

M&A Hotline

April 14, 2022

SEBI CRACKS DOWN ON UNSOLICITED TRADING TIPS!

SEBI AND INVESTOR PROTECTION

In an interesting development, pursuant to two complaints received by Securities and Exchange Board of India ("SEBI"), SEBI initiated proceedings against certain unregistered persons using social media platforms such as Telegram, Whatsapp, and Twitter to influence the prices of the stocks to make illegal profits.

On account of increasing instances of bulk SMSs being sent to the investors and the general public eliciting them to purchase stocks of identified listed entities, the SEBI had earlier stated¹ that investment advice and stock tips can only be given by investment advisors and certain other registered entities. To address the challenges in identifying reliable information and its senders, SEBI in consultation with the Telecom Regulatory Authority of India ("TRAI") had issued directions² to provide *inter alia* (a) SMSs pertaining to investment advise/stock tips may be sent only by SEBI registered intermediaries through registered telemarketers; and (b) mechanisms to filter and block bulk SMSs with certain identified keywords such as buy/sell/hold/accumulate/target followed by scrip code/name.

Thereafter, SEBI also cautioned³ the investors regarding such unsolicited messages not only in the form of bulk SMSs but also through websites and various social media platforms. In March 2021, SEBI advised all registered entities to ensure compliance with the Telecom Commercial Communications Customer Preference Regulations, 2018⁴ ("TCCCP Regulations") issued by TRAI. TCCCP Regulations required registration of the senders of messages, identification and categorization of different types of messages by their headers, to prevent deliberate mixing of promotional messages into transactional communication to customers, and lastly bestowed the customer/subscriber with complete control over the consent granted in connection with the messages including the ability to revoke the consent so granted.

SEBI'S ORDER

Based on the complaints received, SEBI conducted search and seizure operations on certain unregistered persons ("Noticees") for a period of 11 months from January 2021 to November 2021 to discover facts relevant to the said allegations.

SEBI discovered the following *modus operandi* in the operations of the Noticees:

- Noticees buy the stocks of a particular listed entity;
- then recommend to their subscribers (on their social media platforms) to buy the stocks of such listed entities, resulting in the creation of artificial demand and an increase in the prices of such stocks; and
- once the subscribers started purchasing the stocks of such listed entity and the stock prices increased, the Noticees sold the stocks held by them of such listed entity, to unjustly enrich themselves at the cost of other investors.

On the basis of the findings of the investigation and the depositions of the Noticees, SEBI passed an interim order-cum-show cause notice ("Interim Order") on the said Noticees⁵ noting that the Noticees were earning profits by defrauding the retail investors on their Telegram channel (*which falsely claimed that the Noticees were in the process of being registered as research analysts with SEBI*) and that the Noticees were in violation of certain provisions of the Securities and Exchange Board of India Act, 1992 ("Act") and SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 ("PFUTP Regulations").

In this regard, it is important to note that the Act and PFUTP Regulations prohibit using or employing any manipulative or deceptive devices or contrivance⁶ for violation of provisions of the Act and the PFUTP Regulations. The PFUTP Regulations apart from prohibiting any person from indulging in any manipulative, fraudulent or unfair trade practices in the securities market, also specifies certain conduct to be deemed to be a manipulative, fraudulent or unfair trade practice. Such conduct includes⁷:

- knowingly indulging in any act which creates false or misleading appearance of trading in the securities market;
- inducing any person for dealing in any security for artificially inflating, depressing, maintaining or causing fluctuation in the price of securities through any means;
- any act or omission amounting to manipulation of the price of security including influencing or manipulating the reference price or bench-mark price of any securities;

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- iv. disseminating information or advice through any media, whether physical or digital, which the disseminator knows to be false or misleading and which is designed or likely to influence the decision of investors dealing in securities;
- v. fraudulent inducement of any person by a market participant to deal in securities with the objective of enhancing his brokerage or commission or income; and
- vi. knowingly planting false or misleading news which may induce the sale or purchase of securities.

SEBI, in the Interim Order, noted that there was no fundamental research or analysis prior to giving recommendations and the sole purpose of such recommendations was only to create artificial demand for a particular stock. The investigation conducted by SEBI corroborates this fact. While a general comment in good faith suggesting trends in the securities market would not qualify as fraud under the PFUTP Regulations, however, that was not the approach of the Noticees in this scenario.

Accordingly, as per the power accorded to SEBI under the Act, the Interim Order was issued to the Noticees:

- a. restraining them from buying, selling, or dealing in securities;
- b. impounding the bank accounts of the Noticees jointly and severally for an amount of INR 2,84,29,948 (*being the amount of alleged unlawful gains*);
- c. mandating the Noticees to deposit the said amount into an escrow account and creation of a lien in favour of SEBI; and
- d. restricting the Noticees to dispose-off or alienate their assets.

PREVENTIVE ACTIONS BY SEBI

SEBI has been conducting search and seizure operations at various locations in India and has recovered multiple devices used in the commission of various activities by various entities and individuals which are not consistent with the Act, PFUTP Regulations and a detailed investigation into such activities is underway.⁸ Further, SEBI has yet again cautioned the investors to not rely on the investment tips/advice received from social media platforms and advised the exercise of utmost caution while taking investment decisions in the securities market, as these could be schemes and tools used to defraud the investors. SEBI has been attempting to make the investors aware of various grievance redressal mechanisms available to them and encouraged them to lodge their complaints.⁹

CONCLUSION

SEBI recognizes that the pace at which technology is growing brings along with it the hazards of its potential abuse by offenders who use it for performing illicit activities and is gearing up its tracking mechanism to track these offenders.

The Interim Order along with the aforesaid press releases carries a prescription of a cautionary approach for investors and participants in the securities market. While SEBI rightfully noted that perpetrators of offense employ new methods, technologies, and marketing techniques to defraud the investors, SEBI has also demonstrated that a collaborative approach to resolving these evolving issues is imperative even if the same necessitates a further overhaul of the existing regulatory framework.

— Akash Kumar, Yogesh Nayak & Nishchal Joshipura

You can direct your queries or comments to the authors

¹ SEBI PR No. 54/2017.

² TRAI F.No.311-3/2015-QoS dated August 10, 2017.

³ SEBI PR No.53/2020.

⁴ Issued by TRAI on July 19, 2018.

⁵ On January 12, 2022

⁶ Sections 12A (a), (b) and (c) of the Act and Regulations 3, (a), (b), (c) and (d) of the PFUTP Regulations.

⁷ Regulations 4(2) (a), (d), (e), (k), (o) and (r) of the PFUTP Regulations.

⁸ SEBI Press Release PR No.7/2022.

⁹ Increasing Awareness regarding Online Mechanisms for Investor Grievance Redressal, Circular No. SEBI/HO/MRD1/MRD1_ICC1/P/CIR/2022/05, dated January 05, 2022; Empowering Investors through Investor Charters, SEBI Press Release No. PR No. 2/2022, dated January 17, 2022.

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