

Business Standard

Why Sebi's consent mechanism needs an overhaul

Keep a demarcation on what is to be kept out of consent settlement to deter offences, say experts

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Sebi's widely written regulations and non-uniformity in settlement have created uncertainty

Audit firm [Price Waterhouse](#) recently moved a consent plea with the [Securities](#) and Exchange Board of India (Sebi) to settle an eight-year old investigation relating to the [Satyam](#) Computer Services fraud. Earlier, the [National Stock Exchange](#) was in talks with [Sebi](#) to settle the co-location matter through a [consent mechanism](#). These high-profile cases have once again put a spotlight on the consent route, which helps alleged wrongdoers settle pending matters with [Sebi](#) without accepting or denying guilt by undergoing a penal action.

Introduced in 2007, the [consent mechanism](#) initially gained popularity among [stock market](#) participants, as it helped save time and expenses of a legal proceeding. However, legal experts say there is scope for improvement in the framework. Also, data provided by [Sebi](#) show, due to lack of clarity, not many cases have been settled through this mechanism in recent years.

Earlier, there were doubts over its legal sanction because it was implemented through a mere circular. On several occasions the consent circular was challenged in court on the ground that it lacked legislative backing. First through an ordinance and later by enacting a regulation, the Settlement of Administrative and Civil Proceedings, 2014, the consent mechanism's legal standing has been fortified.

During 2016-17, [Sebi](#) had received 171 applications and settled 103 applications by passing orders in the consent and compounding category. The total settlement amount for these cases was a paltry Rs 13 crore. In 2015-16, 177 consent applications were received by [Sebi](#). This was a far cry from the 600-odd applications processed in the first three years after the mechanism was introduced.

Experts say the modified settlement rules have placed many restrictions on offences that qualify for consent settlement, which could be deterring applications. Offences that are serious in nature or that have market-wide impact or cause substantial losses to [investors](#) or affect the rights of [investors](#) in securities, especially retail [investors](#) and small shareholders, are kept out of its purview.

This is leading to ambiguity. Also, there is lack of clarity in computing the penalty, say experts. "Sebi's widely written regulations and non-uniformity in settlement have created uncertainty. The formulae for computing the settlement amount are also questionable," says Sumit Agrawal, founder, Suvan Law Advisors and author of a book on the [Sebi](#) Act.



ILLUSTRATION: AJAY MOHANTY

DWINDLING INTEREST

Consent applications	FY16	FY17
Received	177	171
Rejected	82	23
Pending	181	232
Amount*(₹ cr)	4.4	13.5

*Amount received towards disgorgement, settlement and legal expenses

DEALING WITH PENDENCY

Status of appeals before the Securities Appellate Tribunal in FY17

Pending	411	
Filed	470	
Upheld	50	
Remanded	125	

Source: Sebi Annual Report

Outgoing [Sebi](#) whole-time member S Raman recently told *Business Standard* that the scope of the [consent mechanism](#) could be increased. "It is wrong to exclude many infractions from the [consent mechanism](#). We are actually diluting the system by filing so many inefficient cases. Instead, hefty penalty should be a sufficient punishment," says Raman.

Experts say there needs to be a clear demarcation on what is to be kept out of consent settlement to deter serious offences. They point out that in 2012 the market regulator moved to make only more objective violations capable of being settled through the consent scheme. “The key would be to see how the penalties can be levied and how [Sebi](#) deals with more subjective violations,” says Simone Reis, head, PE and M&A practice, Nishith Desai Associates. An easy settlement process may incentivise non-compliance with the laws, she adds.

Reis is of the view that the terms of the settlement in cases of more serious [securities law violations](#) should be stricter and the penalty higher.

The smooth functioning of the consent route is also critical for Sebi, which is overburdened with pending litigation. Despite all efforts, litigation remains a challenge for the market regulator; during 2016-17, 376 cases were filed across various judicial forums. As on March 31, 2017, 1,311 cases were pending before various judicial forums. Besides, 470 appeals were filed in the [Securities](#) Appellate Tribunal (SAT). Further, 185 appeals were dismissed (ruled in favour of Sebi) while seven were allowed (ruled against Sebi). About 411 appeals were pending with the SAT as on March 31.

Experts suggest several alternatives to [Sebi](#) for reducing the number of pending cases. Increasing the number of adjudicating officers, new benches and members in the SAT (as proposed by Finance Minister Arun Jaitley in the 2015-16 Budget) and the opening of new benches will be helpful, says Reis.

There is always the possibility of competitors challenging settlement mechanism agreements as market impact and profits made are open to interpretation. Exploitation of this relaxation is another factor that [Sebi](#) needs to guard against. “Some traders may be open to the risk of fee settlement or short-term debarment while seeking to gamble with small and medium gains,” notes Prem Rajani, managing partner, Rajani Associates. As a way out, some experts are in favour of graded penalties, which can be low for the first or second offence, but high for repeat offenders.