in any event indirectly benefit the investing community as well.

Second, the legal system may adopt a model that relies upon the courts to grant remedies to investors who are victims of inaccurate or misleading disclosures thereby suffering losses. This presupposes the existence of robust substantive laws to deal with misstatements by issuer companies, and also strong enforcement of the laws by the courts. The “legal origins” strain of literature posits that in common law countries the judiciary plays an important role in enforcing investor rights, thereby enhancing the value of capital markets. On the other hand, civil law countries tend to rely heavily on governmental intervention in regulating the capital markets. As the arbiter of disputes between investors and issuer companies, the courts perform the role of remedying the grievances of investors. More importantly, courts may (and do) impose civil liability on issuers, their directors and capital market intermediaries and award compensation to redress investor losses. In some countries, especially in developed markets in the common law world, the strong role of the judiciary is seen as key in ensuring liquid and vibrant capital markets.

In this paper, I test the efficacy of the two models discussed above in their application to one emerging economy, viz. India. The exploration of the Indian capital markets is both interesting and helpful because they have witnessed exponential growth in the last two decades since the liberalization of India’s economy in 1991. The Indian capital markets have not only grown substantially in comparison with the prior period but the growth rates have been remarkable even

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6 Id. at 1577-78.
relative to several developed economies.\(^8\) By way of an example, in 2013 India’s National Stock Exchange ranked highest in terms of number of equity trades.\(^9\)

Moving on to the legal tools that may have facilitated such growth in India’s capital markets, it is simple at first blush to attribute the growth to India’s legal system through civil liability and its enforcement through the judiciary. This would be consistent with the “legal origins” notion of investor protection because India’s legal system is steeped in the common law heritage it obtained through centuries of British colonial rule.\(^10\) India not only has a sufficiently robust substantive law on investor protection, but the independent judicial system drawn from the common law tradition allows for judges to mold the law to suit specific circumstances. In other words, the system permits judge-made law as a method of reforming the legal system to adapt to the dynamic capital markets.

However, as I argue in this paper, the efficacy of India’s legal system as a tool for investor protection necessitates a more nuanced treatment. Counter-intuitively, India’s common law legal system operating through the judiciary has not played a vital role in the development of the capital markets through the imposition of civil liability upon issuer companies or the compensation of investors for losses due to misstatements. Despite the existence of substantial rules for civil liability and compensation and the presence of an elaborate court system, the associated conditions for the judiciary to create an impact on investor protection are conspicuous by their absence.\(^11\) The Indian court system is plagued by delays, costs, and other inefficiencies. Nearly 32 million cases are pending before different levels within the Indian judiciary thereby causing a significant strain on the

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\(^9\) *NSE top-ranked globally for equity trades for 2nd year in 2013*, The Economic Times (Jan. 19, 2014). However, the two leading Indian stock exchange do not rank very highly when measured against market capitalization.


system. Cases can on average take 15 years to achieve final outcomes. It is a classic scenario in which the considerably strong (and progressively strengthening) substantive laws on civil liability for securities law violations are overshadowed by inefficiencies in the enforcement of the laws. For this reason, civil liability and compensation of investors’ losses have almost never been utilized to any meaningful extent in the Indian markets as a tool to strengthening the capital markets.

To my knowledge, there is no single instance in recent decades of an issuer company having been ordered by an Indian court to pay a significant amount in compensation to investors for incorrect or misleading disclosures. This can be amply illustrated by contrasting results that ensued in a high-profile corporate governance and disclosure failure that occurred in 2009 in Satyam Computer Services Limited, a leading player in the information technology sector. The chairman of Satyam confessed to having falsified the financial statements of the company, including by showing fictitious cash assets of over US$ 1 billion on its books. Consequently, the stock price of the company fell sharply, thereby causing significant losses to its investors. The company was dual-listed, with its equity shares being listed on Indian stock exchanges and its American depository receipts (ADRs) on the NYSE. Class actions were promptly initiated in the United States (U.S.) courts against Satyam as well as its auditors Pricewaterhouse-Coopers (PwC) on behalf of affected ADR-holders. In 2011, Satyam settled the action against it by agreeing to pay U.S.$ 125 million to the plaintiffs, while PwC settled the action against it by agreeing to pay U.S.$ 25.5 million. In stark contrast to these settlements where plaintiff shareholders were successful in recovering some of their losses, there was no payout whatsoever to Indian shareholders who suffered

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similar losses. Although an Indian investor association initiated a claim before the Supreme Court of India on behalf of affected Indian shareholders, the claim was not sustained in the court. This anecdotal evidence presents the glaring differences in the use of the judicial system for investor protection in the U.S. and in India.

This situation presents an important puzzle. If the Indian court system is hardly attuned to the use of the customary common law method of imposing civil liability on errant companies and compensating losses of affected investors, how have the Indian capital markets witnessed significant growth in recent years? This raises grave doubts about the applicability of the “legal origins” thesis to the Indian capital markets. Surely, there may be other factors at play. This leaves us with one explanation that the growth of the capital markets has been attributable to the role of the securities regulator and subsidiary legislation promulgated by it in the form of regulations that govern the capital markets. The Securities and Exchange Board of India (SEBI), which formally received statutory recognition in 1992, has been instrumental in formulating policies and regulations governing the capital markets. Its actions have been rapid and dynamic to suit the changing needs of the markets. It has operated through the power of sanctioning various market players by applying the principle of deterrence.

While the general approach in most common law markets is for courts to play a significant role in the development of capital markets through the process of compensating investors for losses, the success of India’s capital markets growth has hinged upon the regulatory process rather than the courts, thereby deviating from the general approach adopted by common law systems. At the same time, as I detail later in this paper, recent legislative developments in India seek to

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17 SEBI derives its statutory powers from the Securities and Exchange Board of India Act, 1992. Under that legislation, SEBI is empowered to promulgate various regulations pertaining to the capital markets and also to take appropriate action in the interests of investors and the capital markets.
18 These findings are broadly consistent with an earlier work that examined the growth of financial markets in India in general (including both equity and debt). Armour & Lele, supra note 10.
embolden the ability of investors to initiate class actions to recoup their losses.\(^{19}\) Although it is reasonable to predict that the balance in the future will tilt somewhat towards greater impact of the court system on the state of the capital markets, there is no cause for great optimism on this count unless deeper issues relating to India’s justice delivery system are addressed in a more overarching fashion.

Part II of this paper tracks the recent evolution and growth of India’s capital markets and the capital structure of publicly listed Indian companies. Part III discusses the role of securities regulation in the markets and comments upon the role, powers and functions of SEBI, which has been instrumental in the development of the capital markets. Part IV analyzes the nature and extent of shareholder litigation in India, and identifies factors due to which there is a complete absence of mechanisms to motivate shareholders to successfully claim compensation for losses due to misstatements and wrongful disclosures by issuer companies. It also focuses on recent legislative developments that may favor shareholder litigation as a tool for investor protection, more so than in the past. Part V concludes.

II. INDIA’S CAPITAL MARKETS

A. Phases in Capital Market Development

Since its independence in 1947, India’s capital markets have witnessed two eras. The first is the pre-1991 era, during which the focus was predominantly on the manufacturing sector. The then prevalent license-raj and industrial capacity quota system ensured that only a few businesses thrived.\(^{20}\) This led to the growth of certain business families and industrial groups (largely to the exclusion of others) that held large chunks of capital in even publicly listed companies. Finance

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\(^{19}\) The recently enacted Companies Act, 2013 (which substitutes the pre-existing Companies Act, 1956) is expected to come into force in phases, with a few provisions already having taken effect. Among other things, this legislation includes a statutory class action mechanism for shareholders.

was essentially available only through banking channels (as opposed to the capital markets). The banks and development financial institutions took up large shareholdings in companies and also nominated directors on boards of such companies. During this era, due to concentrated ownership of shares, the controlling shareholders, which were primarily business families or the state, continued to exert great influence over companies at the cost of minority shareholders. Governance structures were opaque as financial disclosure norms were poor.

Signs of change, however, rapidly emerged with the 1991 reforms through economic liberalization that led to a new era in the Indian capital markets. After its establishment in 1992, SEBI rapidly began ushering in securities market reforms that gradually led to the exponential growth of the capital markets. The post-liberalization era also witnessed the emergence of the information technology and knowledge-based sector in India that depends heavily (and sometimes solely) on the equity capital markets for external finance as compared to the manufacturing sector that relies substantially on debt finance. These developments catapulted India onto the global arena in the last couple of decades, thereby earning it a place in an elite group of emerging economies.

B. Current State of the Capital Markets in India

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22 This was also fuelled by the introduction of the derivatives (futures and options) segment. Allen, Chakrabarti & De, supra note 8.


24 Brazil, Russia, India and China (BRICs) are leading emerging economies as their present growth trajectory is expected to put them amongst the world largest economies within a few years. Goldman Sachs, Global Economics Paper No. 99, Dreaming With BRICs: The Path to 2050 (2003), available at http://www2.goldmansachs.com/ideas/brics/book/99-dreaming.pdf. This group has since been joined by South Africa, to make it the “BRICS”.

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India’s capital markets have directly benefited from India’s explosive economic growth since liberalization. This has been aided by the inflow of foreign investment as various sectors of the economy were opened up.\textsuperscript{25} As of March 2013, the total market capitalization of Indian companies was around Indian Rupees 63,878 billion (U.S.$ 1,174 billion).\textsuperscript{26} This compares to a market capitalization of U.S.$ 15.22 billion on the NYSE Euronext for the relevant time.\textsuperscript{27} Over the years, there has also been a significant increase in trading volumes in Indian stocks. They went up from Indian Rupees 9,689 billion (U.S.$ 203 billion) in FY 2003 to Indian Rupees 32,571 billion in FY 2013.\textsuperscript{28}

The intensity of activity on a stock exchange is measured by the number of trades on the exchange, where the National Stock Exchange of India Limited (NSE) has been the world leader for the last two years. Its performance relative to its peers on this count is set out below:\textsuperscript{29}

\begin{table}[h]
\centering
\begin{tabular}{|l|c|c|c|}
\hline
Exchange & End December 2011 & End December 2012 & End September 2013 \\
\hline
NSE & 1,384,112 & 1,406,498 & 1,102,896 \\
NYSE Euronext (US) & 1,994,898 & 1,374,539 & 894,235 \\
Korea Exchange & 1,191,124 & 1,218,992 & 800,713 \\
Shanghai Stock Exchange & 1,273,277 & 925,550 & 860,876 \\
Shenzhen SE & 1,030,324 & 935,565 & 949,662 \\
\hline
\end{tabular}
\caption{Total Number of Trades in Equity Shares (year to date, in thousands)}
\end{table}

\textsuperscript{25} Inflow of funds into the stock markets has been primarily through foreign institutional investors (FIIs), which have been recognised as a separate category of portfolio investors under the relevant Indian laws and regulations.

\textsuperscript{26} This is based on the market capitalization on the Bombay Stock Exchange (which can be taken as a proxy for the all-India market capitalization). National Stock Exchange of India Limited, \textit{Macroeconomic Development and Securities Markets} 19, available at http://www.nseindia.com/research/dynaContent/ismr.htm [\textit{Macroeconomic Development and Securities Markets}].


\textsuperscript{28} National Stock Exchange of India Limited, \textit{Macroeconomic Development and Securities Markets}, supra note 26 at 19.

\textsuperscript{29} This data has been extracted from National Stock Exchange of India Limited, \textit{Capital Market} 61, available at http://www.nseindia.com/research/dynaContent/ismr.htm [\textit{Capital Market}].
The depth of the capital markets is measured as a ratio of the market capitalization compared to the gross domestic product (GDP) of the country. In India’s case, this ratio stood at 68.6% at the end of 2012, which is comparable with other emerging markets, but lower than leading developed markets. The number of companies listed on India stock exchanges is quite high. As of December 2013, 5,294 companies were listed on the BSE while 1,638 companies were listed on the NSE.

It is also the case that the capital markets are skewed heavily in favour of equity rather than debt. While in the developed economies the market for corporate bonds is closer in size to the equity market, in India the corporate bond market lags substantially behind the equity markets. For example, the ratio of the corporate bond market to GDP is a miniscule 4%. While the regulators in India have sought to introduce a number of reforms to boost the corporate bond markets, their efforts have not been successful, largely due to various underlying factors including difficulties in enforcing contracts and the lack of a robust framework for corporate insolvency in India.

C. Corporate Ownership Pattern & Concentration of Shareholdings

The data available across various parameters present the existence of significant capital markets activity in India, primarily on the equities side, which has been progressively increasing. The Indian stock exchanges are among the leading ones in the world. However, the stock markets in India are representative of a phenomenon that is common to most of the world (apart from the U.S. and the


31 These numbers for the two exchanges are not to be considered cumulatively as some companies may be listed on both, thereby causing some overlap.


United Kingdom (U.K.), which is the concentration of shareholdings even in publicly listed companies. Most public companies are controlled (by virtue of dominant shareholding) by either business families or the state. Business families predominantly own and control companies (even those that are listed on stock exchanges). In addition, it is quite common to find state-owned firms as well. Several listed companies are also majority owned by multinational companies. However, diffused ownership (in the sense of the Berle and Means corporation) can be found only in a handful of Indian listed companies, where such structures exist more as a matter of exception rather than the rule.

Examining the ownership aspect empirically, it was found in 2002 that “the average shareholding of promoters in all Indian companies was as high as 48.1%.” A later study confirms this position, even in the case of listed companies. A more recent study “tracks the movements in corporate ownership in India among its top companies in the first decade of the new millennium and moving forward in to the second”. It finds that over the period of the study from 2001 to 2011, controlling shareholders have further entrenched themselves in companies by substantially increasing their shareholdings, especially in larger companies while strengthening their already significant holdings in smaller companies. Moreover, retail non-institutional shareholding has been giving way to greater institutional shareholding.

There is more to it than absolute ownership percentages. The power of concentrated ownership is bolstered by controlling shareholders through other

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36 Chakrabarti, supra note 35, at 11 [emphasis supplied]. In this context, the expression “promoter” is used in India to mean a controlling shareholder.


39 Id. at 31.

40 Id. at 32.
mechanisms such as cross-holdings, pyramid structures and tunneling. These phenomena “mark the Indian corporate landscape.” They often lead to greater benefits to the controlling shareholders at the cost of the minority shareholders. Such practices can also have an adverse effect on the development of capital markets as minority shareholders are considerably exposed to the actions of controlling shareholders. All these are evidence of ownership concentration in Indian listed companies, with significant powers to the controlling shareholders. The general assumption is that the growth of the capital markets and greater liquidity will give rise to diffusion in shareholding in listed companies. But, that assumption has not received any support through empirical evidence in the Indian context, as discussed above.

In essence, India represents the story of rapidly growing capital markets with two world-class stock exchanges. The expansion, however, has been largely on the equities side, with the corporate bond market lagging considerably behind (leaving scope for much improvement). Despite the expansion of the capital markets, concentration of shareholding in public listed companies continues to be the order of the day (with some honorable exceptions), thereby providing substantial power to the controlling shareholders, arguably putting the minority shareholder interests at some risk.

With this background, I now proceed to deal with the various legal and regulatory tools available in India to protect minority investors, particularly against issuers companies and controlling shareholders for misstatements in

41 For an introductory discussion of these concepts, see, See, LaPorta, Rafael, Florencio Lopez-de-Silanes & Andrei Shleifer, Corporate Ownership Around the World, 54 J. FIN. 471, 474 (1999).

42 Chakrabarti, supra note 35, at 1. See also, Bertrand, P. Mehta & S. Mullainathan, Ferreting Out Tunneling: An Application to Indian Business Groups, 117(1) QUARTERLY JOURNAL OF ECONOMICS 121, 126 (2002), observing the concept of cross-holdings in Indian family business groups.

43 Chakrabarti, supra note 35, at 12.


45 See, supra notes 38-40, and a accompanying text.
prospectuses or other disclosures made by them to the markets, which may have affected the interests of minority investors.

III. SECURITIES REGULATION AND INDIA'S CAPITAL MARKETS

The rapid advancement of securities regulation in India as also the constantly expanding role and powers of SEBI as the securities regulator have both contributed substantially to the development of India's capital markets. My goal in this Part is to analyze the securities regulation and its enforcement by SEBI with a view to determining its impact on the capital markets.

A. Securities Regulation; Disclosure Norms

Prior to 1992, India followed the merit-based regulation of securities offerings. Companies intending to offer securities to the public were required to obtain the approval of the Controller of Capital Issues, a government body, which would specifically approve each public offering and its terms, including the price at which shares were to be offered. There was complete governmental oversight of the capital markets. Due to the somewhat excessive stringency in accessing the capital markets, public offering of shares by Indian companies was not that prevalent.

Since the assumption of regulatory responsibilities by SEBI in 1992, there was a move towards a more disclosure-based regulation of public offerings of securities by Indian companies. SEBI's role as the regulator has been to ensure accurate and timely disclosures to the markets, on the basis of which investors are free to invest in securities of Indian companies. The regulatory oversight over the terms of the offerings diminished over time when in the mid-to-late 1990s there

46 Merit regulation involves a review by a securities regulator of the quality and suitability of the offering of securities by a company within the jurisdiction of the regulator. See, Ronald J. Colombo, Merit Regulation Via the Suitability Rules, 12 J. INT'L BUS. & L. 1, 7 (2013).


48 Upon the establishment of SEBI, the office of the Controller of Capital Issues was abolished. ARVIND PANAGARIYA, INDIA: THE EMERGING GIANT 242 (2008).
was a complete shift from fixed-price offerings to book-built offerings. Under this regime, companies are free to invite bids from investors within certain indicative limits on the basis of a draft prospectus that contains all the necessary disclosures. Pricing through regulatory intervention gave way to a market-based price discovery process. This enabled companies since the mid-to-late 1990s to raises billions of dollars in capital through public offering of shares and accompanied listings through a disclosure-based regime where pricing was based purely upon factors of demand and supply. These factors triggered a dramatic shift in the Indian capital markets, particularly on the primary-markets front.

SEBI’s emphasis on disclosure-based regulation has witnessed a proliferation of disclosure norms for various types of capital raising activities by Indian companies. Over the last two decades, SEBI has gradually expanded the disclosure norms and prospectus requirements, culminating in the presently applicable SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 (the ICDR Regulations). The ICDR Regulations contain detailed disclosure requirements to be complied with by companies undertaking various types of securities offering. While the disclosure requirements pertaining to public offerings are quite extensive, they are somewhat limited in the case of rights offerings and

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50 For a brief description of the manner in which the bookbuilding process was to be carried out for the purpose of price discovery, see, S.S.S. Kumar, *Short and Long-run Performance of Bookbuilt IPOs in India* 20-21, available at http://dspace.iimk.ac.in/bitstream/2259/523/1/sssk.pdf.

51 It is also the case that “the Indian bookbuilding process is the most transparent in the world in that the bookbuilding activity is shown live on stock exchange website with updates every 30 minutes”. Arif Khurshed, Stefano Paleari, Alok Pande & Silvio Vismara, *IPO Certification: The Role of Grading and Transparent Books* 3, available at http://www.cass.city.ac.uk/_data/assets/pdf_file/0006/86640/Khurshed.pdf. This allows retail investors to make their bids with full knowledge of the nature of bids made by the better-informed institutional investors. Id. at 3-4.


53 SEBI issued a set of Disclosure and Investor Protection Guidelines in 1992, which was followed through with a number of clarifications issued over the years. In 2000, these were consolidated in the SEBI (Disclosure and Investor Protection) Guidelines, 2000.
the more targeted qualified institutional placements (QIPs). The ICDR Regulations are prescriptive and encompass disclosures pertaining to the business, risks, legal matters, capital structure and even the controlling shareholders and other entities within the group in which they hold shares.\textsuperscript{54} Moreover, the uses for the proceeds of the offering must be enumerated to the minutest detail. The requirements in the ICDR Regulations are so onerous that the disclosures required to give effect to a public offering in the Indian markets are comparable (or possibly even far exceed) those required in most developed markets. The trajectory followed by SEBI in the last two decades demonstrates the pivotal nature of disclosure as a tool for securities regulation in the primary markets.

At the same time, the existence of a stark disparity between the disclosure regimes governing the primary and secondary markets is somewhat puzzling. While a strong disclosure regime has been a boon to the primary markets, an equally weak disclosure regime in the secondary markets has been a malaise with far less continuing disclosure obligations on companies that are already listed on a stock exchange. The secondary market disclosures are governed through the listing agreement that listed companies are required to enter into with the stock exchanges where their securities are listed.\textsuperscript{55} While episodic disclosures are required to be made by companies upon the occurrence of material events that affect the price of their securities and periodic disclosures are to be made such as the announcement of quarterly results and decisions at board meetings, these requirements are considerably lighter than those prescribed for primary market transactions. Moreover, the regulations and liability regime for misstatements in secondary market disclosures are far from clear. Due to this disparity, there have been calls for the introduction of an integrated disclosure regime in India through standardizing and streamlining the corporate disclosures by integrating initial disclosures made under a primary market offering document with continuous

\textsuperscript{54} Just to obtain a flavor of the extensive (and possibly intrusive) nature of the disclosures, it may be noted that the ICDR Regulations even require the photograph and passport number of the controlling shareholders (in case they are individuals) to be included in the offering document!

\textsuperscript{55} SEBI has prescribed a standard format of the listing agreement.
disclosure requirements thereafter. Although SEBI has considered this issue based on the recommendations of a Sub-Committee appointed by it for the purpose, there is still a long way to go before the integration of the primary and secondary market disclosures in India. The latest step towards improving the enforcement of secondary market disclosures is by empowering the stock exchanges to take action against errant issuers.

B. The Regulatory Set-up: SEBI and the Stock Exchanges

The primary market disclosure requirements are enforced by SEBI, as the capital markets regulator. SEBI is managed by a board, which is presided over by a chairperson. Over the years, the Government has enhanced SEBI’s functional autonomy and also equipped it with greater powers. Although SEBI’s regulatory set up has aided it in spearheading capital market reforms in India, some concerns still remain about its autonomy, as key appointments are still subject to government control, and often overlaps with the jurisdiction of related regulators have required remedial action on the part of the Government. Despite some minor inefficiencies in its regulatory set up, SEBI’s role in enhancing India’s capital markets is not subject to any significant doubt.

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58 Securities and Exchange Board of India, Compliance with the provisions of Equity Listing Agreement by listed companies - Monitoring by Stock Exchanges, Circular CIR/CFD/POLICYCELL/13/2013 (Nov. 18, 2013). The impact of this measure is yet to be known, as it is a fairly recent one.


As of March 2013, SEBI had a total of 666 employees, with 553 of them being officers in various grades. While the number of employees appears high in absolute terms, SEBI is understaffed given the vast nature of India's capital market and its players. The enforcement of securities regulation continues to be a challenge due to the inadequacy of resources within the regulator. However, SEBI has been taking steps to meet with the needs of a dynamic stock market environment. More recently, it appointed a management consultant to revisit the structural and organizational issues, to re-prioritize areas of focus and to concentrate on building up the required expertise and human resources to meet with the modern challenges. Based on the recommendations of the consultant, SEBI is in the process of establishing a more focused approach towards enforcement of its regulations.

As secondary market disclosures are regulated through the listing agreement, the stock exchanges are responsible for their enforcement. The benefit of this arrangement is the flexibility it provides as the basis for enforcement is through self-or-market regulation. However, stock exchanges are not vested with significant powers of enforcement against errant issuers in the same way that SEBI has been as a regulator. Stock exchanges hold the weapon of delisting, which they are usually hesitant to deploy as this measure hurts minority investors more than it benefits them. Hence, not only are the secondary market disclosures dissimilar and much less extensive than primary market disclosures in terms of substantive regulation, but their enforcement by the stock exchanges is far less effective compared to the enforcement of primary market disclosures by SEBI through extensive measures available to it, as I detail in the next sub-part.

C. SEBI’s Enforcement Powers and Activities

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62 Id. at 180.

63 Samie Modak, Special unit to aid stricter regulatory enforcement, BUSINESS STANDARD (Jan. 23, 2014).
The primary role of SEBI is to protect the interests of investors in securities and to promote the development of (and to regulate) the securities markets. In doing so, it has been conferred very wide powers to take “measures as it thinks fit”. More specifically, SEBI is empowered to regulate the manner in which companies access the capital markets, including the nature and extent of disclosures required. In enforcing these requirements, SEBI can even prohibit any company from “issuing prospectus, any offer document, or advertisement soliciting money from the public for the issue of securities”. This specific remedy for violation of disclosure norms in primary market transactions is therefore preventive in nature.

1. General Enforcement Measures

Apart from the specific remedy set out above, SEBI possesses several other powers and sanctions to deal with securities law violations. First, SEBI may suspend the trading of a security on a stock exchange, although as an investor unfriendly measure it is rarely exercised. Second, SEBI may restrain persons from accessing the securities markets and prohibit them from dealing in securities. Such a restraint order is usually imposed for a defined period of time. This power has been exercised quite frequently and effectively by SEBI to deal with securities law violations. The restraint orders are binding on either the issuer companies, their directors or promoters or all of them. For instance, in Securities and Exchange Board of India v. Ajay Agarwal, based on a complaint received regarding alleged non-disclosures in a prospectus, SEBI conducted an investigation and passed an

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64 Securities and Exchange Board of India Act, 1992, §11(1).
65 Id.
68 These powers emanate from the Securities and Exchange Board of India Act, 1992, §11 read with §11B.
69 These orders are upheld on appeal if they are found to be preventive in nature and not if they are punitive in nature. For a discussion of the relevant case law, see Sumit Agrawal & Robin Joseph Baby, Agrawal & Baby on SEBI Act 164-65 (2011).
order against the joint managing director of the issuer company restraining him from associating with any corporate body in accessing the securities market. On appeal, the Supreme Court of India upheld SEBI’s order. Third, SEBI may suspend the office bearers of a stock exchange or other self-regulatory organization. Fourth, SEBI may impose other types of orders including impounding the proceeds of the sale of shares effected in violation of securities laws, attach property such as bank accounts and also issue a restraint against alienation of property. The common thread that runs through these measures is that they are targeted at wrongdoers. More specifically, SEBI’s aim in imposing these measures is to act to prevent the commission or continuation of violations by the errant parties. The element missing in this scheme of things is the compensation of investors who may have suffered losses. SEBI’s regulatory focus is on the violators rather than the victims.

2. **Disgorgement of Profits**

The question of whether SEBI can order a disgorgement of profits has been the subject matter of some contention before the Indian courts. Such an order deserves greater attention because it appears similar to compensation of investor losses. The analysis of disgorgement begins with the need to determine whether “it is compensatory in nature or amount[s] to mere deprivation of the wrongdoer from its unjust enrichment”. In certain earlier cases, the appellate authority hearing appeals over SEBI’s orders refused to grant orders of disgorgement of profits as they were found to be either compensatory or penal in nature. However, subsequently the powers of SEBI to impose orders of disgorgement of profits were recognised on the ground that they are neither compensatory nor penal in nature. It was found that disgorgement of profits amounted to depriving the wrongdoers of

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71 In another case, the Delhi High Court recognised SEBI’s power to investigate into alleged misstatements or non-disclosures in a prospectus, and to pass appropriate orders based thereon. *Kimsuk Krishna Sinha v. Securities and Exchange Board of India*, [2010] 155 Comp. Cas. 295 (Del).

72 AGRAWAL & BABY, *supra* note 69 at 207.


their ill-gotten gains and to preventing them from unjustly enriching themselves.\textsuperscript{75} In other words, the need for disgorgement of profits and the computation of the amounts are based on the wrongful profits made by the violators of securities regulations rather than the losses caused to the investors. The present position regarding disgorgement of profits has been aptly summarized as follows:

As noted above, initially the disgorgement was sought to be characterized as compensatory in nature in \textit{Hindustan Lever}, then as equitable remedy in \textit{Rakesh Agarwal}, and in ... some IPO scam cases as an inherent power. Difficulty in characterizing the disgorgement as compensatory in nature is that loss of a person cannot directly be related to the person from whom disgorgement is made in all circumstances. Also for disgorgement it is not necessary to have an identifiable investor or person and the amount of loss suffered by him. Difficulty arises essentially in establishing a causal relationship. Order of disgorgement which merely seeks to appropriate illegal profits essentially lessens the intensity of the wrong and therefore is apt to be described as a remedial measure which is permissible to be taken under Section 11B. ...\textsuperscript{76}

Any ambiguity in SEBI’s powers to order disgorgement of profits has been put to rest through a recent legislative effort that has expressly recognized the power.\textsuperscript{77} The Securities Laws (Amendment) Second Ordinance, 2013 (the 2013 Ordinance)\textsuperscript{78} expressly confers SEBI with the power to order a disgorgement of “an amount equivalent to the wrongful gain made or loss averted by such contravention”.\textsuperscript{79} This suggests that the measures of disgorgement have a link to the losses suffered by the investors. Moreover, the 2013 Ordinance also states that the amounts recovered from wrongdoers through disgorgement shall be deposited into the Investor

\textsuperscript{75} \textit{Karvy Stock Broking Ltd. v. SEBI}, [2008] 84 SCL 31 (SAT). Several other cases are discussed in \textit{Agarwal & Baby, supra note 69} at 208-211.

\textsuperscript{76} \textit{Agarwal & Baby, supra note 69} at 211-12.

\textsuperscript{77} Previously, the courts and appellate authorities had to derive this power through necessary implication.

\textsuperscript{78} An Ordinance is promulgated by the President as a temporary legislative measure during the period when the Parliament is not in session. An Ordinance is valid for a period of 6 months. The 2013 Ordinance lapsed on January 15, 2014, and various options are being considered to prolong the applicability of its provisions. Shishir Sinha, \textit{Political Stalemate Defangs SEBI}, \textit{HINDU BUSINESS LINE} (Jan. 15, 2014). This paper assumes the validity of the 2013 Ordinance.

\textsuperscript{79} The Securities Laws (Amendment) Second Ordinance, 2013, §4. The Ordinance has been drafted so as to clarify that SEBI was always intended to have the power of disgorgement.
Education and Protection Fund (IEPF) \(^{80}\) to be utilized in accordance with appropriate regulations prescribed for the purpose. One of the objectives of the utilization of funds from the IEPF is towards compensation of losses to investors.

In this emerging scenario, there is a greater nexus between the ability of SEBI to order disgorgement of profits and its objective of making good investor losses. However, it is unclear whether the measure of disgorgement can be treated as a compensatory effort. Significant differences continue to exist. For instance, while the nature and extent of investor losses is an important determinative factor while ordering a disgorgement of profits, the amounts recovered cannot be directly applied towards investors’ losses as if it is an order for compensation. This is because the amounts are to be credited into the IEPF. Compensation of investor losses requires the discharge of a judicial or adjudicatory powers which are to be specifically authorized and cannot be merely inferred from statute. \(^{81}\) Such powers are generally conferred upon the civil courts that perform that adjudicatory role. Given that SEBI is only a regulatory authority and cannot perform all the functions of an adjudicatory body such as a civil court, its ability to order compensatory orders continues to carry some doubt.

Despite the fact that the gap between disgorgement and compensation has been gradually reducing under Indian law, the distinction continues to carry significant legal import in that SEBI continues to largely perform an administrative or regulatory role that is preventive in nature, while compensation of investor losses is inherently an adjudicatory mechanism that can only be carried out by the normal civil courts. \(^{82}\) The experience over the next few years will dictate whether SEBI is willing to utilize the newfound disgorgement powers to meet investor losses so as to constitute an effective substitute to compensatory mechanisms implemented through the normal civil courts.

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\(^{80}\) The IEPF has been established by the Central Government under company law. See, Companies Act, 2013, §125. Under this provision, several amounts recovered by the Government or the regulator are to be credited into the fund, which will be utilized mainly for investor protection purposes. One of the types of amounts to be credited is the proceeds of an order of disgorgement of profits.

\(^{81}\) AGARWAL & BABY, supra note 69, at 216.

\(^{82}\) Id.
3. Other Measures

While the substantive laws relating to securities regulation have become progressively extensive and sophisticated in India, one principal concern has often been the lack of effective enforcement of these laws by SEBI. Robust substantive laws lack the desired effect unless they are effectively enforced by the regulator.

This perceptible regulatory gap has more recently been addressed through the 2013 Ordinance. Several amendments to the legislation are aimed at bolstering SEBI’s investigative and enforcement powers. For example, SEBI is empowered to exercise the powers of search and seizure, recording of statements under oath and to call for information and records, including telephone call data records (which will become useful in cases such as insider trading where circumstantial evidence is crucial). In terms of enforcement, violators of securities regulations may be subject to attachment of their property, bank accounts and also the arrest and detention of violators in prison. All of these substantially enhance SEBI’s powers to deal with securities law violations, including misstatements in prospectuses in primary market offerings.

In addition to the preventive measures discussed earlier, SEBI also possesses the powers of imposing penalties through an adjudicatory process and also the power to initiate criminal prosecution of securities law offenders. As for adjudication, SEBI is entitled to appoint one of its own officers of a suitable rank to act as an adjudicating officer to impose penalties for various types of offences. In addition to the penalties imposed through adjudication, securities law violators

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84 While the precise amount of the penalty would depend upon the nature of violation, the maximum amount can extend up to Rs. 250 million in certain cases. In adjudicating the quantum of penalty to be imposed, the adjudicating officer may consider, among other things, the amount of losses caused to an investor or group of investors as a result of the violation. Securities and Exchange Board of India Act, 1992, §15((b)).
may be subject to criminal prosecution that SEBI may initiate before the regular criminal courts. Although both adjudication and criminal prosecution powers are available to SEBI, it is only the adjudicatory mechanism that has been extensively and successfully utilized by SEBI in various securities law violations to hand down penalties. As for criminal prosecution, SEBI’s track record has been far from successful. To my knowledge, it has not managed to secure criminal conviction in any high-profile case involving securities law violations. The reasons for this outcome range from the onerous nature of evidentiary burden in criminal prosecutions to the delays and inefficiencies in the criminal justice system in India. However, the need for better deterrent measures through criminal prosecutions has been recognised and the 2013 Ordinance envisages the establishment of special courts to try securities law offences so that such cases can be decided in a fast-track manner without being subjected to the delays in the regular court system. While criminal prosecutions have never been successfully employed as an enforcement mechanism for securities laws, this might change in the future, albeit gradually.

4. Settlements and Consent Orders

It is possible for alleged securities law violators to initiate the process of obtaining consent orders by way of settlement. SEBI has introduced a specific scheme for the purpose. SEBI passes consent orders based on the recommendations of a High Powered Advisory Committee comprising a retired judge of a High Court and two other external experts. Although SEBI has issued several consent orders, there has

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85 Securities and Exchange Board of India Act, 1992, §24. Punishment can extend to imprisonment up to a term of 10 years or with fine, which may extend up to Rs. 250 million, or both. SEBI does not have the powers to hand down punishment that is criminal or penal in nature, and hence must pursue charges before the regular criminal courts.

86 It is also the case that the adjudicating officer’s orders are subject to appeal before the Securities Appellate Tribunal (SAT). In several cases, the adjudicating officers’ orders have been overturned by the SAT.

been some level of criticism that the consent order mechanism was operated in an
*ad hoc* manner and that it lacked transparency.\textsuperscript{88} In response to this and based on
its experience of implementing the consent mechanism in the initial years, SEBI in
2012 modified process to streamline it further.\textsuperscript{89} Among the significant changes to
the scheme, the consent order was made inapplicable at the outset to violations
under specific categories such as insider trading, serious fraudulent and unfair
trade practice and failure to make disclosures in offer documents that materially
affect the rights of investors, except in certain specific circumstances after
considering the facts of the case. It appears that SEBI’s objective is to exclude
serious types of violations listed above at the outset rather than to leave the
discretion to the various authorities managing the consent process. This introduced
objectivity and transparency in the process, which were arguably missing in the
erstwhile guidelines. However, this also has the effect of substantially limiting the
scope of the consent order mechanism to minor violations that are technical in
nature and do not substantially affect investor rights.

While the consent mechanism is available to parties to initiate before SEBI,
it is unlikely to be available in case of serious offences, particularly given the more
stringent measures announced in the process implemented since 2012.

5. SEBI Enforcement Measures in Practice

In the background of the various powers exercisable by SEBI, it would be helpful to
briefly explore the extent to which SEBI has in fact exercised them in practice.
Reviewing recent data, SEBI has initiated investigation in respect of alleged
violations of securities laws. These include “price manipulation, capital issue
related irregularities, takeover related violations, non-compliance of disclosure

\textsuperscript{88} V. Umakanth, *SEBI Tightens Consent Order Norms*, INDIACORPLAW BLOG (May 27, 2012),
available at http://indiacorplaw.blogspot.sg/2012/05/sebi-tightens-consent-order-norms.html.

\textsuperscript{89} Securities and Exchange Board of India, *Amendment to the Consent Circular dated 20th April
requirements and any other misconduct in the securities markets”.  

In terms of the spread of the types of cases, the position is as follows:

Table 2: Nature of investigations taken up and completed by SEBI

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Investigations Taken up</th>
<th>Investigations Completed</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2011-12</td>
<td>2012-13</td>
</tr>
<tr>
<td>Market manipulation and price rigging</td>
<td>73</td>
<td>86</td>
</tr>
<tr>
<td>“Issue” related manipulation</td>
<td>35</td>
<td>43</td>
</tr>
<tr>
<td>Insider trading</td>
<td>24</td>
<td>11</td>
</tr>
<tr>
<td>Takeovers</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>20</td>
<td>12</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>154</strong></td>
<td><strong>155</strong></td>
</tr>
</tbody>
</table>

While market manipulation and pricing rigging, which emanates in the secondary markets, constitute SEBI’s primary focus in terms of number of investigations, securities offering related matters concerning the primary markets follow second. Although not evident from the data available from SEBI, not all of these investigations may pertain to the lack of disclosures or to misstatements in prospectuses related to public offerings of securities.

In terms of regulatory actions taken or measures adopted by SEBI, the spread is as follows:

Table 3: Types of regulatory actions taken during 2012-13

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Number of Entities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Suspension</td>
<td>31</td>
</tr>
<tr>
<td>Warning issued</td>
<td>9</td>
</tr>
<tr>
<td>Prohibitive directions issued under Section 11 of SEBI Act (other than consent orders)</td>
<td>168</td>
</tr>
<tr>
<td>Cancellation</td>
<td>3</td>
</tr>
</tbody>
</table>

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90 SEBI Annual Report, *supra* note 61, at 130.

91 *Id.* at 133.
<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Adjudication orders passed</td>
<td>485</td>
</tr>
<tr>
<td>Administrative warning / warning letter issues</td>
<td>31</td>
</tr>
<tr>
<td>Deficiency observations issued</td>
<td>14</td>
</tr>
<tr>
<td>Advice letter issued</td>
<td>23</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>764</strong></td>
</tr>
</tbody>
</table>

The statistics paint a clear picture displaying SEBI’s approach. SEBI deploys adjudication as a substantial measure in order to impose penalties (either monetary or non-monetary) on securities law violators, following by prohibitive orders. All of these are targeted at the violators and intend to be either preventive or deterrent in nature. Curiously enough, none of the measures adopted in the year in review was focused on the victims. The information does not disclose any disgorgement order passed during the period, and it is possible there was none.

In concluding this Part, I find that SEBI has acquired the status of an important regulator within India’s regulatory apparatus. It has acted during the last two decades to substantially enhance the disclosure and other norms governing both the primary and secondary markets. It has also emboldened itself with increasing enforcement powers, which it has in fact exercised in practice as the data demonstrate. Although there is room to adding to SEBI’s capacity and functions to meet with the dynamic demands of the Indian markets, it difficult to argue against the crucial role that SEBI has played in the explosion of India’s capital markets over the last two decades.

However, as the discussion in this Part seeks to demonstrate, SEBI role has been primarily regulatory in nature, acting swiftly to deal with developments in the capital markets and in a fairly independent manner. It has achieved this through its wide menu of sanctions and measures targeted at securities law violators. In this arrangement, however, the focus has hardly been on investors who have suffered losses. Compensation of such investors has not formed the mainstay of SEBI’s regulatory approach, at least not thus far.

### IV. SHAREHOLDER LITIGATION IN INDIA
This Part explores the remedies available to investors who may have suffered losses due to misstatements in prospectuses issued by companies. While significant remedies have historically been available under company law as well as contract law to affected shareholders, they have not been effectively used as a means of enforcing securities regulation. Despite the existence of a robust set of substantive laws (which have been further strengthened), the Indian legal system does not provide the requisite incentives to generate a higher level of shareholder litigation by affected investors. Considering the size and extent of India's capital markets, the number of shareholders actions that have reached the higher courts in India is miniscule, thereby suggesting that civil liability and shareholder actions for compensation to affected investors have not played a significant role in the development of India's capital markets.92

Before dealing with the substantive law as well as enforcement mechanisms, it is necessary to note that Indian companies' legislation is in a state of transition. The erstwhile Companies Act, 1956 (the 1956 Act) has been the principal companies' legislation for over 5 decades. This is in the process of being replaced by the Companies Act, 2013 (the 2013 Act). The 2013 Act has been passed by Parliament and has received the assent of the President of India, but only 98 out of its 470 sections have been notified so as to come into effect.93 The remaining provisions are expected to come into effect in due course once the Government of India promulgates the relevant rules under those provisions. Interestingly, some of the principal provisions relating to prospectus and liability for misstatement under the 2013 Act have already been brought into force. However, the provisions relating to enforcement mechanisms, such as class actions and a fast track dispute resolution procedure therefor are yet to become effective.

92 As we shall see, a substantial portion of the shareholder actions relate to the first half of the 20th century. Even though there has been an exponential growth of the capital markets in the last two decades, there is no evidence of relatable increase in shareholder actions.

A. Substantive Law for Civil Liability

Investors who are victims of misstatements in prospectus are entitled to two different (but related) causes of action under Indian law. They may either initiate an action seeking compensation under company law for losses or damage caused as a result of the misstatement, or they may initiate a claim under contract law for treating the contract of issuance of shares as void or for rescinding the contract. While restitution of the investors is the primary aim of either of these methods, there could be some technical differences in the nature and result of these actions under company law and contract law.94

Under company law, Section 35 of the 2013 Act95 provides that where a person has subscribed for securities of a company acting on any statement in a prospectus or the omission of any matter which is misleading, and has thereby sustained any loss or damage as a consequence, then such person may be entitled to claim compensation for such loss or damage.96 The affected investor may bring a claim against the issuer company and several other persons, including the directors, persons who have authorised themselves to be named in the prospectus, the promoters and experts.97

Some of the questions that arise in this behalf relate to who can bring and action and on what basis. At the outset, only investors who have subscribed to shares issued under the prospectus are entitled to bring an action. A person who is not a shareholder of the company cannot bring an action on the footing of an apprehension that members of the public may subscribe to shares of a company on

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94 The goal in this paper is to deal with the broad principles rather than the minor technical details of the differences between company law claims and contractual claims from a doctrinal perspective.

95 This section has been notified and is effective.

96 Section 35 of the 2013 Act replaces section 62 of the 1956, which imposed civil liability for misstatements in prospectus. While the new legislation represents an improvement over the old one in certain respects, some of the case law under the old legislation continue to be relevant, which I refer to in this Part.

97 In addition to a claim for civil liability, these persons may also be subject to criminal liability for “fraud” in accordance with the Companies Act, §447.
the basis of statements incorrectly made in the prospectus, although the 2013 Act expressly recognizes the rights of investor associations to bring an action. It is unlikely that investors who purchased shares in the secondary markets by relying on the prospectus will be able to bring an action for misstatement, as there may insufficient proximity to enable such action even if the statements contained in the prospectus influenced the shareholder. The 2013 Act appears to bring in clarity on certain counts. First, the omission of any matter in the prospectus that makes it misleading would be sufficient to invoke the civil liability provisions under section 34. Second, the requirement that the subscriber to the securities must have been “acting on any statement” would suggest an element of reliance, which must be established before an action may succeed. To my knowledge, the Indian courts have not adopted the “fraud-on-the-market” presumption, and it would be necessary for individual investors to establish reliance. Apart from the materiality of the misstatement, it is not necessary for the plaintiff investor to prove that the company or the directors knew that the statement was untrue. The investor only needs to prove that the statement was a material one and that the investor suffered losses by relying upon the same.

Investor actions may be brought against the issuer company, its directors, persons who have authorized the issue of the prospectus or the promoters. While

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99 Companies Act, 2013, §37, which provides that the suit may be filed “by any person, group of persons or any association of persons affected by any misleading statement or the inclusion or omission of any matter in the prospectus”.
101 See also, S. Chatterjee v. Dr. K.L. Bhave, AIR 1960 MP 323 [Chatterjee v. Bhave]; Shiromani Sugar Mills Ltd. v. Debi Prasad, AIR 1950 All 508 at ¶7 [Shiromani Sugar] (finding that the misrepresentation must have been of a material fact and that the investor must have been induced by it).
102 Basic v. Levinson, 485 U.S. 224 (1988). Brian T. Frawley, et. al., Supreme Court to Consider Overruling “Fraud-on-the-Market” Presumption, The Harvard Law School Forum on Corporate Governance and Financial Regulation (Dec. 4, 2013) available at https://blogs.law.harvard.edu/corpgov/2013/12/04/supreme-court-to-consider-overruling-fraud-on-the-market-presumption/ (noting: “Under this presumption, which may be rebutted by a defendant, an investor bringing a securities fraud claim may prove reliance without a showing that it actually was aware of and considered an allegedly material misrepresentation in making its purchase or sale of a security if that representation was made publicly and if the security it related to is traded in an efficient market.”).
103 Ramiya, supra note 100, at 976.
the actions against the issuer company are natural, the company's directors could potentially be faced with civil liability to compensate investor losses, which might require them to take necessary precautions before providing their consent to the issue of a prospectus. In India, promoters constitute an important constituency that is subject to the civil liability regime for misstatements in prospectus. The 2013 Act contains a wide definition of the expression “promoter” that includes any person who is named as such in the prospectus and also any controlling shareholder.104 Given the prevalence of concentrated shareholding in Indian companies and the somewhat extensive role played by controlling shareholders,105 the express recognition of their liability would augur for the benefit of the affected investors in case of misstatements. Given that controlling shareholders may themselves be corporate entities with financial resources, it confers a better chance of recovery for suing investors (in addition to what they may obtain from the company and its directors).

Defendants in investor actions may avail of certain safe harbor provisions. If a director withdraws consent before the issue of the prospectus, then such director may avoid liability.106 If the prospectus is issued without the knowledge or consent of any person (director or promoter) and such person gave reasonable public notice of the fact immediately upon becoming aware therefore, liability may be avoided.107 Although there is no statutory due diligence defence against misstatement claims similar to certain other jurisdictions, directors have a general duty to act with skill, care and diligence.108 Upon establishing that the directors’ conduct meet with these general diligence standards, it may be possible for directors to set up a defence against misstatement claims, although this area of the law is yet untested in India.109

104 Companies Act, 2013, §2(69).
105 See, supra Part IIC.
106 Companies Act, §35(2)(a).
107 Companies Act, §35(2)(b).
108 Companies Act, §166(3).
109 It is likely that courts will be required to rely on developments in common law in this behalf.
Courts in India would award compensation for actual loss suffered by the investors. Although there is no statutory guidance on the measure of damages, principles can be drawn from general law relating to contractual or tort liability. The measure of damages for such loss arising from an untrue statement or omission would be the “difference between the value which the shares would have had but for such statement or omission and the true value of the shares at the time of allotment”.\(^{110}\) The measure of damages would be computed as the difference in the price paid by the affected investors and the real value of the shares at the date of purchase.\(^{111}\) In *Chatterjee v. Bhave*,\(^{112}\) the court held that in computing the market value of the shares of the company care must be taken to ensure that such value itself is not the result of the fraudulent misrepresentation complained of. Instead, it is necessary to determine the “intrinsic value” of the shares as a measure of its value.\(^{113}\) The courts have not clearly ruled on how best one may determine the intrinsic value of the shares. As for the timing in relation to which the losses must be computed, it would not be the time of purchase of the affected securities, but rather the time when the fraud or misstatement was discovered,\(^{114}\) at which time the market is expected to settle or correct itself.

The remedy for misstatement in prospectus does not lie solely in company law, which provides for a claim in damages. Remedies may be invoked under contract or tort law as well.\(^{115}\) For example, an investor who suffers losses due to a material misstatement or omission in a prospectus may bring a contractual claim for rescission of contract, and claim for repayment of the monies invested in a

\(^{110}\) *RAMAIYA, supra* note 100, at 979.

\(^{111}\) *Id.*

\(^{112}\) *Supra* note 101, at ¶22.

\(^{113}\) *Id.*

\(^{114}\) *Id.*, at ¶23.

\(^{115}\) The 1956 Act expressly provided that the liability provisions in that Act shall not “limit or diminish any liability which any person may incur under the general law …” Companies Act, 1956, §56(6). *See also, Shanmugam Sundaram Chettiar v. Rangarama Naicker*, (1934) 4 Comp. Cas. 367; *Amichand Doss v. Manavedan Tirumalpad*, AIR 1945 Mad 5. Although the 2013 Act does not contain an express provision that preserves liability under general law, it does not exclude the possibility of such liability either and hence it would be open to affected investors to initiate legal actions based on contract or tort law as well.
company's securities that was influenced by such misstatement or omission. This is because a contract based on misrepresentation is voidable under Indian contract law.

Returning to company law, the 2013 Act provides affected investors with an additional remedy, which is similar to an appraisal right. For example, when the issuer company wishes to utilize monies raised through a prospectus for any objects other than that for which the monies were raised, it shall not do so without obtaining a special resolution of the shareholders. Moreover, the dissenting shareholders shall be given an opportunity to exit from the company by selling their shares either to the company or the controlling shareholders in accordance with regulations to be prescribed by SEBI. Similarly, any variation of terms of a contract referred to in the prospectus would require the authority of the shareholders by way of a special resolution with similar exit rights given to the dissenting shareholders. Although these appraisal-type rights do not directly relate to misstatements or omissions in the prospectus, but rather to the variation of the terms (particularly the utilization of proceeds of the offering), they do provide significant rights to minority shareholders.

Finally, in terms of timing of an investor action, it must be brought within the statutory limitation period. A claim for compensation under company law or one for rescission under contract law would have to be brought within 3 years from the time the cause of action arises. The limitation period would usually run from the time at which the misrepresentation or omission comes to the knowledge of the investor.

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116 Ramaiya, supra note 100, at 981.
118 A special resolution requires a 75% majority of shareholders (or, as the case may be, value of shares) among those present and voting at a shareholders’ meeting. Companies Act, 2013, §114(2).
119 Companies Act, 2013, §13(8).
120 Id. In this behalf, the crucial issue pertains to the manner in which the fair value for the exit by the minority will be determined by SEBI.
121 Companies Act, 2013, §27(2).
of the claimant. In case of significant delays, the court may refuse to entertain a claim, thereby depriving the affected investors of their remedy.\footnote{One of the grounds due to which a court refused to intervene to grant the remedy sought by the affected investors was that the investors had “lost their right to rescind the contract by their laches.” \textit{Shiromani Sugar}, supra note 101, at ¶19.}

Indian law therefore provides a sufficiently robust remedy for investors who may have suffered losses due to misstatements or omissions in a prospectus by which a company raises funds. The substantive law is comparable to legal systems in the common law world. However, there have only been a handful of report cases in India whereby investors have initiated legal actions. This, as we shall see in the next sub-section, is because of the lack of effective enforcement mechanisms and the necessary incentives to initiate legal actions rather than the quality of the substantive law relating to investor rights.

\textbf{B. Enforcement}\footnote{Parts of this section have been derived from the broader discussion on shareholder derivative actions in India contained in Vikramaditya Khanna & Umakanth Varottil, \textit{The rarity of derivative actions in India: reasons and consequences}, in \textit{Dan. W. Puchniak, Harald Baum & Michael Ewing-Chow, The Derivative Action in Asia: A Comparative and Functional Approach} (2012) [\textit{Derivative Actions}].}

The substantive law on civil liability for misstatements in prospectus is effective only if it is properly enforced. The enforcement mechanism depends upon various factors, including the ability to aggregate actions by small investors, a timely resolution of disputes by the court system, cost-effective nature of the remedy and the existence of other factors including a plaintiff bar that is sufficiently incentivized to pursue actions. Most of these factors that apply in developed common law system are absent in India.

1. Aggregation of Securities Actions

Usually, in the case of misstatements or omission in prospectus that give rise to shareholder claims, the same event can give rise to numerous causes of action to various investors. If so, any mechanism that permits effective aggregation of
securities claims so as to make the actions worthwhile will operate to ensure proper enforcement of substantive securities laws. In the U.S. context, the class action mechanism has performed this role effectively. However, although Indian law does recognize the concept of aggregation of claims, the class action mechanism has not been utilized effectively in the context of securities regulation.

In India, the concept of representative actions under the Civil Procedure Code, 1908 (CPC) comes closest to the class action mechanism. Under Order 1 Rule 8 of the CPC, where numerous persons have the same interest in a suit, one or more such persons may bring or defend an action on behalf of, or for the benefit, of all persons so interested. However, such an action requires the permission of the court before it can proceed. Upon receiving the court’s permission, the plaintiff (at its expense) must give notice to all interested parties regarding the institution of the suit, and the interested parties may seek to be included as parties to the suit. In such case, the parties included within the class would be entitled to the benefit of the suit if it succeeds. Although class actions are possible as representative suits, they have not been popular in the corporate and securities law fields. For example, even though shareholder derivative actions in India are brought as representative actions under Order 1 Rule 8 of the CPC, an earlier study found that “[o]ver the last sixty years only about ten derivative actions have reached the high courts or the Supreme Court. Of these, only three were allowed to be pursued by shareholders, and others were dismissed on various grounds.”

Recognizing the need for a specific class action mechanism for shareholder actions, the 2013 Act includes a provision for the same. Section 245 of that Act enables any shareholder or class of shareholders to file an application before the National Company Law Tribunal (NCLT) on behalf of all shareholders if they are

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126 The court decides at the interlocutory stage.
127 See also, Pritha Chatterjee, Securities fraud and class action suits in India: need for legislative riders in clause 216 of the Companies Amendment Bill 2009, 32(9) Comp. Law. 284, 284 (2011).
128 Khanna & Varottil, Derivative Action, supra note 125 at 380.
129 This provision is yet to be notified and hence is not effective for the time being.
130 Such class actions are to be filed before the NCLT, which is a specialized tribunal, rather than the regular courts, a matter that is discussed in detail later in this Paper. See, infra Part IVB2.
of the opinion that the management or conduct of affairs of the company are being conducted in a manner prejudicial to the interests of the company or its shareholders. The scope of section 245 is very wide thereby enabling the class of shareholders to seek various types of remedies against the company and persons associated with it. Among these remedies, the class of shareholders may claim damages or compensation from (i) the company or its directors for any fraudulent, unlawful or wrongful action or omission; (ii) the auditor or audit firm of the company for any improper or misleading statement of particulars in the audit report; or (iii) any expert advisor or consultant for any incorrect or misleading statement made to the company.\(^{131}\) The class action mechanism is therefore available for compensating investors for losses caused due to misstatements or omissions in the prospectus so long as it falls within one of the situations described above.

The specific provision for class actions also contains some details regarding the procedure for aggregation. For example, once a member of the class files an application, a public notice is to be served for admission of the application to all members of the class.\(^{132}\) Moreover, similar applications made in several jurisdictions may be consolidated into a single action.\(^{133}\) The NCLT may take into account several factors such as whether the suing shareholders are acting in good faith, whether the action could be pursued by the shareholder individually than as part of the class, and whether the disinterested members of the class are in favor of continuing to pursue the action.\(^{134}\) In case the shareholder action is found to be frivolous or vexatious in nature, the NCLT may reject the application and make an order requiring the suing shareholder to meet a portion of the costs.\(^{135}\)

The class action mechanism also carries within it certain checks and balances to prevent the opening up of the floodgates resulting in too much

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131 Companies Act, 2013, §245(1)(g).
132 Companies Act, 2013, §245(5)(a).
133 Companies Act, 2013, §245(5)(b).
134 Companies Act, 2013, §245(4).
135 Companies Act, 2013, §245(8).
litigation against companies. Accordingly, a class action can be brought only if it carries a minimum level of support, i.e. 100 shareholders or 10% of the total number of shareholders in the company. This provision was not contained in the initial drafts of the Companies Bill and was introduced subsequently due to concerns from the industry as a result of the potential risks that companies would face numerous lawsuits from shareholders, many of which may not carry merit. Given this requirement of a substantial number of shareholders for initiating class actions, it seems unlikely that there will be a spate of investor class actions against Indian companies even after this mechanism under the 2013 Act becomes effective.

2. Forum for Adjudication

Investor suits for misstatements are brought before the regular civil courts. Once the trial is conducted and verdict passed, parties have the option of preferring an appeal to the High Court and thereafter to the Supreme Court of India, if leave is granted. The striking feature of the Indian judicial system at different levels is the inordinate delays in the disposal pending matters. It takes more than 15 years on average for disputes to be finally determined by the Indian courts, due to which nearly a whopping 32 million cases are pending before Indian courts at different levels. While desperate measures are being taken by the executive and the judiciary to reduce pendency levels, it would be long before the systems achieves the required levels of efficiency. The delays in recovery result in substantially

136 Companies Act, 2013, §245(3).
138 A number of other specific operational concerns have been raised regarding the effectiveness of the class action mechanism, which are beyond the scope of this paper. For details, see, Mihir Naniwadekar, Class Actions in the Companies Act, 2013: A Recipe for Confusion?, INDIACORPLAW BLOG (Sep. 6, 2013), available at http://indiacorplaw.blogspot.sg/2013/09/class-actions-in-companies-act-2013.html; Pritha Chatterjee, supra note 127, at 288; Khanna & Varottil, Derivative Actions, supra note 125, at 394-96.
139 In the cities of Mumbai, Chennai and Kolkata, the High Court has the original jurisdiction to conduct the trial at the outset if the amount claimed in the suit is beyond the minimum amount required to invoke the High Court’s original jurisdiction. This therefore becomes available when the amounts claimed are substantial, but not otherwise.
140 Supra notes 3-4, and accompanying text.
reducing the incentives of affected investors to make the claims. Even if the investors are ultimately successful, the value of the amounts recovered allowing for the delays would be insubstantial in that while the losses are computed with respect to the value of money at the time the losses are suffered or the suit is initiated, successful parties are able to reap the benefit thereof only after a prolonged gap, by which time the amount recovered would only represent a fraction of the value computed as of the date of recovery. This may make the suit cost-ineffective.141

The 2013 Act seeks to sidestep judicial delays by permitting affected investors to initiate class actions before the NCLT, a new body to be established once the relevant provisions of the legislation are made effective.142 The NCLT is a quasi-judicial body that will assume the role that courts and certain tribunals currently perform under company law.143 The advantage of the NCLT is that it will be a specialized body dealing solely with disputes relating to corporate law, and will not be subject to the delays and other concerns afflicting the regular court system. At the same time, some questions remain regarding the exercise of powers by the NCLT. For example, it is doubtful whether a quasi-judicial body is capable of adjudicating civil disputes between affected investors on the one hand and issuer companies, directors or intermediaries on the other hand with a view to awarding compensation. Moreover, given the independence of the judiciary and other

141  The following example exemplifies the problem:

For example, let us assume that the non-reimbursable costs of legal action are $5,000 and the benefits of a successful claim are $11,000. If the judgment comes within one year then the present value of the benefits is $10,000 and the present value of the costs is (say) $5,000; this provides an expected gain of $5,000 and the suit is worth bringing. If the judgment granting the $11,000 recovery occurs ten years from now, however, then it may have a present value of only $4,000, but the legal costs may still have a present value closer to $5,000 (because much of the legal expense is incurred at the start of the process). Now the suit is not worth bringing.

Khanna & Varottili, Derivative Actions, supra note 125, at 375-76.

142  Companies Act, 2013, Chapter XXVII. Not all of the provision of this Chapter are effective yet.

143  Apart from investor class actions, the NCLT will assume the jurisdiction currently exercised by the High Courts for schemes of arrangement and amalgamation as well as winding up of companies, and the jurisdiction currently exercised by the Company Law Board for matters involving oppression and mismanagement.
constitutional protections, the establishment of the NCLT has been subject to judicial challenge in the past. Although the constitutional validity of the NCLT was upheld by the Supreme Court of India subject to certain conditions, its potential establishment under the 2013 Act has again been challenged before courts, which makes it likely that there would be further delays before the NCLT can see the light of day.

Given the delays and inefficiencies in the court system, it is difficult to be optimistic regarding investor suits constituting an important mechanism for compensating investors and thereby enabling the enhancement of the securities markets in India. While the NCLT is potentially a solution to the problem, the fact that its establishment has been (and would continue to be) mired in legal controversy casts a pall of gloom over its future.

3. Costs

India follows the English rule on costs, whereby the loser pays the reasonable costs of the opponent as ordered by the courts. Although Indian courts are likely to award reasonable (but not significantly high) costs to the successful party in civil litigation, the costs are likely to be substantial for individual retail investors to bring actions against large companies if the shareholders are likely to fail in such litigation. Therefore, the rule on costs acts as a disincentive to affected investors even if they have a strong case on the merits.

Moreover, in India the costs are not limited to attorneys’ fees. Because investor actions are brought before the regular civil courts, plaintiffs usually have to pay stamp duty and court fees. Although the incidence of stamp duty and court fees is not significant in some states, in others it is determined on an ad valorem basis.

146 Civil Procedure Code, 1908, §35(2). Furthermore, courts have the power to award compensatory costs in respect of false or vexatious claims or defences, Civil Procedure Code, 1908, §35-A. However, the maximum award of compensatory costs is Rs. 3,000, which is insubstantial in corporate or securities litigation.
basis as a percentage of the claim. Since one of the objectives of investor action is to secure compensation from the wrongdoers, an *ad valorem* determination could send the legal costs skyrocketing.

Despite the high costs, investor litigation might still be possible if there are strong incentives to other constituencies such as the plaintiff bar to bring actions against errant issuer companies and their directors. Contingency fees are one way to motivate entrepreneurially minded attorneys to take on riskier suits with the likelihood that they would partake a portion of the proceeds if the suit were successful. In other words, the risk of success or failure is shifted from the affected investors to the plaintiff attorneys. This even incentivizes attorneys to identify instances of possible misstatements and to take up actions on behalf of potential plaintiffs whereby it is the attorneys who spearhead the legal action and bear its costs. Although this system has worked in the U.S. and a number of other jurisdictions, contingency fees are prohibited in India thereby disincentivizing plaintiff attorneys from taking on riskier suits. Due to the complete absence of a plaintiff bar, affected investors themselves (especially the smaller ones) do not find it worthwhile to initiate class actions as there is neither a certainty of recovery nor of obtaining a net benefit from the suit (after taking into account the costs incurred).

Over the last few years, however, SEBI has decided to utilize amounts in its Investor Protection and Education Fund to aid investor associations recognized by it to undertake legal proceedings in the interest of investors in securities that are listed or proposed to be listed. This relates to proceedings involving a breach of

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147 See, for example, Karnataka Court Fees and Suits Valuation Act, 1958, §21, which provides that, in suits for money (including suits for damages, or compensation or arrears of maintenance, of annuities or of other sums payable periodically), court fees shall be payable on the amount claimed – that is, on an *ad valorem* basis without any limit. This is similar to the central legislation, the Court Fees Act, 1870, §7, which is applicable in states that have not enacted their own legislation on court fees.

148 This concern will be addressed once the NCLT is in place because such hefty stamp duty and court fees are not payable in actions before it, for it is not a regular civil court but rather a special tribunal.

149 Bar Council of India Rules, Part VI, Chapter II, §II, Rule 20.

securities regulation, which include misstatements and non-disclosures in connection with the issue, sale or purchase of securities.\(^{151}\) The funding mechanism is tightly controlled by SEBI, as applicants must demonstrate that they have a *prima facie* case and that the action is in the greater interest of shareholders.\(^{152}\) Funding will be provided for not more than 75% of the expenses incurred,\(^{153}\) with absolute caps of Rs. 2 million for actions before the Supreme Court and Rs. 1 million before other courts.\(^{154}\) The amounts will only be reimbursements of costs incurred and not upfront payments. The SEBI funding mechanism signals the intention of the regulator to promote investor activism through shareholder suits, and its readiness to assist by addressing the cost factor, at least partially if not fully.

4. Availability of Alternate Remedies

There are practical advantages to bringing alternate remedies through SEBI, which might even result in precluding shareholder suits for compensation claims. As we have seen,\(^ {155}\) SEBI has broad remedial powers for securities law violations, including to pass prohibitory orders, impose penalties, and initiate criminal prosecution. The objectives of actions before SEBI are the same as investor suits for misstatements as both tend to focus on investor protection as the goal. Curiously enough, where SEBI is empowered to act, the availability of the regular civil courts is excluded. This is because sections 15Y and 20A of the SEBI Act bar the jurisdiction of civil courts to entertain a suit or proceedings on matters in which SEBI is empowered to take action (e.g. securities law violations). This exclusion of civil jurisdiction has been interpreted widely with respect to SEBI.\(^ {156}\) It is only if

\(^{151}\) SEBI (Investor Protection and Education Fund) Regulations, 2009, §2(1)(g).


\(^{153}\) SEBI (Aid for Legal Proceedings) Guidelines, 2009, §6(5).

\(^{154}\) SEBI (Aid for Legal Proceedings) Guidelines, 2009, §6(1).

\(^{155}\) *See supra* Part III.

\(^{156}\) *Kesha Appliances P. Ltd. v. Royal Holdings Services Ltd.*, [2006] 130 Comp. Cas. 227 (Bom).
SEBI is not empowered to act in a particular manner that the civil court’s jurisdiction becomes potentially available.\textsuperscript{157}

Given this situation, the absence of investor actions against errant issuer companies for misstatements may be attributable to a variety of reasons: (i) the regular civil courts lack a speedy and effective remedy for investor actions for misstatements; (ii) the costs involved in bringing such actions is prohibitive and, given the absence of plaintiff bar, there are no incentives to bring such actions; (iii) small investors may be more inclined likely to approach SEBI because SEBI’s actions are likely to be speedier and less costly; (iv) the gradual enhancement of SEBI’s powers in recent years in order to fashion various types of remedies makes that approach more attractive; and (v) investors’ hands may also be tied because of the exclusion of the civil courts’ jurisdiction under sections 15Y and 20A of the SEBI Act for matters pertaining to securities regulation.

\textit{C. Conflict of Laws}

In case of cross-listed companies, a question may arise as to which law would apply to determine investor-related disputes. In the past two decades, several Indian companies have been listed on overseas stock exchanges through offerings of American depository receipts (ADRs), which are listed on the principal U.S. stock exchanges,\textsuperscript{158} or global depository receipts (GDRs), which are listed in London, Luxembourg or Singapore. There has not been much of the converse whereby foreign companies may list on Indian stock exchanges through Indian depository receipts (IDRs). Thus far, there has been only one foreign company that has listed its IDRs in India.\textsuperscript{159} Hence, it is more likely that Indian companies may be sued by investors located in other jurisdictions holding ADRs or GDRs of Indian companies.

\textsuperscript{157} There is an argument, though, that since the SEBI Act only provides for SEBI as a regulator without a mechanism for redressing the grievances of individual investors, civil courts will continue to have jurisdiction over actions for compensation under securities law, contract or tort. \textit{AGARWAL \\& BABY, supra} note 69, at 510. The scope of exclusion of the civil court’s jurisdiction is not beyond controversy.

\textsuperscript{158} Nearly a dozen Indian companies are listed on the NYSE or NASDAQ in the form of ADRs.

\textsuperscript{159} That is Standard Chartered Bank.
It is much less likely for a foreign company to be sued in India by investors holding IDR s because there is only one company that has ever issued them.

Given the difficulties of bring a legal action for compensation in India, it would not be surprising to find that ADR/GDR holders may consider themselves better off to sue in their respective jurisdictions (as the securities are listed there). In such case, a question would arise as to whether those court orders are enforceable in India, particularly when most of the assets of the issuer company are located within Indian territory. The provisions of the Civil Procedure Code, 1908 (CPC) determine the enforcement of foreign judgments in India. The manner in which foreign judgments are enforced in India depends upon the country in which the judgment has been passed. If the court that has passed the judgment is in a country with which India has entered into reciprocal arrangements for judgment enforcement, then the judgment may be enforced as if it were passed by an appropriate Indian civil court. India has entered into reciprocal arrangements with a few countries, primarily in the Commonwealth, including the U.K, Hong Kong, Singapore, New Zealand and Malaysia. Judgments obtained from these countries may be directly enforced in India.

In case of other countries, which include the U.S. as well as most civil law countries, a judgment obtained therein is not directly enforceable in India. Under the CPC, the holder of a judgment must bring a suit in India in which the foreign judgment will be conclusive as to any matter adjudicated upon. This is not a direct enforcement proceeding but rather a fresh suit, which is an additional step compared to judgments from countries with reciprocating arrangements. Moreover, the foreign judgment would not be conclusive in certain exceptional circumstances listed in the CPC, including where it has not been pronounced by a court of competent jurisdiction, where it has not been given on the merits of the case, or even where it sustains a claim founded on a breach of any law in force in India. For non-reciprocating territories, therefore, there could be multiplicity of

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160 Civil Procedure Code, 1908, §44-A.
162 Id.
litigation before judgment obtained from such territories can be successfully enforced against an Indian party.

Given the increasing incidence of cross-listings by Indian companies, the issues of conflict of law come to the fore. While it may be tempting for affected investor to initiate legal action outside India (e.g. in the jurisdiction where the securities are listed), they could face significant obstacles while attempting to enforce the judgment obtained, particularly if it is from a non-reciprocating territory.

V. CONCLUSION

This paper began with the hypothesis that shareholder litigation seeking compensation for losses due to misstatements would constitute an important tool for protection of minority investors thereby resulting in the enhancement of capital markets. This hypothesis is entirely reasonable in the Indian context given its common law heritage, robust substantive securities law for protection of investors and an extensive and independent judicial system. However, this paper concludes without finding adequate support for the hypothesis. This is attributable to a potent cocktail of factors, including inefficiencies in the enforcement mechanisms such as delays and high rate of pendency before the Indian courts, prohibitive costs in bringing civil suits which are not met with counterincentives such as a robust plaintiff bar and also the presence of alternate remedies that potentially bar civil suits from being initiated.

Despite the pessimism as to shareholder litigation, Indian capital markets have not only thrived, but have witnessed a dramatic explosion in the last two decades. As this paper seeks to demonstrate, the basis for such growth is attributable to

\[163\] For example, the issue of whether the ADR investors in Satyam ought to be permitted to sue in the U.S. or in India came up for consideration in the trial before a U.S. court. See, supra note 15, and accompanying text. Three different expert witnesses on Indian law submitted their reports, among other issues, on the question of the appropriate forum and the enforceability of foreign judgments in India. See, Kian Ganz, Satyam's settled US class action had no hope in India?, LEGALLY INDIA (Feb. 18, 2011). However, the court did not have the opportunity to decide on this question as the matter was settled.
securities regulation implemented through SEBI that is focused on the wrongdoers rather than on compensating the victims. The specialized capabilities possessed by SEBI coupled with its relative independence, flexibility and dynamism have had a much deeper impact on the development of India’s capital markets.

The paper therefore concludes with the finding that while the general approach in most common law markets is for courts to play a significant role in the development of the capital markets through the process of compensating investors for losses, the success of India’s capital markets growth has hinged upon the regulatory process rather than the courts.