

# DETHRONED ADANI, UNSTABILISED MARKET AND DISTRESSED INVESTORS: THE DOMINO EFFECT OF ADANI-HINDENBURG SAGA

*Basil Gupta & Ayush Mangal\**

*On January 24, 2023, shockwaves reverberated through the Indian stock market as the Hindenburg Research unveiled their report on the Adani Group. The report's allegations of stock manipulation and fraudulent accounting against the Adani Group arrived just as the conglomerate prepared for a monumental INR 20,000 crore further public offer ('FPO') the following week. Swiftly responding to these allegations, Adani framed the accusations as an assault on the nation's economic fabric, an assertion that disrupted the FPO, causing a seventy-percent collapse in Adani stocks and rattling retail investors. Adani's counter also shed light on Hindenburg's advantageous short selling tactics. This seismic event prompted a regulatory flurry, prompting three public interest litigations demanding a Supreme Court investigation, with both the Reserve Bank of India and the Securities and Exchange Board of India launching independent inquiries into the allegations against the Adani conglomerate. In this paper, the authors undertake a comprehensive analysis of the Adani-Hindenburg saga and the broader implications it carries. The authors navigate the intricate legal, regulatory, and ethical landscape to critically evaluate the existing mechanisms designed to safeguard investor interests from the influencers and research analyst organisations such as Hindenburg. By examining the strengths, gaps, and opportunities for improvement within these mechanisms, this paper seeks to provide a nuanced understanding of how the financial ecosystem can better shield investors against unforeseen market turmoil and manipulative practices.*

## TABLE OF CONTENTS

<i>I. Introduction.....</i>	<i>75</i>	<i>A. Laying the Safety Net – From Base to...?.....</i>	<i>79</i>
<i>II. Regulating 'Fins' of the Market – Strengthening Securities' Safety Nets Against Financial Frauds .....</i>	<i>78</i>	<i>B. Guidelines by ASCI: Influencing the Regulatory Framework.....</i>	<i>81</i>
		<i>C. Cross-Jurisdictional Analysis .....</i>	<i>82</i>

\* 4th-year students at National Law University, Jodhpur. The authors are grateful to the Editors of the NUJS Law Review for their constructive feedback and comments on the previous drafts of this article. All errors, if any, are solely attributable to the authors. The authors may be contacted at [basil.gupta@nlujodhpur.ac.in](mailto:basil.gupta@nlujodhpur.ac.in) and [ayush.mangal@nlujodhpur.ac.in](mailto:ayush.mangal@nlujodhpur.ac.in), respectively, for any feedback or comments.

III. <i>Between Short Selling and Securities Regulation</i> .....	84	1. <i>Nexus Test</i> .....	94
A. <i>Feasibility of Short-Selling in the Indian Regulatory Mechanism</i> .....	85	2. <i>Effect Doctrine Test</i> .....	96
1. <i>Under SEBI Research Analyst Regulations, 2014</i> .....	86	3. <i>Mechanisms for the Enforcement of Order by the Sebi Against the Hindenburg</i> .....	97
2. <i>Under SEBI Prohibition of Unfair and Fraudulent (PFTUP) Regulations, 2003, read with the SEBI Act, 1992</i> .....	89	IV. <i>Investor-Protection Framework: Protecting Investors From Share-Meltdown</i> .....	100
3. <i>Under SEBI (Investment Advisers) Regulations, 2013</i> .....	91	A. <i>Enforcement Measures: Fraud, Market Misconduct, and Breach of SEBI Regulations</i> .....	101
4. <i>Under SEBI (Prohibition of Insider Trading) Regulation, 2015</i> .....	92	B. <i>Smooth Trade and Settlement Process: Managing Market Fluctuations</i> .....	102
B. <i>Extra-Territorial Jurisdiction of SEBI</i> .....	93	C. <i>Disclosures By Listed Enterprises: Enabling Informed Investment Choices</i> .....	104
		V. <i>Conclusion</i> .....	105

## I. INTRODUCTION

In the fast-paced realm of financial markets, where fortunes can swiftly change, safeguarding investor interests is a paramount concern for regulators and stakeholders. The recent Adani-Hindenburg saga has spotlighted this issue, sparking discussions about the urgent need for a robust framework to ensure investor protection.<sup>1</sup> In financial markets, transparency holds the key to investors understanding their commitments and investments. The ever-volatile investment and share market frequently witnesses manipulations and financial disruptions.

Founded by Nathan Anderson in 2017, Hindenburg Research specialises in dissecting equities, credit, and derivatives, gaining recognition for unveiling corporate misconduct and adopting positions against corporations.<sup>2</sup> A prominent target has been the Adani Group, helmed by chairman Gautam Adani, India's second-largest conglomerate, encompassing seven highly valuable publicly traded stocks with a combined market value of approximately INR 17.8 trillion (USD 218 billion).<sup>3</sup>

<sup>1</sup> *Adani-Hindenburg Saga: Protect Indian Investors' Interests Against Market Volatility, Supreme Court to Centre*, THE ZEE BUSINESS, February 11, 2023, available at <https://www.zeebiz.com/companies/news-adani-hindenburg-saga-supreme-court-central-government-gautam-adani-group-indian-market-investors-interests-sebi-rbi-regulatory-mechanism-221689> (Last visited on September 28, 2023).

<sup>2</sup> *What is Hindenburg Research, the Company that has accused Adani Group of Stock Manipulation, Fraud?*, THE INDIAN EXPRESS, January 30, 2023, available at <https://indianexpress.com/article/explained/explained-economics/what-is-hindenburg-research-accused-adani-fraud-8404531/> (Last visited on August 22, 2023).

<sup>3</sup> Pooja Sitaram Jaiswar, *Adani Group's Market Value Rises Over Rs. 2 Lakh Cr in 5 Days Rally; Stocks Gain up to 45%*, March 6, 2023, available at <https://www.livemint.com/market/>

The unveiling of Hindenburg Research's report on January 24, 2023, had seismic repercussions for the Adani Group, as allegations of fraudulent share sales sent shockwaves through the conglomerate.<sup>4</sup> The report accused the conglomerate of "pulling the largest con in corporate history".<sup>5</sup> The firm posed some really important questions regarding the Adani Group's rapid expansion, the high valuation of its shares, and also suggested potential regulatory authorities' involvement in the accounting fraud and stock price manipulation. However, apart from the obvious fallout of the report, i.e. loss of confidence of investors and analysts in the Adani Group, the report has been seen as an attempt to smear reputation of India by many financial pundits.<sup>6</sup>

This cascade effect led to an astonishing INR 10.25 lakh crore nose-dive in domestic stock values of Adani Group and triggered bond sell-offs on an international scale.<sup>7</sup> The report's revelations thrust Adani's borrowing practices and liquidity concerns into the spotlight, igniting doubts about the conglomerate's integrity and prompting a re-evaluation of potential long-term manipulation strategies. These allegations acted as a clarion call for Indian investors to exercise caution and prudent decision-making. Hindenburg's assertions regarding the use of shell companies and front entities to obscure losses and manipulate stock prices were promptly met with counter arguments from Adani, who emphasised the proper disclosure of related-party transactions.<sup>8</sup> As the Adani Group's influ-

---

stock-market-news/adani-group-s-market-value-rises-over-rs-2-lakh-cr-in-5-days-rally-stocks-gain-up-to-45-11678110850604.html (Last visited on August 22, 2023).

<sup>4</sup> *Adani Group: How the World's 3<sup>rd</sup> Richest Man is Pulling the Largest Con in Corporate History*, HINDENBURG RESEARCH, January 24, 2023, available at <https://hindenburgresearch.com/adani/> (Last visited on August 10, 2023).

<sup>5</sup> Astha Rajvanshi, *India's Richest Man accused of Pulling the 'Largest Con in Corporate History*, January 29, 2023, available at <https://time.com/6250052/adani-hindenburg-fraud/> (Last visited on August 22, 2023).

<sup>6</sup> Shan Li & Weilun Soon, *Adani Group Calls Fraud Allegations Baseless, Bemoans Stock Moves*, THE WALL STREET JOURNAL, January 26, 2023, available at <https://www.wsj.com/articles/adani-group-calls-fraud-allegations-baseless-bemoans-stock-moves-11674741029#:~:text=The%20energy%20and%20infrastructure%20conglomerate,created%20anguish%20for%20Indian%20citizens> (Last visited on August 22, 2023); Hitesh Jain, *All that's problematic about Hindenburg Report and the Allegations in it*, BUSINESS STANDARD, May 20, 2023, available at [https://www.business-standard.com/companies/news/all-that-s-problematic-about-hindenburg-report-and-the-allegations-in-it-123052000878\\_1.html](https://www.business-standard.com/companies/news/all-that-s-problematic-about-hindenburg-report-and-the-allegations-in-it-123052000878_1.html) (Last visited on August 22, 2023); Reeba Zachariah & Partha Sinha, *Hindenburg Report 'Calculated Attack' on India, Claims Adani*, TIMES OF INDIA, January 30, 2023, available at <https://m.timesofindia.com/business/india-business/hindenburg-report-calculated-attack-on-india-claims-adani/articleshow/97428362.cms> (Last visited on August 22, 2023); *On Hindenburg, Adani Evokes 'Matrubhumi', Flaunts Spunk and Success*, THE ECONOMIC TIMES, July 18, 2023, available at <https://economictimes.indiatimes.com/news/company/corporate-trends/on-hindenburg-adani-evokes-matrubhumi-flaunts-spunk-and-success/articleshow/101854501.cms?from=mdr> (Last visited on August 22, 2023).

<sup>7</sup> Yuthika Bhargava, *Adani Group Market Value Fell 52% in 6 Months up to April, 6.4% Drop for India's Top 500 Pvt Firms*, June 21, 2023, available at <https://theprint.in/economy/adani-group-market-value-fell-52-in-6-months-up-to-april-6-4-drop-for-indias-top-500-pvt-firms/1635131/> (Last visited on August 22, 2023).

<sup>8</sup> Anwesa Madhukalya, *Hindenburg's Allegations v Adani's Response: Shell Companies, Money Laundering, Vinod Adani's Role*, January 30, 2023, available at <https://www.businesstoday.in/>

ence stretches across borders, including the United States of America ('USA') and Australia, regulatory scrutiny heightened, with investigations launched by the Securities and Exchange Board of India ('SEBI').<sup>9</sup>

Closely associated with the Adani-Hindenburg saga is the challenge in relation to the influence of 'finfluencers', who defended the report published by Hindenburg. This challenge highlights the need for comprehensive guidelines and regulations in the financial sector. Although SEBI has taken steps and initiated discussions in this regard, effective regulation in this area remains a distant goal. 'Finfluencers' are individuals who wield significant influence over financial decisions through social media and digital platforms, despite often lacking formal financial education.<sup>10</sup> They can enter into paid partnerships and advertising arrangements, raising concerns about conflicts of interest and the accuracy of advice. The cases of misleading information disseminated by 'finfluencers' have highlighted the urgency of regulation. While existing securities regulations have been used to address misconduct, it shall be argued in subsequent parts that a dedicated framework is required to comprehensively oversee 'finfluencers' in the digital age.

This paper underscores the intricate relationship between finfluencers, market turbulence, and regulatory responses, presenting a comprehensive perspective for stakeholders navigating this evolving landscape. By analysing Hindenburg's impact on the Adani Group within India's regulatory framework, the paper sheds light on vital considerations for addressing similar future incidents.

Part II delves into the evolving role of finfluencers, highlighting the necessity for robust regulatory frameworks to govern their expanding influence. Current progress, led by SEBI, remains gradual, necessitating adjustments to existing SEBI Regulations and Advertising Standards Council of India ('ASCI') Guidelines, drawing inspiration from global models. Part III delves into the impact of Hindenburg's report on Indian markets and the existing regulatory provisions of SEBI, while also contemplating potential legal avenues to address such incidents within the Indian context. Part IV examines the aftermath, emphasising on the Supreme Court's ('SC') involvement and SEBI's initiatives to enhance market transparency and resilience, showcasing a collaborative approach towards finfluencer-related market upheavals. Part V offers concluding remarks.

---

latest/corporate/story/hindenburgs-allegations-vs-adanis-response-shell-companies-money-laundering-vinod-adanis-role-368131-2023-01-30 (Last visited on August 22, 2023).

<sup>9</sup> Jayshree P. Upadhyay, *India Market Regulator Increases Scrutiny of Adani Group – Sources*, January 27, 2023, available at <https://www.reuters.com/markets/asia/india-market-regulator-increases-scrutiny-adani-group-sources-2023-01-27/> (Last visited on September 28, 2023).

<sup>10</sup> See *infra* Part II on "Regulating "Fins" of the Market – Strengthening Securities' Safety Nets Against Financial Frauds".

## II. REGULATING ‘FINS’ OF THE MARKET – STRENGTHENING SECURITIES’ SAFETY NETS AGAINST FINANCIAL FRAUDS

When Hindenburg Research released the report, many financial influencers, commonly referred to as ‘finfluencers’, defended the act, calling it a “freedom of speech and expression”. As SEBI consultation paper put forth, financial influencers are “persons who provide information and/or advice on various financial topics such as investing in securities, personal finance, banking products, insurance, etc., through social media/digital platforms and have ability to influence the financial decision of the followers”.<sup>11</sup>

Nonetheless, finfluencers generally align themselves with entities such as Hindenburg as a way to offer financial guidance without taking on responsibility or being held accountable. However, unlike Hindenburg which is regulated by the American authorities, financial influencers in India find themselves outside of the ambit of the legislative framework and therefore, remain largely unregulated. The current state of affairs seems more threatening in the era where social media has the ability to sway the users’ decisions, which confers the ability on finfluencers to control the market, despite lacking formal financial education or relevant credentials. While SEBI has imposed responsibilities on certified investment advisors and research analysts who possess comparable market-influencing capabilities, similar regulations do not exist for financial influencers.

Despite SEBI being vehement on regulating finfluencers since January 2022, it has yet to come up with a regulation on the same.<sup>12</sup> However, the SEBI released a consultation paper on unregistered entities including finfluencers, inviting public comments, which provides that,

- a. No SEBI registered intermediaries/regulated entities can have any monetary/non-monetary association with any unregulated entity including finfluencers;
- b. No SEBI registered/regulated entities shall not share any confidential information of their clients with unregistered entity; and
- c. Finfluencers registered with SEBI must also display their registration number, contact details and, must adhere to code of conduct and advertisement guidelines issued by SEBI.<sup>13</sup>

<sup>11</sup> Securities and Exchange Board of India, Consultation Paper on Association of SEBI Registered Intermediaries/Regulated Entities with Unregistered Entities (including Finfluencers), August 25, 2023, ¶3.2 (“Consultation Paper”).

<sup>12</sup> *SEBI Finalising Draft Discussion over Guidelines for ‘Finfluencers’*, THE HINDU, June 29, 2023, available at <https://www.thehindu.com/business/markets/sebi-finalising-draft-discussion-paper-over-guidelines-for-finfluencers/article67022754.ece> (Last visited on August 22, 2023).

<sup>13</sup> Consultation Paper, *supra* note 11, ¶4.

Meanwhile, till SEBI is not finalising the consultation paper, it would also be erroneous to say that the space is completely devoid of any regulation. Thus, it leaves us to deal with the SEBI (Prevention of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003 ('PFUTP Regulations') and, the ASCI Guidelines, with a mix of consumer laws coming in play.

In this part, the authors undertake a thorough examination of the current regulatory landscape governing financial influencers in India. They place a particular emphasis on SEBI's approach in tackling issues associated with these influencers. Subsequently, the authors delve into the existing mechanism under the Consumer Protection Act, 1986, and introduce the guidelines established by ASCI. They also underscore the inherent limitations of these guidelines in effectively addressing the challenges presented by financial influencers. Finally, the authors offer insights into potential avenues through which SEBI can draw inspiration from regulatory practices adopted in other nations such as the United Kingdoms ('UK'), the USA, Australia, and Germany, with the aim of crafting a robust framework for the regulation of influencers.

### A. LAYING THE SAFETY NET – FROM BASE TO...?

Finance Minister Nirmala Sitharaman asked investors to maintain caution in seeking financial influencers' advice in taking any financial decision.<sup>14</sup> Yet the effectiveness of influencer campaigns is much higher than Google or Facebook Ads due to their pre-existing niche audience, which exhibits a strong inclination toward testing investment products, further leading to a notably high conversion rate for fintech startups.<sup>15</sup>

The rise of financial influencers can be attributed to the pandemic when people confined to their homes increasingly turned to online platforms such as YouTube for insights into the financial markets, to learn the importance of investing their money as a means to secure future.<sup>16</sup> Further, learning about finances might not be as captivating as watching shows or movies, and this is where financial influencers play a significant role. They captivate their audiences by imparting knowledge about financial subjects that might otherwise appear uninteresting to the general public.

<sup>14</sup> *FM Sitharaman Warns Against Fin-Influencers: What's a Financial Influencer, How to Approach Advice with Caution*, May 1, 2023, available at <https://economictimes.indiatimes.com/news/how-to/fm-sitharaman-warns-against-fin-influencers-whats-a-finance-influencer-how-to-approach-advice-with-caution/articleshow/99891879.cms?from=mdr> (Last visited on August 22, 2023).

<sup>15</sup> Sashind Ningthoukhongjam, *Finfluencers' Earnings: Who Bears the Real Cost?*, MINT, May 15, 2023 available at <https://www.livemint.com/money/personal-finance/the-rise-of-finfluencers-how-social-media-personalities-are-changing-the-face-of-financial-advice-and-investment-11684173907021.html> (Last visited on August 22, 2023).

<sup>16</sup> Atanu Biswas, *Finfluencers on Song*, THE HINDU BUSINESS LINE, September 27, 2023, available at <https://www.thehindubusinessline.com/opinion/finfluencers-on-song/article67354288.ece> (Last visited on August 22, 2023).

Though the financial influencers revolutionised the way financial advice is disseminating, they have tremendous impact on individual's investment decisions. Without any adequate regulations to mandate disclosure, in cases of paid partnership, advertising, conflict of interest, many investors can lose their hard-earned money. To illustrate, in March 2023, the SEBI barred thirty-one entities from the securities market for involving in Pump and Dump Scheme, by uploading misleading videos on YouTube to buy shares of Sharpline Broadcast and Sadhna Broadcast.<sup>17</sup> The complaint alleged publication of videos on social media platforms that disseminated false information on possible deals, financials, growth prospects, and expansions, to lure retail investors in buying the scrips of Sharpline and Sadhna Broadcast, creating unusual rise in prices.<sup>18</sup> Once the prices increased rapidly, the promoters off loaded their holding at an inflated price, thereby, violating the provision of the SEBI Act, 1992, and the PFUTP Regulations.<sup>19</sup>

Similarly, in a first-of-kind action against finfluencer, SEBI penalised P.R. Sundar for providing investment advice through his website, without obtaining the necessary registration from SEBI.<sup>20</sup> In another move, SEBI issued warning against self-styled investment advisor Gunjan Verma for offering unregistered investment advice, violating registration requirements under SEBI (Investment Advisers) Regulations, 2013 ('Investment Advisers Regulation').<sup>21</sup> The SEBI also penalised of INR 2.84 crore on telegram channel ran by two brothers, who first bought shares of the company and then recommended subscribers of the channels to buy those shares.<sup>22</sup> Thereafter, they sold those shares on inflated prices, thereby committing an act of stock manipulation.<sup>23</sup>

In the absence of specific regulation for finfluencers, the SEBI often relies on the PFUTP Regulations. Here, reference is made to Regulation 4(k) which prohibits "disseminating information or advice through any media, whether physical or digital, which the disseminator knows to be false or misleading in a reckless or careless manner and which is designed to, or likely to influence the

---

<sup>17</sup> The Securities and Exchange Board of India, Interim Order in the matter of Stock Recommendations using YouTube in the scrip of Sadhna Broadcast Limited, WTM/ANISD/ISDSEC-1/24333/2022-23 (March 2, 2023); The Securities and Exchange Board of India, Interim Order in the matter of Stock Recommendations using YouTube in the scrip of Sharpline Broadcast Limited, WTM/ANISD/ISDSEC-1/24334/2022-23 (March 2, 2023).

<sup>18</sup> *Sebi Bars Arshad Warsi, Others for Stock Manipulation via Youtube*, THE INDIAN EXPRESS, March 3, 2023, available at <https://indianexpress.com/article/business/companies/sebi-ban-sadhna-broadcasts-promoters-arshad-warsi-securities-mkt-8474861/> (Last visited on August 20, 2023).

<sup>19</sup> SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003; *See also*, The Securities and Exchange Board of India Act, 1992, §11.

<sup>20</sup> The Securities and Exchange Board of India, Settlement Order in respect of Mansun Consultancy Private Limited, SO/AA/EFD2/2023-24/7081 (May 25, 2023).

<sup>21</sup> The Securities and Exchange Board of India, Order in the matter of unregistered investment advisory by Gunjan Verma, QJA/GG/WRO/26637/2023-24 (May 26, 2023).

<sup>22</sup> The Securities and Exchange Board of India, Final Order in the matter of Stock Recommendations using Social Media Channel Telegram, WTM/AN/ISD/ISD-SEC-3/25879/2023-24 (April 26, 2023).

<sup>23</sup> *Id.*

decision dealing in securities”.<sup>24</sup> The SEBI also broadened the ambit of Investment Advisors Regulations to render advice through an electronic medium as “investment advice” and therefore, require influencers to register themselves as an investment advisor with the SEBI.<sup>25</sup>

Further, the existing mechanism also revolves around §21 of the Consumer Protection Act, 1986, which empowers the Central Consumer Protection Authority to issue directions to influencers to discontinue an advertisement, if the same is misleading and is prejudicial to the interest of any consumer.<sup>26</sup> However, the scope of the aforesaid legislation is limited to the influencers promoting investment products and services of their own or those of third parties. Therefore, it may not cover all kinds of influencers such as those who are offering advice independently without associating with any third party.

Hence, it necessitates a tailor-made framework to address the influencer phenomenon, with the ASCI Guidelines potentially serving as a guiding reference for SEBI’s regulations concerning financial influencers.

## *B. GUIDELINES BY ASCI: INFLUENCING THE REGULATORY FRAMEWORK*

The ASCI came up with revised guidelines for financial influencers, defining them as “someone who has access to an audience and the power to affect their audiences’ decisions or opinions because of the influencer’s authority, knowledge or relationship with their audience”.<sup>27</sup> The definition primarily highlights the influence of financial influencers as being derived from their authority, knowledge, and relationships. In contrast, the SEBI consultation paper provides a comprehensive definition of financial influencers, encompassing a broad spectrum of topics and placing particular emphasis on their direct impact.

The said guidelines state that if there is any material connection, not limited to the monetary compensation, between advertiser and influencer, the same is required to be disclosed with a disclosure label that clearly identifies it as an advertisement.<sup>28</sup> Additionally, if an influencer contests any material connection with the advertiser, they must provide a declaration from the advertiser to ASCI, affirming the absence of such a connection. In instances where the advertiser’s

<sup>24</sup> The SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, Regulation 4(k).

<sup>25</sup> The Securities and Exchange Board of India (Investment Advisors) Regulations, 2013, Regulation 2(1)(l).

<sup>26</sup> The Consumer Protection Act, 2019, §21.

<sup>27</sup> The Advertising Standards Council of India, Guidelines for Influencer Advertising in Digital Media (August 17, 2023).

<sup>28</sup> *Id.*, 2.



location is unknown, proof of purchasing the featured products and brands can serve as substantial evidence to disprove any material connection.<sup>29</sup>

Furthermore, the guidelines provide that influencers providing banking, financial service, and insurance related advice, should be registered with SEBI and, must have suitable qualifications as well, and, must abide by all the disclosure requirements.<sup>30</sup>

Though the guidelines released by ASCI is remarkable to the effect that individuals can make well-informed choices, the foremost issue remains the enforcement of the same. Being a voluntary and self-regulatory body, its guidelines are binding only on its signatories,<sup>31</sup> and there is an absence of a redressal mechanism in cases of violation of the guidelines.<sup>32</sup> Though a complaint can be filed against the non-compliance, and the Consumer Complaints Council can adjudicate the same, there is no legislative mechanism to seek enforcement of the decision.<sup>33</sup>

The guidelines directed influencers to register themselves with the SEBI. However, till SEBI does not finalise its discussion paper, the enforcement of the same remains in the grey-area.

### C. CROSS-JURISDICTIONAL ANALYSIS

SEBI can also draw inspiration from other jurisdictions, going forward, to create a successful and robust framework. The UK's Code of Non-Broadcast Advertising and Direct & Promotional Marketing ('the Code')<sup>34</sup> read with the Social Media Advertisement Guide, outline rules for social media marketing, and provide detailed guidelines on disclosure of sponsored content to the followers. Further, the violation of the same can warrant criminal investigations as well.<sup>35</sup> Recently, the UK Financial Service Regulator, the Financial Conduct Authority ('FCA'), has also published a consultation paper to update its guidance on social media financial promotions. It provides that for promotions from influencers and unauthorised persons on social media, an approval from an authorised

---

<sup>29</sup> *Id.*, 5.

<sup>30</sup> *Id.*

<sup>31</sup> *Common Cause v. Union of India*, (2018) 13 SCC 440; *Procter and Gamble Home Products (P) Ltd. v. Hindustan Unilever Ltd.*, 2017 SCC OnLine Del 7072, ¶14, ¶16; *Century Plyboards (India) Ltd. v. Advertising Standards Council of India*, 1999 SCC OnLine Bom 444, ¶8.

<sup>32</sup> *Teleshop Teleshopping v. Advertising Standards Council of India*, 2015 SCC OnLine Bom 8777.

<sup>33</sup> *Id.*, ¶13, 18.

<sup>34</sup> *The United Kingdom Code of Non-Broadcast Advertising and Direct & Promotional Marketing* (12th ed., 2010).

<sup>35</sup> *Advertising Standards Authority (UK), Recognising ads: Social Media and Influencer Marketing*, March 23, 2023, available at <https://www.asa.org.uk/advice-online/recognising-ads-social-media.html> (Last visited on August 20, 2022).

person shall be required under §21 of the Financial Service and Markets Act, 2000.<sup>36</sup>

Likewise, the USA's Securities and Exchange Commission's ('SEC') office issued an investor alert on social media and investment fraud and filed charges against eight social media influencers for their involvement in a USD 100 million securities fraud scheme.<sup>37</sup> The influencers were accused of purchasing specific stocks and subsequently using platforms such as Twitter and Discord to manipulate the trading of exchange-traded stocks.<sup>38</sup> Further, the SEC's office issues an investor alert on social media and investment fraud in the cases of crypto investment scams, romance scams and, particularly in market manipulation schemes wherein fraudsters can manipulate the share price of a company's stock by spreading misinformation on social media.<sup>39</sup>

Reliance can also be placed on Australian Securities and Investment Commission's Information Sheet-269, which provides guidelines to influencers and, confers two primary obligations –*first*, licensing and good practices and *second*, disclosure.<sup>40</sup> The guidelines states that individuals providing financial product advice are required to possess an financial service license under the Corporations Act, 2001, and in the absence of same an individual may face imprisonment of up to five years.<sup>41</sup>

Further, India can take cue from the Germany which follows horizontal market control approach wherein, competitors and specific consumer associations are allowed to police market participants, which may lead to wider reporting of disclosure breaches.<sup>42</sup>

As regulatory authorities persist in their efforts to strike an equilibrium between the preservation of uninhibited expression and the upholding

<sup>36</sup> The UK Financial Conduct Authority, *GC23/2: Financial Promotions on Social Media*, July 17, 2023, available at <https://www.fca.org.uk/publications/guidance-consultations/gc23-2-financial-promotions-social-media> (Last visited on August 20, 2022).

<sup>37</sup> Press Release, THE US SECURITIES AND EXCHANGE COMMISSION, December 14, 2022, available at <https://www.sec.gov/news/press-release/2022-221#:~:text=The%20Securities%20and%20Exchange%20Commission,to%20manipulate%20exchange%2Dtraded%20stocks> (Last visited on August 20, 2022).

<sup>38</sup> *Id.*

<sup>39</sup> The US Securities and Exchange Commission, *Social Media and Investment Fraud – Investor Alert*, August 29, 2022 available at <https://www.sec.gov/oiea/investor-alerts-and-bulletins/social-media-and-investment-fraud-investor-alert> (Last visited on August 20, 2022).

<sup>40</sup> Press Release, AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION, March 21, 2022, available at <https://asic.gov.au/about-asic/news-centre/find-a-media-release/2022-releases/22-054mr-asic-issues-information-for-social-media-influencers-and-licensees/> (Last visited on August 20, 2022).

<sup>41</sup> *Id.*

<sup>42</sup> Anushka Borkar, *One Click and a Million Hits: Analysing the ASCI Guidelines for Influencer Advertising on Digital Media*, October 19, 2021, available at <https://theleaflet.in/one-click-and-a-million-hits-analysing-the-asci-guidelines-for-influencer-advertising-on-digital-media/> (Last visited on August 20, 2022).

of market integrity, the next part of this paper delves into an additional facet of market volatility – short-selling. The disruption caused by Hindenburg’s report on the Adani group highlights the significant consequences that such actions can potentially inflict on the Indian securities market. The act of short selling, in spite of its divergence from established investment paradigms, serves as a platform to demonstrate the emergent strategies that are actively reformulating the contours of the financial domain.

### III. BETWEEN SHORT SELLING AND SECURITIES REGULATION

Hindenburg Research’s area of expertise is conducting forensic financial research on corporate houses and conglomerates.<sup>43</sup> Thereby, it satisfies the criteria of being a ‘research analyst’ organisation under the USA Financial Industry Regulatory Authority (‘FINRA’) Rule.<sup>44</sup> Similarly, it also qualifies as a research analyst under the SEBI (Research Analyst) Regulations, 2014, (‘RA Regulations’) since it prepares and publishes reports on listed securities.<sup>45</sup> Hindenburg, also actively engages in short selling,<sup>46</sup> an advanced trading strategy which completely defies the conventional approach to investing.<sup>47</sup> The process involves borrowing securities with the anticipation of their value decreasing.<sup>48</sup> Once borrowed, they sell the securities at the prevailing market price.<sup>49</sup> Later, when the market price of the borrowed securities falls, they repurchase them at the lower price.<sup>50</sup> The borrowed securities are then returned to their original owner,<sup>51</sup> thereby making a profit.

It is also essential to understand the momentous short positions held by Hindenburg in Adani’s listed entities at the time of publishing their report. These short positions were established using non-Indian reference securities and US-traded bonds,<sup>52</sup> which raises concerns about potential hidden motives of

<sup>43</sup> Hindenburg Research, *About Us*, available at <https://hindenburesearch.com/about-us/> (Last visited on August 9, 2023).

<sup>44</sup> The Research Analysts and Research Reports, Financial Industry Regulatory Authority Rules, Rule 2241(8) (USA).

<sup>45</sup> The Securities and Exchange Board of India (Research Analyst) Regulations, 2014, Regulation 2(u).

<sup>46</sup> Tania Roy, *Everything You Need to Know About Short Selling, and How it is Done in India*, February 15, 2023, available at <https://thewire.in/business/explainer-short-selling-futures-india-adani-stocks-hindenburg> (Last visited on August 7, 2023).

<sup>47</sup> Anna-Louise Jackson & Benjamin Curry, *Short Selling Guide*, December 14, 2022, available at <https://www.forbes.com/advisor/investing/shortselling/#:~:text=Short%20selling%20is%20an%20advanced,the%20stock's%20price%20will%20decline> (Last visited August on 7, 2023).

<sup>48</sup> Neha Sharma, *Impact of Short Selling in Financial Markets*, Vol. 11(3), JOURNAL OF SOCIAL SCIENCE RESEARCH, 2447-2481 (2017).

<sup>49</sup> *Id.*

<sup>50</sup> *Id.*

<sup>51</sup> *Id.*

<sup>52</sup> Ritu Maria Johny, *Why Hindenburg Research Decided to Short only Adani Stocks Listed Outside India*, February 6, 2023, available at <https://www.hindustantimes.com/>

Hindenburg Research. By holding these short positions before releasing the report, they could potentially profit from the predicted price decline. If the report prompts shareholders to sell their stocks, Hindenburg Research could benefit by repurchasing these shares at a lower price, allowing them to take advantage of the ensuing market downturn.

In this part, the authors explore the complex interplay between short selling strategies and securities regulation, shedding light on the nuances and implications of these practices. In the subsequent sub-parts, the authors will discuss the feasibility of short selling within the Indian regulatory mechanism scrutinising its legality. Furthermore, the authors delve into the extraterritorial jurisdiction of SEBI, examining its authority to prosecute entities operating beyond India's borders.

### *A. FEASIBILITY OF SHORT-SELLING IN THE INDIAN REGULATORY MECHANISM*

The theoretical support for short selling is that it is used to correct market imbalances, especially when securities are thought to be overvalued.<sup>53</sup> Investors may opt for short selling if they believe a stock's price is inflated or in a bubble.<sup>54</sup> Exchanges disclose overall short positions to help investors make informed decisions. However, there are concerns when short sellers publish their own research reports because of potential conflicts of interest and lack of verification.<sup>55</sup>

The Satyam scandal of 2009, and the Wirecard and Enron scandals in the early 2000s, present a comparable situation. In the Satyam Scandal, the Chairman of Satyam acknowledged to regulatory authorities that the company had manipulated its financial records for an extended period.<sup>56</sup> Following a thorough investigation, these regulatory bodies made this revelation public and took appropriate regulatory steps.<sup>57</sup> Simultaneously, these regulators also received further 'disclosures' for several consecutive days, reportedly from CEOs of various other companies.<sup>58</sup> These 'disclosures' underwent meticulous examination, yet the regulators opted not to publicise them, choosing instead to dismiss them.<sup>59</sup> In contrast to the accurate disclosure made by Satyam, the rest of these 'disclosures' were

---

business/why-hindenburg-research-decided-to-short-only-adani-stocks-listed-outside-india-101675671991234.html (Last visited on August 7, 2023).

<sup>53</sup> Dr. C.K.G. Nair & M.S. Sahoo, *Short Selling and Activism don't go Together*, THE BUSINESS STANDARD, March 29, 2023, available at [https://www.business-standard.com/opinion/columns/short-selling-and-activism-don-t-go-together-123032901217\\_1.html](https://www.business-standard.com/opinion/columns/short-selling-and-activism-don-t-go-together-123032901217_1.html) (Last visited on August 7, 2023).

<sup>54</sup> *Id.*

<sup>55</sup> *Id.*

<sup>56</sup> Madan Bhasin, *India's Satyam Accounting Scandal: How the Story Unfolded?*, Vol. 2(1), INTERDISCIPLINARY REVIEW OF ECONOMICS AND MANAGEMENT, 23 (2012).

<sup>57</sup> *Id.*

<sup>58</sup> *Id.*

<sup>59</sup> *Id.*

proven to be groundless.<sup>60</sup> If all of these ‘disclosures’ had been made public, it could have inflicted significant damage on the market and stakeholders. This is due to the uncertainty surrounding the accuracy and extent of each claim that could have resulted in irreversible harm.

Likewise, in the instant case, if the objective of these ‘disclosures’ by Hindenburg is to expose governance lapses, established avenues exist, such as utilising the whistle blower mechanism, or engaging as proxy advisers, or working as research analysts while adhering to specific legal frameworks,<sup>61</sup> so as to avoid creating situations of market volatility. In previous instances, such as the Satyam Scandal, the regulatory body disclosed information to the public only after conducting due diligence. In contrast, Hindenburg made claims without substantial evidence or diligence on their part. As a result, the actions of the organisation cast doubt on their credibility and suggest that such practices may be driven more by personal interests.

Furthermore, in the case of Enron and Wirecard, both entities faced accounting scandals before their collapse. Enron’s downfall, partly due to renowned short seller Jim Chanos, was prompted by fraudulent accounting, leading to a loss of over USD 65 billion and bankruptcy.<sup>62</sup> Wirecard, accused of money laundering by short seller Fraser Perring, saw its share price crash when it admitted a USD 2 billion discrepancy in its balance sheet in June, 2020, ultimately declaring insolvency that month.<sup>63</sup>

In this part, the authors scrutinise the theoretical foundation of short selling and its role in correcting market imbalances. The authors also draw parallels with historical corporate scandals to underscore the importance of fair and transparent market practices. Furthermore, in the subsequent sub-parts, the authors delve into RA Regulations and PFUTP Regulations to assess Hindenburg’s actions within the Indian regulatory framework.

## 1. Under SEBI Research Analyst Regulations, 2014

Under the RA Regulations specific guidelines have been established for research analysts and research organisations that compile reports regarding companies listed within India.<sup>64</sup> As per these guidelines, any research analyst or entity that intends to publish a report concerning an Indian listed company is

---

<sup>60</sup> *Id.*

<sup>61</sup> Tania Roy, *supra* note 46.

<sup>62</sup> Huileng Tan, *The Massive Selloff in Adani Shares Eclipses those of other Short-Seller Targets like Enron and Wirecard*, February 7, 2023, available at <https://www.businessinsider.in/stock-market/news/the-massive-selloff-in-adani-shares-eclipses-those-of-other-short-seller-targets-like-enron-and-wirecard/articleshow/97681640.cms> (Last visited on August 30, 2023).

<sup>63</sup> *Id.*

<sup>64</sup> Apoorva Mandhani, *Hindenburg Report: ‘How to Ensure Investors are Protected,’ SC Seeks Suggestions from SEBI*, February 10, 2023, available at <https://theprint.in/>

required to comply with SEBI's regulatory framework, which may include obtaining necessary approvals or registrations.<sup>65</sup> Once these regulatory requirements are met, SEBI may issue a registration certificate to the publisher that is directly linked to the research conducted on the listed company.<sup>66</sup>

Furthermore, the RA Regulations provides a definition of the term 'research report' under Regulation 2(w).<sup>67</sup> In this context, a research report encompasses, "written or electronic communications that encompass research analysis, research recommendations, or opinions pertaining to securities or public offers". These communications serve as a foundational basis for facilitating well-considered investment decisions.<sup>68</sup> However, it is important to note that there are specific categories of communications that are excluded from this definition. These include,

- i. Observations that relate to broad trends observable within the securities market.
- ii. Discussions centered around wide-reaching indices.
- iii. Commentaries that address economic, political, or market conditions.
- iv. Routine reports or other communications designed for unit holders of mutual funds, alternative investment funds, or clients of portfolio managers and investment advisers.
- v. Internal communications that are not intended for current or potential clients.
- vi. Communications that serve as offer documents or prospectus materials distributed in accordance with the regulations stipulated by the Board.
- vii. Summarised statistical presentations of financial data concerning companies.
- viii. Technical analyses that are tied to the interplay between supply and demand within a specific sector or index.<sup>69</sup>

Furthermore, the regulations extend their scope to include foreign research analysts and organisations. Regulation 4 holds that any foreign research

---

judiciary/hindenburg-report-how-to-ensure-investors-are-protected-sc-seeks-suggestions-from-sebi/1365527/ (Last visited on August 8, 2023).

<sup>65</sup> The Securities and Exchange Board of India (Research Analyst) Regulations, 2014, Regulation 3.

<sup>66</sup> *Id.*

<sup>67</sup> *Id.*, Regulation 2(w).

<sup>68</sup> *Id.*

<sup>69</sup> *Id.*

analyst or organisation that intends to publish research reports about Indian entities listed on the stock exchange must first enter into a partnership with a research analyst registered with SEBI in India.<sup>70</sup> Only after establishing this collaborative arrangement with an Indian research analyst can the foreign entity engage in research activities and release reports concerning businesses listed on stock exchanges in India.<sup>71</sup> This requirement plays a crucial role by empowering SEBI to actively supervise the stock market and extend its authority to cover foreign research analysts and organisations.

It has already been established before that Hindenburg is a research analysis for the purposes of the RA Regulations. The Hindenburg report unquestionably qualifies as a 'research report' according to Regulation 2(w), as it presents detailed research analysis and opinions on securities, specifically those related to the Adani group of companies. Furthermore, it does not fall under the specified exceptions, as it is a targeted analysis of specific companies and their securities, focusing on financial and operational aspects. Regarding its status as a foreign research analyst, the report originates from Hindenburg Research, an entity that is based outside India. Further, without establishing any partnership with an Indian research analyst registered under the regulations, Hindenburg effectively evaded SEBI's jurisdiction as per Regulation 4 of the RA Regulations.

Therefore, it can be conclusively established that Hindenburg, contrary to SEBI's regulations, took an adverse course of action by publishing its report,<sup>72</sup> without establishing any agreement with an Indian research analyst registered under the RA Regulations. As mentioned earlier, Hindenburg also actively engages in short selling activities. Their possession of short positions prior to releasing the report subsequently had a negative impact on investors' confidence in their investments within the Adani group of companies. This resulted in profitable outcomes for those involved in short selling, which included Hindenburg itself.<sup>73</sup> Due to Hindenburg's failure to establish an agreement with an Indian research analyst, they effectively managed to evade falling within the purview of SEBI's jurisdiction.

Furthermore, there's the possibility that Hindenburg could be granted immunity by the Union of India, as stipulated in §24B of the SEBI Act, 1992.<sup>74</sup> This provision outlines the government's potential to provide protection against prosecution in India if the entity, which is Hindenburg in this case, agrees to disclose further details about the allegations presented in their report, along

---

<sup>70</sup> *Id.*, Regulation 4.

<sup>71</sup> *Id.*

<sup>72</sup> HINDENBURG RESEARCH, *supra* note 4.

<sup>73</sup> *GQG's Adani Investment Lifts Market Sentiment, SBI Leads Sensex 1.5% Higher*, THE HINDU BUREAU, March 3, 2023, available at <https://www.thehindu.com/business/gqg-investment-in-adani-stocks-lift-market-sentiment-indices-gain-more-than-15/article66576584.ece> (Last visited on August 10, 2023).

<sup>74</sup> The Securities and Exchange Board of India Act, 1992, §24B.

with substantial and corroborative evidence. However, the same has not yet been done by Hindenburg, and thereby, the possibility of grant of immunity is low.

## 2. Under SEBI Prohibition of Unfair and Fraudulent (PFTUP) Regulations, 2003, read with the SEBI Act, 1992

The practice of short selling in trading is widely acknowledged as lawful.<sup>75</sup> However, in India, only regulated short selling is allowed.<sup>76</sup> Hindenburg's report release initiated a strategic short selling strategy with the aim of reducing the value of Adani stocks. This intention was clear, as they already held short positions before unveiling the report.

§12A of the SEBI Act, 1992, prohibits the use of deceptive or manipulative methods in dealing with securities listed or intended for listing on Indian stock exchanges.<sup>77</sup> The provision reads as, "Nobody is allowed to:

- a) Use tricky or misleading methods when dealing with securities listed or going to be listed on a recognized stock exchange. These methods should follow the rules set out in this law and related regulations.
- b) Use any plans or schemes to trick people when dealing with securities listed or about to be listed on a recognized stock exchange.
- c) Do things that are meant to deceive or cheat people when dealing with securities listed or set to be listed on a recognized stock exchange. This should not go against the rules set in this law or related regulations[...]
- d) Gain excessive control over a company or its securities beyond what the rules allow when the company's securities are listed or going to be listed on a recognized stock exchange under this law." (emphasis on relevant sub-sections).<sup>78</sup>

This provision is closely associated with Regulation 4 of the PFTUP Regulations.<sup>79</sup> This regulation considers the spreading of false or misleading information or advice through any medium, be it physical or digital, with the intention

---

<sup>75</sup> Katherine McGavin, *Short Selling in a Financial Crisis: The Regulation of Short Sales in the United Kingdom and the United States*, Vol. 30, NW. J. INT'L L. & BUS., 201 (2010).

<sup>76</sup> The Securities and Exchange Board of India, *Discussion Paper on Short Selling and Securities Lending and Borrowing*, December 29, 2005, available at [https://www.sebi.gov.in/reports/reports/dec-2005/discussion-paper-on-short-selling-and-securities-lending-and-borrowing\\_12618.html](https://www.sebi.gov.in/reports/reports/dec-2005/discussion-paper-on-short-selling-and-securities-lending-and-borrowing_12618.html) (Last visited on August 10, 2023).

<sup>77</sup> The Securities and Exchange Board of India Act, 1992, §12A.

<sup>78</sup> *Id.*

<sup>79</sup> The Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003, Regulation 4.



of influencing investor decisions, as manipulative, fraudulent, and unfair in the context of securities trading.<sup>80</sup>

These laws highlight India's strict stance against unfair and manipulative stock trading practices, a response to past stock market fraud that impacted the economy and eroded investor trust.<sup>81</sup> These events led to the creation of securities laws to counter such deceptive trading methods. In *N. Narayan v. Adjudicating Officer, SEBI*,<sup>82</sup> the SC emphasised that these provisions aim to prevent manipulative trading and market misinformation. Market manipulation, per the court, involves unjustified interference with supply and demand equilibrium, undermining market integrity and efficiency.<sup>83</sup> Moreover, the SC in the cases of *Pooja Menghani v. SEBI*,<sup>84</sup> and *SEBI v. Kanaiyalal Baldevbhai Patel*,<sup>85</sup> clarified that although the term 'unfair' is not precisely defined in the PFTUP Regulations, it covers trading techniques that breach ethical standards and goes against good faith.

Possessing short positions prior to revealing the Adani group report signifies Hindenburg's deliberate employment of manipulative trading tactics, evident in the subsequent market downturn post-report publication.<sup>86</sup> The report generated doubt among investors concerning Adani's listed entities, eroding their confidence in investments. Hindenburg exploited investor trust and assurance in Adani's entities, resulting in notable gains for their investors through short selling.<sup>87</sup> In terms of ethical standards, Hindenburg's approach of releasing a potentially damaging report, which may have contained bold claims without substantial evidence, raises ethical questions. Engaging in short selling with the intent to profit from the resulting market turmoil, while potentially harming the interests of other investors, may be considered unethical in the context of responsible and fair-trading practices.

Further, Hindenburg's actions are in violation of §12A of the SEBI Act 1992, specifically sub-sections (a), (b), (c), and (f). *Firstly*, they may have employed tricky and misleading methods as per sub-section (a) by initiating a strategic short selling strategy with the aim of reducing the value of Adani stocks.<sup>88</sup> *Secondly*, their plan to release a potentially damaging report might fall under

---

<sup>80</sup> *Id.*

<sup>81</sup> Umakanth Varottil & Jayant Thakur, *Supreme Court on "Market abuse"*, April 19, 2013, available at <https://indiacorplaw.in/2013/04/supreme-court-on-market-abuse.html> (Last visited on August 10, 2023).

<sup>82</sup> *N. Narayan v. SEBI*, (2013) 12 SCC 152.

<sup>83</sup> *Id.*, ¶21.

<sup>84</sup> *Pooja Menghani v. SEBI*, 2019 SCC OnLine Cal 4950.

<sup>85</sup> *SEBI v. Kanaiyalal Baldevbhai Patel*, (2017) 15 SCC 1.

<sup>86</sup> Aviraj Pandey, *Adani- Hindenburg Swindle - An Analysis from SEBI's Perspective* Taxmann, July 27, 2023, available at <https://www.taxmann.com/research/company-and-sebi/top-story/10501000000023128/adani-hindenburg-swindle-an-analysis-from-sebis-perspective-experts-opinion> (Last visited on August 10, 2023).

<sup>87</sup> *Id.*

<sup>88</sup> The Securities and Exchange Board of India Act, 1992, §12A(a).

sub-section (b),<sup>89</sup> as it could be viewed as an attempt to trick investors. *Thirdly*, if their actions are deemed deceptive or aimed at cheating investors, they could be in violation of sub-section (c).<sup>90</sup> *Lastly*, if their short selling aimed to gain excessive control over Adani's securities by manipulating the market, this would contravene sub-section (f).<sup>91</sup> Therefore, it is clear that Hindenburg's trading actions violate the PFTUP Regulations read with the SEBI Act, 1992.

### 3. Under SEBI (Investment Advisers) Regulations, 2013

As per Regulation 2(m) of the SEBI (Investment Advisers) ('IA Regulations') an 'adviser' encompasses any individual or entity engaged in the business of providing investment advice to clients, individuals, or groups in return for compensation.<sup>92</sup> This definition also includes those who represent themselves as investment advisers, regardless of the specific title or designation they may use.<sup>93</sup> While Hindenburg Research predominantly functions as an investment research firm, its role can be likened to that of an 'adviser' as it offers information and analysis that can educate investors and their decisions. Thus, applying purposive interpretation to Regulation 2(m)<sup>94</sup> of IA Regulations, Hindenburg would be an 'adviser' under the said regulation.

Further, the IA Regulations mandate for advisers to maintain clear distinction between trading and advisory activities to prevent conflicts of interest.<sup>95</sup> Short sellers function as traders,<sup>96</sup> and their trading positions are generally kept private unless there's a requirement for disclosure.<sup>97</sup> Whether an investor holds short, long, or neutral positions in trading, this information is not typically disclosed unless it surpasses specific equity holding thresholds set by the regulations for takeover.<sup>98</sup> Trading data is openly available on exchanges without revealing the trader's identity.<sup>99</sup> Moreover, in India, stock exchanges disclose combined short trade positions without divulging individual identities, aligning with the original purpose and rationale behind introducing anonymous trading in the securities market.<sup>100</sup>

---

<sup>89</sup> *Id.*, §12A(b).

<sup>90</sup> *Id.*, §12A(c).

<sup>91</sup> *Id.*, §12A(f).

<sup>92</sup> The Securities and Exchange Board of India (Investment Advisers) Regulations, 2013, Regulation 2(m).

<sup>93</sup> *Id.*, Regulation 2(m).

<sup>94</sup> *Id.*

<sup>95</sup> *Id.*, Regulation 15.

<sup>96</sup> Bob Bernstein, *The CFTC's Attempt to Impose Speculative Position Limits on Off-Exchange Swap Contracts Likely to Face Continued Legal Challenge*, Vol. 30(3), *TOURO L. REV.*, 561(2014).

<sup>97</sup> Nair & Sahoo, *supra* note 53.

<sup>98</sup> *Id.*

<sup>99</sup> *Id.*

<sup>100</sup> *Id.*

#### 4. Under SEBI (Prohibition of Insider Trading) Regulation, 2015

It is also argued that there is a possible violation of the Prevention of Insider Trading ('PIT Regulations'). In future, even if Hindenburg's investigative findings are proven to be correct, then they would effectively assume the role of insiders, as they would gain access to 'unpublished price-sensitive information'. Regulation 2(n) of PIT Regulation defines 'unpublished price-sensitive information' as any information not in the public domain and, if revealed, could significantly influence the prices of securities.<sup>101</sup> This assumption of an insider role by Hindenburg could occur if and when they obtained non-public information through their investigative efforts. This information would be considered 'unpublished price-sensitive information' under the PIT Regulations.

Subsequently, engaging in trading based on such privileged information would breach regulations under the PIT Regulations, specifically Regulation 3 prohibiting insider trading,<sup>102</sup> Regulation 4 imposing restrictions on communication and trading by insiders,<sup>103</sup> and Regulation 5 mandating disclosure of trading by insiders.<sup>104</sup> Violations of these regulations can lead to severe penalties, including fines, disgorgement of profits, and even imprisonment in certain cases,<sup>105</sup> depending on the severity of the breach and the circumstances involved.

On the other hand, if their allegations are unsubstantiated, the act of disseminating unfounded claims about a specific entity would amount to market manipulation, thereby contravening the PFUTP Regulations.<sup>106</sup> The convergence of active short selling with the public disclosure of their investigation findings represents a fusion of conflicting roles,<sup>107</sup> a scenario that could have detrimental effects on the stability and overall integrity of financial markets.

Therefore, apart from transgressing the market's underlying logic and principles regarding short sales, the act of Hindenburg publishing investigation findings pertaining to Adani Group of companies runs contrary to the fundamental principles and intent of the SEBIRA and IA Regulations. Additionally, adopting an activist investigative approach as short sellers violate the PFUTP Regulations read with the SEBI Act, 1992, and possibly the PIT Regulation, as shown above.

---

<sup>101</sup> The Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015, Regulation 2(n).

<sup>102</sup> *Id.*, Regulation 3.

<sup>103</sup> *Id.*, Regulation 4.

<sup>104</sup> *Id.*, Regulation 5.

<sup>105</sup> The Securities and Exchange Board of India Act, 1992, §15G.

<sup>106</sup> The Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003, Regulation 4.

<sup>107</sup> Aviraj Pandey, *supra* note 86.

## B. EXTRA-TERRITORIAL JURISDICTION OF SEBI

The preceding arguments unequivocally establish that Hindenburg has violated the existing securities laws in India, irrespective of the accuracy of the report's claims. This thereby provides the SEBI with legitimate grounds to initiate legal proceedings against a research organisation based in the USA. The foundational principle governing the territorial application of laws enacted by the Indian Parliament is outlined in Article 245 of the Constitution of India.<sup>108</sup> Article 245(1) establishes the widely acknowledged presumption that laws formulated by a nation are inherently bound by its territorial confines.<sup>109</sup> However, Article 245(2) of the Constitution introduces a crucial exception, asserting that laws passed by the Parliament under Article 245(1) cannot be deemed void solely due to potential extraterritorial implications.<sup>110</sup>

The regulations allegedly violated by Hindenburg indeed fall within the ambit of provisions marked by extraterritorial enforceability. A similar perspective is reflected in §1(3) of the Foreign Exchange Management Act, 1999, ('FEMA') that explicitly outlines provisions for its extra-territorial application.<sup>111</sup> In comparison, the SEBI Act, 1992, lacks an analogous provision. Nevertheless, the SEBI has effectively exercised its authority to formulate regulations under §30 leading to the creation of several regulations marked by the distinctive trait of extraterritorial enforceability.<sup>112</sup> These distinctive traits in SEBI's regulations primarily revolve around their ability to govern and regulate activities involving Indian securities even when conducted outside India. They empower SEBI to oversee and take action against entities, domestic or foreign, involved in activities that may impact the integrity of the Indian securities market, regardless of where these actions originate. This means that SEBI can assert its jurisdiction and enforce its regulations on individuals or entities outside India if their actions have a bearing on the Indian securities market.

These distinctive traits grant SEBI the necessary authority and flexibility to maintain the integrity and stability of the Indian financial system in an increasingly interconnected global market. Further, the actions of Hindenburg including publishing a research report and engaging in short selling activities, which potentially influenced Indian securities, align with the scope of SEBI's extraterritorial regulations. This establishes the grounds for SEBI to initiate legal proceedings against Hindenburg, emphasising the extraterritorial enforceability of the relevant provisions.

---

<sup>108</sup> The Constitution of India, 1950, Art. 245.

<sup>109</sup> *Id.*, Art. 245(1).

<sup>110</sup> *Id.*, Art. 245(2).

<sup>111</sup> The Foreign Exchange Management Act, 1999, §1(3).

<sup>112</sup> The Securities and Exchange Board of India Act, 1992, §30.

While Article 245 of the Indian Constitution primarily deals with laws made by the Parliament, a pertinent question arises concerning the applicability of Article 245 to delegated legislations, such as regulations formulated by SEBI. Delegated legislations, including SEBI regulations, often derive their authority from the parent statute, in this case, the SEBI Act, 1992. The SC, in the case of *St. Johns Teachers Training Institute v. NCTE*,<sup>113</sup> has established that regulations framed under powers conferred by the parent statute hold the same force and effect as an Act passed by the competent legislature.<sup>114</sup> Applying this principle, delegated legislations framed by SEBI could potentially fall within the purview of Article 245 if they have a real and substantial nexus with India. This underscores the complexity of the legal framework surrounding SEBI's extraterritorial regulations and their potential alignment with constitutional provisions.

In this part, the paper examines SEBI's extra-territorial jurisdiction and its legal underpinnings. Subsequently, it delves into the nexus test, which scrutinises the criteria for SEBI's jurisdiction. Afterward, it investigates the effect doctrine test and its significance in protecting Indian investors. Finally, the paper explores the mechanisms for enforcing SEBI's orders against entities operating outside India's borders. Collectively, these sub-parts provide a comprehensive insight into SEBI's extra-territorial jurisdiction and its strategies for enforcement.

## 1. Nexus Test

The SC in a landmark case of *GVK Industries v. ITO*,<sup>115</sup> analysed the Parliament's legislative authority under Article 245, and held that enacting legislation concerning extraterritorial matters or causes lacking a substantial connection to India would signify a significant evasion of parliamentary responsibility.<sup>116</sup> Hence, for a law with extraterritorial implications to hold validity, it must meet the nexus test, requiring a genuine and tangible connection.<sup>117</sup>

For instance, let us consider a hypothetical scenario involving a foreign company that operates in India but is headquartered in another country. If this foreign company engages in fraudulent activities that harm Indian investors, the Indian authorities may seek to apply Indian securities regulations to hold the company accountable. In this case, the 'nexus' or connection between the foreign company's actions and India's interests is evident. The activities directly impact Indian investors and the integrity of the Indian financial market. Therefore, Indian authorities would be justified in invoking extraterritorial jurisdiction to address the wrongdoing, as it satisfies the nexus test by demonstrating a clear link between the foreign company's actions and India's legal and economic interests. This

---

<sup>113</sup> (2003) 3 SCC 321.

<sup>114</sup> *Id.*, ¶10.

<sup>115</sup> (2011) 4 SCC 36.

<sup>116</sup> *Id.*, ¶¶59-61.

<sup>117</sup> *Id.*, ¶¶4-5.

illustration highlights that the nexus test is essential in determining whether a law's extraterritorial application is legitimate and justifiable. It ensures that laws with international implications are not applied arbitrarily but are based on a genuine connection to the country seeking to enforce them beyond its borders.

Further, in the case of *Pan Asia Advisor v. SEBI*,<sup>118</sup> ('Pan Asia Advisor') the SC reaffirmed the legal capacity of the SEBI to prosecute individuals absent from India's territorial jurisdiction. This assertion was founded on §11(3) of the SEBI Act, 1992, that empowers SEBI to gather relevant information for investigations related to securities transactions, irrespective of any conflicting provisions in other legal statutes, such as the FEMA and the Reserve Bank of India Act, 1934.<sup>119</sup> Regarding the fulfillment of nexus test with respect to extra-territorial application of SEBI rules and regulations, the SC reaffirmed the SEBI Act's efficacy in dealing with individuals engaged in fraudulent activities that detrimentally impact the interests of Indian investors.<sup>120</sup> The court reached this conclusion by affirming that Parliament has the authority to legislate for matters impacting India or its interests, even if they have extraterritorial aspects.<sup>121</sup>

The SEBI Act, 1992, along with the Securities Contracts (Regulation) Act, 1956,<sup>122</sup> and the Depository Receipt Mechanism Scheme, 1993,<sup>123</sup> were found to empower legal actions against those engaging in fraudulent activities that detrimentally affect Indian investors, in line with the 'nexus test' requiring a genuine connection to India.<sup>124</sup> This legal basis supported the court's conclusion regarding the SEBI Act's effectiveness in addressing such fraudulent activities. Additionally, the court concluded that SEBI is within its legal authority to pursue individuals located outside India if their actions undermine the nation's lawful interests.<sup>125</sup> This underscores the notion that safeguarding the well-being of Indian investors establishes a valid 'nexus with India,' thereby allowing SEBI to initiate legal proceedings even in cases where the actions occur beyond the geographical confines of India.

In examining the Hindenburg Research situation, it becomes evident that their actions have significant implications within the Indian regulatory landscape. Hindenburg's strategic short selling, coupled with the publication of their research reports, represents a direct challenge to the principles outlined in the SEBI regulations. Their report on the Adani Group, while potentially lacking substantial evidence, managed to erode investor confidence and prompt market

<sup>118</sup> 2015 SCC OnLine SC 626 ('Pan Asia Advisor').

<sup>119</sup> The Securities and Exchange Board of India Act, 1992, §11(3).

<sup>120</sup> *Pan Asia Advisor*, *supra* note 118, ¶96.

<sup>121</sup> *Id.*

<sup>122</sup> The Securities Contracts (Regulation) Act, 1956, §12A.

<sup>123</sup> S.S. Khakase et al., *Global Depository Receipts in India: Boon or Bane*, 2021, available at <https://financetp.fa.ru/jour/article/download/1325/872> (Last visited on October 8, 2023).

<sup>124</sup> *Pan Asia Advisor*, *supra* note 118.

<sup>125</sup> *Id.*, ¶¶97-113.

volatility. By holding short positions prior to releasing the report, Hindenburg stood to profit from the ensuing market downturn, thus raising ethical concerns and suspicions of market manipulation.

These actions directly contravene the RA Regulations, the IA Regulations, the PFTUP Regulations, and even the PIT Regulations, as discussed earlier. Such violations, in effect, create a tangible and direct nexus between Hindenburg's actions and the interests of Indian investors. SEBI's jurisdiction extends to ensuring the integrity and stability of the Indian securities market, even when activities originate beyond India's borders. Therefore, based on the protection of Indian investors and the preservation of market integrity, SEBI possesses legitimate grounds to initiate legal proceedings against Hindenburg Research for their actions, as they directly impact the well-being and confidence of Indian investors in the securities market.

## 2. Effect Doctrine Test

The SC in *Haridas Exports v. All India Float Glass Manufacturers' Assn.*,<sup>126</sup> analysed the 'effects doctrine' test and scrutinised its applicability within the context of the Monopolies and Restrictive Trade Practices Act, 1969 ('MRTP Act'). The court affirmed that if a transaction conducted outside India led to a restrictive trade practice within the country, the MRTP Commission could exercise its jurisdiction to issue relevant orders.<sup>127</sup>

Although the MRTP Act is no longer in force, the lasting relevance of the 'effects doctrine' was validated through its application in the Pan Asia Advisor case.<sup>128</sup> This emphasised that SEBI maintains extraterritorial jurisdiction when transactions carry substantial implications for Indian investors.<sup>129</sup> While discussing the 'effect doctrine,' it is crucial to note that not all valuation losses lead to substantial implications. The threshold for significance varies, considering factors such as loss magnitude, market importance, and impact on investors. The 'effect doctrine' does not replace the restrictive trade practice test but complements it by considering broader effects on the Indian market. It remains relevant despite the MRTP Act's absence, indicating that actions abroad can affect India, justifying regulatory intervention. The threshold for substantial implications depends on specific circumstances and case consequences.

Consequently, SEBI possesses the authority to prosecute Hindenburg for trade transactions conducted in the USA, as analysts' reports can significantly

<sup>126</sup> 2002 SCC OnLine SC 652.

<sup>127</sup> *Id.*, ¶46.

<sup>128</sup> Pan Asia Advisor, *supra* note 118, ¶111.

<sup>129</sup> Bharat Vasani & Varun Kannan, *Extra-Territorial Application of India's Securities Law – Has SEBI Cast its Net too Wide?*, July 28, 2021, available at <https://corporate.cyrilamarchandblogs.com/2021/07/extra-territorial-application-of-indias-securities-law-has-sebi-cast-its-net-too-wide/#:~:text=Effects%20doctrine,for%20Indian%20investors> (Last visited on October 8, 2023).

impact a company's stock price when widely disseminated through various media outlets, potentially influencing investors to adjust their trading decisions accordingly.<sup>130</sup> The same was observed when Hindenburg released their report, as the value of Adani group of companies dropped considerably, from INR 19.18 lakh crore to just INR 7.15 lakh crore, amounting to a total decrease in value of INR 12.02 lakh crore.<sup>131</sup>

In conclusion, the 'effect doctrine' is a pivotal concept for SEBI's extraterritorial jurisdiction, allowing it to assert authority over actions conducted abroad when they have substantial consequences within the Indian market. While not all valuation losses automatically trigger this jurisdiction, it hinges on factors such as loss magnitude, market significance, and investor impact. Hindenburg's report on Adani companies serves as a practical example of this doctrine's relevance, highlighting SEBI's authority to address such cases. The 'effect doctrine' remains vital for safeguarding Indian investors in a global market.

### 3. Mechanisms for the Enforcement of Order by the Sebi Against The Hindenburg

The central issue now pertains to as to how the SEBI would take action against Hindenburg. The *first* option is to go through International Organization for Securities Commission ('IOSCO') to which both India and the USA are a part of. It is a worldwide body that connects securities regulators to set industry norms.<sup>132</sup> Back in May, 2002, IOSCO members entered into an agreement to cooperate and share information, aiming to ensure compliance with their respective laws and rules.<sup>133</sup> Nevertheless, despite having a structured plan, the real enforcement of SEBI's order remains uncertain due to conflicts in domestic laws and other challenges.<sup>134</sup>

---

<sup>130</sup> The US Securities and Exchange Commission, *Analysing Analyst Recommendations*, August 30, 2010, available at <https://www.sec.gov/about/reports-publications/investor-publications/analyzing-analyst-recommendations#:~:text=Research%20analysts%20study%20publicly%20traded,or%20sector%20of%20the%20economy> (Last visited on October 8, 2023).

<sup>131</sup> Yash Sadhak Shrivastava, *One Month of Hindenburg Report – Adani Shares Fall Close to Short Sellers' Value Target; What Next?*, February 24, 2023, available at <https://www.financialexpress.com/market/one-month-of-hindenburg-report-adani-shares-fall-close-to-short-sellers-value-target-what-next/2991492/> (Last visited on August 12, 2023).

<sup>132</sup> The International Organization of Securities Commissions, *Enhanced Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and The Exchange of Information*, 2016, available at <https://www.iosco.org/about/?subsection=emmou> (Last visited on August 12, 2023).

<sup>133</sup> *Id.*

<sup>134</sup> Khushboo Tiwari & Samie Modak, *Global Body IOSCO Flags Challenges to Operational Independence*, February 16, 2023, available at [https://www.business-standard.com/article/markets/iosco-flags-operational-independence-risks-at-five-global-regulators-123021601053\\_1.html](https://www.business-standard.com/article/markets/iosco-flags-operational-independence-risks-at-five-global-regulators-123021601053_1.html) (Last visited on August 12, 2023).



Further, it is crucial to delve deeper into the identified regulatory challenges. These challenges vary by jurisdiction due to differing market conditions and regulations. Achieving uniform regulatory standards globally is complex, with challenges in enforcement, information sharing, and coordination.<sup>135</sup> To address this, a framework for cross-border cooperation is needed. The varying market complexities require high-level regulatory guidance empowering market intermediaries to exercise judgment. Measures include information barriers, effective procedures, record-keeping, and stringent penalties for non-compliance.<sup>136</sup> Overcoming these challenges is vital for market integrity and investor protection.

The *second* option for SEBI is to utilise Mutual Legal Assistance Treaties ('MLATs') to prosecute Hindenburg. It has been clearly established that they have committed an offence by releasing the report under PIT and PFUTP Regulations, with the cooperation of the SEC. An illustrative instance is the existing MLAT between India and the USA, which encourages cooperative endeavors between their respective law enforcement agencies in the investigation and prosecution of criminal activities, including those related to securities and financial fraud.<sup>137</sup> This accord establishes a structured framework for the exchange of information and evidence during criminal investigations and legal proceedings. Both nations' law enforcement agencies have the authority to request assistance from each other, which includes activities like sharing evidence, delivering legal documents, and obtaining witness testimonies.<sup>138</sup>

The MLAT significantly bolsters the efficacy of criminal investigations and nurtures collaborative initiatives in addressing global transnational crimes. It is essential to understand that the utilisation of MLATs is governed by strict legal and procedural prerequisites, and there exists multiple challenges stemming from legal, practical, and political elements.<sup>139</sup> From a legal standpoint, the strict prerequisites and variations in legal systems between countries can lead to complex and time-consuming processes. For example, the requirement of dual criminality, where the offense under investigation must also be a crime in the requested country, can hinder cooperation, especially in cases like corruption, where definitions may differ.<sup>140</sup>

---

<sup>135</sup> The International Organization of Securities Commissions, *Complaint Handling and Redress System for Retail Investors*, 23, FR01/2021, January, 2021, available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD670.pdf> (Last visited on August 12, 2023).

<sup>136</sup> *Id.*

<sup>137</sup> Treaty between the Government of the United States of America and the Government of the Republic of India on Mutual Legal Assistance in Criminal Matters, (U.S. and India), October 17, 2001.

<sup>138</sup> Faraz Alam Sagar et al., *Understanding Cross Border Legal Assistance*, October 29, 2020, available at <https://corporate.cyrilamarchandblogs.com/2020/10/understanding-cross-border-legal-assistance/> (Last visited on August 12, 2023).

<sup>139</sup> *Id.*

<sup>140</sup> *Id.*

On a practical level, the execution of MLAT requests can face obstacles related to procedural delays, the absence of designated central authorities, and appeals by individuals targeted by the requests, leading to significant delays in providing necessary evidence. The political dimension is also crucial, as some countries may be reluctant to act against their own citizens, introducing diplomatic challenges. This reluctance may pose difficulties in cases involving individuals or entities from countries with strong diplomatic ties. While MLATs have the potential to facilitate international cooperation in legal matters, it is important to recognise these challenges and address them to ensure the effective implementation of this mechanism. The author advocates for MLATs as a means to foster cooperation and establish a formalised process for mutual legal assistance, despite these obstacles, aiming for a more reliable and predictable framework for international legal cooperation.

If SEBI takes a legal action against Hindenburg, then initiating such legal measures could yield a dual advantage: *first*, sanctioning wrongdoers and *second*, recovering their illicit gains, while also affording investors the possibility to pursue compensation for the harm inflicted. Nonetheless, the cooperation between SEBI and SEC assumes paramount importance here. There have been instances where both these organisations collaborated effectively on a matter. One such example occurred in 2011 when the SEC brought charges against five India-based affiliates of Price water house Coopers in connection with the Satyam accounting fraud.<sup>141</sup> The audit deficiencies identified in the work of these PW India affiliates extended beyond the Satyam case, revealing broader quality control issues within PW India.<sup>142</sup> In a settlement with the SEC, the PW India affiliates agreed to pay a USD 6 million penalty,<sup>143</sup> which stands as the largest penalty ever imposed on a foreign-based accounting firm in an SEC enforcement action. Therefore, by utilising MLAT, SEBI could formally approach SEC to temporarily freeze Hindenburg's assets and subsequently proceed with asset forfeiture, till the verification of their report.

While the world of short selling and the potential pitfalls it presents have been highlighted in this part of the paper, the need for a robust regulatory response and investor safeguards becomes evident. The after-effects of Hindenburg's actions serve as a stark reminder of the consequences that unscrupulous market activities can have on investors, both individual and institutional. The significant decline in the value of Adani's entities demonstrated the real-world impact of distorted market information and the role it plays in the decisions investors make. In light of this turmoil, the next part of the article delves into the crucial issue of

---

<sup>141</sup> The U.S. Securities and Exchange Commission, *SEC Charges India-Based Affiliates of PWC for Role in Satyam Accounting Fraud*, April 5, 2011, available at <http://www.sec.gov/news/press/2011/2011-82.htm> (Last visited on August 12, 2023).

<sup>142</sup> *Id.*

<sup>143</sup> *Id.*

investor protection and the regulatory framework that should be in place to safeguard the interests of investors against market volatility.

#### IV. INVESTOR-PROTECTION FRAMEWORK: PROTECTING INVESTORS FROM SHARE-MELTDOWN

In the aftermath of the Adani-Hindenburg saga, the SC in February called for the protection of investors against market volatility and ordered SEBI to maintain stable securities market to protect the interest of Indian investors.<sup>144</sup> Meanwhile, the court also asked the authority to lay down the existing regulatory framework to protect Indian investors, which includes a wide spectrum of the middle class who reportedly lost lakhs of crores following a meltdown in the Adani Group shares.<sup>145</sup>

The SEBI, in its note, laid down the three key pillars of investment protection:

1. Adequate disclosures made by listed enterprises, with all investors having equal opportunity to access such information, enabling well-informed investment choices;
2. An efficient market system that guarantees smooth trade and settlement processes, encompassing measures to manage market fluctuations; and
3. Implementation of enforcement measures in instances of market misconduct, encompassing fraudulent activities or breaches of SEBI regulations.<sup>146</sup>

The Apex Court, based on the submissions, set up an expert committee to assess the existing regulatory framework and to make recommendations to strengthen the same.<sup>147</sup> In this part of the paper, the authors analyse such a framework on the basis of the aforementioned pillars and propose additional measures aimed at enhancing safeguards for Indian investors against share market downturns.

---

<sup>144</sup> Prakash Gupta v. SEBI, (2021) 17 SCC 451, ¶99; *See also*, Adani Gas Ltd. v. Union of India, (2022) 5 SCC 210.

<sup>145</sup> Vishal Tiwari (Adani Group Investigation) v. Union of India, (2023) 4 SCC 332.

<sup>146</sup> *Id.*, ¶5.

<sup>147</sup> Vishal Tiwari v. Union of India, (2023) 4 SCC 332, ¶¶13, 14; *See generally*, Aneesa Mathur, *Adani Hindenburg Row: SC Sets Up Six-Member Expert Committee Headed by Former Justice AM Sapre*, March 2, 2023, available at <https://www.businesstoday.in/latest/corporate/story/adani-hindenburg-row-sc-sets-up-six-member-expert-committee-headed-by-former-justice-am-sapre-371968-2023-03-02> (Last visited on August 20, 2023).

## A. ENFORCEMENT MEASURES: FRAUD, MARKET MISCONDUCT, AND BREACH OF SEBI REGULATIONS

§11B of the SEBI Act, 1992, grants SEBI the authority to provide directions in the favor of investors and to avert activities that could harm the interests of investors or the securities market.<sup>148</sup> As outlined by SEBI, actions such as insider trading, deceptive trading practices, and unethical professional behavior are highly damaging to the welfare of regular investors and are strongly deprecated under the SEBI Act, 1992.<sup>149</sup>

Such activities include scalping, rumour fraud/puffing advertisements, front running/back running, circular trading, pump and dump scheme, and, Ponzi scheme, among others. To illustrate, in the rebuttal by Adani Group, the Group refuted the report, terming it as a “malicious combination of selective misinformation and stale, baseless and discredited information”, calling the conduct of Hindenburg as “market misconduct and nothing short of a calculated securities fraud.”<sup>150</sup>

The PFUTP Regulations read with the SEBI Act, prohibits any person from indulging in any manipulative, fraudulent, or unfair trade practices in the securities market.<sup>151</sup> SEBI levied monetary penalties of INR 7273.13 crore in total during 2015-2016 on the entities in violation of the PFUTP regulations, making the regulations an effective tool to protect investors against manipulations and unfair trade practices.<sup>152</sup>

Further, as the authors claimed the alleged possibility of ‘insider trading’ in the case of Hindenburg, the investor may resort to the PIT Regulations, which aim to curb insider trading in securities.<sup>153</sup> Regulation 3 restricts the director of the entity from dealing in securities of the company, on the basis of any unpublished price-sensitive information available to them, any violation of the same amounts to market abuse and falls under the ambit of insider trading.<sup>154</sup>

<sup>148</sup> The Securities and Exchange Board of India Act, 1992, §11B.

<sup>149</sup> Samir C. Arora v. Securities and Exchange Board of India, 2004 SCC OnLine SAT 90, ¶6.

<sup>150</sup> Adani Group, *Adani Response to Hindenburg*, January 29, 2023, available at <https://www.adani.com/-/media/Project/Adani/Invetsors/Adani-Response-to-Hindenburg-January-29-2023.pdf> (Last visited on August 20, 2023).

<sup>151</sup> The Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003, Regulation 4(k).

<sup>152</sup> Dr. Gaddam Naresh Reddy, *Fraudulent Financial Practices and Investor Protection in the Indian Capital Market – Role of SEBI*, OSMANIA UNIVERSITY, October 10, 2015, available at <https://www.osmania.ac.in/UGC%20MRP%20final%20Reports2018/FFP%20AND%20IPPROJECT%20FINAL%20REPORT.PDF> (Last visited on August 20, 2023).

<sup>153</sup> The Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015, Regulation 4.

<sup>154</sup> *Id.*, Regulation 3.

However, the regulatory framework in India lacks preventive measures, despite having punitive measures in curbing fraudulent activity. Theoretically, apart from improving risk assessment and awareness, the SEBI, in association with the Central Bureau of Investigation and Serious Fraud Investigation Office, must work to identify the fraud and punish the accused, and to recover money investors lost in such fraudulent activity.<sup>155</sup> Further, in cases where fraudulent activity is committed by any foreign entity, the ambit of the PFUTP regulations must be broadened to cover such entity, if such fraudulent activity harms the interests of the Indian investors. SEBI, in order to prevent any fraudulent activity, can introduce exemplary monetary compensation and may confer power on the National Company Law Tribunal subject to judicial review to determine penalties.

The authors propose that the preventive measures along with punitive measures can be extended to any kind of financial irregularities and market manipulation, not merely limited to short-sellers. The reliance can be placed on the SEC's order to impose penalty of USD 180 million on Luckin Coffee for "intentionally and materially" overstating its revenue.<sup>156</sup> The ordered penalty was more of an exemplary nature in absence of any effective mechanism to hold foreign issuers accountable to the same extent as USA issuers, to ensure public issuers accessing USA markets does not provide false or misleading information to investors.

## *B. SMOOTH TRADE AND SETTLEMENT PROCESS: MANAGING MARKET FLUCTUATIONS*

The SC-appointed expert committee, while investigating the volatile effect on the Adani Group stocks, concluded that since the representation of Adani Group in major India equity indices is relatively minor, such recent events did not pose any systemic market-level risk and the market remained largely stable and resilient.<sup>157</sup> However, the obvious fallout of the Hindenburg report has been a loss of confidence in the Adani Group and put investors' trust in doubt. Therefore, a need for a mechanism is required in order to shield investors from Adani-type volatility.

First, the SEBI utilises a circuit breaker mechanism during significant downward and upward shifts in the market.<sup>158</sup> This mechanism allows investors extra time to pause, assess the information driving price fluctuations, and reconsider their stance.<sup>159</sup> A circuit breaker is described as a "mechanism that momentarily halts ongoing trading in one or multiple securities or contracts, due

<sup>155</sup> DR. REDDY, *supra* note 152.

<sup>156</sup> Press Release, LUCKIN COFFEE AGREES TO PAY \$180 MILLION PENALTY TO SETTLE ACCOUNTING FRAUD CHARGES, December 6, 2020, available at <https://www.sec.gov/news/press-release/2020-319> (Last visited on October 7, 2023).

<sup>157</sup> THE SUPREME COURT OF INDIA, *Report of the Expert Committee*, 57 (May 6, 2023).

<sup>158</sup> Latha Chari et al., *Market Wide Circuit Breaker, Trading Activity and Volatility: Experience from India*, Vol. 46(1), PRAJNAN: JOURNAL OF MANAGEMENT AND SOCIAL SCIENCES, 43 (2017).

<sup>159</sup> Stefano Alderighiet al., *Circuit Breakers and other Market Safeguards*, WORLD FEDERATION EXCHANGE, 4 March 2021, available at <https://www.world-exchanges.org/storage/app/media/>

to a market factor surpassing certain predetermined thresholds”.<sup>160</sup> The SEBI, in its circular dated January 12, 2015, strengthened the existing mechanism of Index based market-wide circuit breaker mechanism.<sup>161</sup> This is the most effective mechanism to protect investors, in cases of market volatility.

*Second*, SEBI also introduced a suggestion akin to SEC’s limit up-limit down, with the aim of enhancing the construction of price bands for securities and to enhance the control of volatility and decrease information imbalances in the market.<sup>162</sup> The proposal suggests that if a stock within the futures and options segment experiences a daily increase or decrease of more than twenty percent, a gradual implementation of a one-hour pause period can be enforced.<sup>163</sup> Subsequently, such a security would be allowed to advance by a maximum of two percent, as opposed to the existing threshold of five percent.<sup>164</sup> This adjustment could serve as a significant instrument to manage excessive market volatility and help restrict the daily price fluctuation of the security.<sup>165</sup>

*Third*, SEBI should understand that similar reports such as Hindenburg can do considerable damage to the normal functioning and behaviour of the market. Therefore, an expedited and quick verification of such reports shall be of utmost importance. To this effect, SEBI came up with the amendment to Regulation 30 read with Schedule III of the SEBI (Listing Obligations and Disclosure Requirements) (Second Amendment) Regulations, 2023, through which it introduced the mandatory requirement to confirm, deny, or clarify market rumours on the top 100 listed entities from October 1, 2023, and extends to the top 250 listed entities from April 1, 2024.<sup>166</sup>

Such mandatory requirements to accept, deny or clarify, will allow the investors to make informed decisions and may tilt the market sentiment in favour of the entity. However, even though an entity may clarify and issue expedited verification of such reports, the authors understand that the same shall require to

---

Circuit%20breakers%20taxonomy%20paper%20March%202021.pdf (Last visited on August 20, 2023).

<sup>160</sup> *Id.*, 7.

<sup>161</sup> The Securities and Exchange Board of India, *Index Based Market-Wide Circuit Breaker Mechanism*, January 12, 2015, available at [https://www.sebi.gov.in/legal/circulars/jan-2015/index-based-market-wide-circuit-breaker-mechanism\\_28855.html](https://www.sebi.gov.in/legal/circulars/jan-2015/index-based-market-wide-circuit-breaker-mechanism_28855.html) (Last visited on August 20, 2023).

<sup>162</sup> The Securities and Exchange Board of India, *Consultation Paper on Price Band Formulation for Scrips in Equity Derivatives Segment to Strengthen Volatility Management and Minimise Information Asymmetry*, May 20, 2023, available at [https://www.sebi.gov.in/reports-and-statistics/reports/may-2023/consultation-paper-on-price-band-formulation-for-scrips-in-equity-derivatives-segment-to-strengthen-volatility-management-and-minimise-information-asymmetry\\_71443.html](https://www.sebi.gov.in/reports-and-statistics/reports/may-2023/consultation-paper-on-price-band-formulation-for-scrips-in-equity-derivatives-segment-to-strengthen-volatility-management-and-minimise-information-asymmetry_71443.html) (Last visited on August 20, 2023).

<sup>163</sup> *Id.*, ¶6.1.3.4.1.

<sup>164</sup> *Id.*

<sup>165</sup> *Id.*, ¶¶2, 3.

<sup>166</sup> The Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) (Second Amendment) Regulations, 2023, Regulation VIII.

be verified from the regulator as well considering the impact the report can have on the investors. Thereby, such disclosures will also comply with the foremost pillar of investment protection with which the authors will deal in the next sub-part.

### C. *DISCLOSURES BY LISTED ENTERPRISES: ENABLING INFORMED INVESTMENT CHOICES*

The Hindenburg report accused Adani Group of stock price manipulation, for falsely overinflating the value of their assets, and controlling seventy-five percent of its shares through different offshore shell entities, terming it as a “brazen stock manipulation and accounting fraud”. The authors are not commenting on the veracity of the accusations. However, even if any of them are correct, should not the Adani Group disclose the same, so that investors could have made informed investment choices?

Regulation 30 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, requires every listed entity to make disclosure of any events or information, which is material as well as price-sensitive information.<sup>167</sup> Further, in accordance with the accounting standards Ind AS 24,<sup>168</sup> and AS 18,<sup>169</sup> entities are required to disclose related-party transactions in the annual report of the entities. However, reportedly, Adani failed to disclose related-party transactions with three offshore entities.<sup>170</sup>

Moreover, in recent times, SEBI has introduced a consultation document aiming to enforce more comprehensive revelations from high-risk Foreign Portfolio Investors (‘FPIs’). This category has been utilised as a method to bypass regulatory prerequisites, such as maintaining the minimum public shareholding obligation.<sup>171</sup> This came after the SEBI could not find beneficial owners of some foreign portfolio investments in Adani stocks, seen as a move towards circumventing regulatory requirements by the Adani Group.

<sup>167</sup> The Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, Regulation 30.

<sup>168</sup> Ministry of Corporate Affairs, *Indian Accounting Standard (Ind AS) 24 – Related Party Transactions*, available at [https://www.mca.gov.in/Ministry/pdf/Ind\\_AS24.pdf](https://www.mca.gov.in/Ministry/pdf/Ind_AS24.pdf) (Last visited on August 20, 2023).

<sup>169</sup> Ministry of Corporate Affairs, *Accounting Standard (AS) 18 – Related Party Disclosures*, available at [https://www.mca.gov.in/Ministry/notification/pdf/AS\\_18.pdf](https://www.mca.gov.in/Ministry/notification/pdf/AS_18.pdf) (Last visited on August 20, 2023).

<sup>170</sup> The Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, Schedule V.

<sup>171</sup> Securities and Exchange Board of India, *Consultation Paper on Framework for Mandating additional disclosures Foreign Portfolio Investors (FPIs) that fulfil certain objective criteria, to 1) guard against possible circumvention of Minimum Public Shareholding (“MPS”), and 2) to guard against possible misuse of the FPI route to circumvent the requirements of Press Note 3 (“PN3”)*, May 31, 2023, available at [https://www.sebi.gov.in/reports-and-statistics/reports/may-2023/consultation-paper-on-framework-for-mandating-additional-disclosures-from-foreign-portfolio-investors-fpis-that-fulfil-certain-objective-criteria-to-1-guard-against-possible-circumvention-of-minim-\\_71946.html](https://www.sebi.gov.in/reports-and-statistics/reports/may-2023/consultation-paper-on-framework-for-mandating-additional-disclosures-from-foreign-portfolio-investors-fpis-that-fulfil-certain-objective-criteria-to-1-guard-against-possible-circumvention-of-minim-_71946.html) (Last visited on August 20, 2023).

Reportedly, in the aftermath of the Adani-Hindenburg saga, the SEBI is also considering making India's conglomerates report transactions involving their unlisted group companies as well, therefore, expanding the scope of disclosures required from listed enterprises.<sup>172</sup>

Irrespective of the fact that whether Adani Group made all disclosures, the SEBI is actively working towards enhancing disclosure requirements of the listed enterprises, in addition to the accounting standards and listing obligations. Further, the authors propose that SEBI should collaborate with educational institutions to launch initiatives that educate investors about abusive short selling and its repercussions to ensure that investors make informed investment choices.

## V. CONCLUSION

While the Hindenburg report is under investigation by SEBI, this incident has brought to light the deficiencies in India's securities regulatory framework. It has showcased how investor trust can be undermined quite effortlessly in this age of digitalisation. The rise of influential voices in the financial space, such as Hindenburg, has raised concerns about the integrity of information and the potential impact on investor trust, affecting their decisions leading to potential market distortions.

Such proliferation of misleading information can lead to a credibility crisis for financial experts, analysts, and institutions. If investors lose faith in the expertise and accuracy of these sources, it becomes challenging to differentiate between reliable advice and speculative claims, further undermining trust. In India, SEBI plays a pivotal role in safeguarding investor trust and maintaining the integrity of the financial markets, particularly in situations where reports similar to the Hindenburg case could potentially shake investor confidence.

The initial hurdle involves establishing a rapid-response system within the purview of market regulators. When a manipulative trading strategy becomes public, the stock exchange should take immediate control over trading activities involving the specific stock in question. SEBI should possess the capability to assess the potential consequences of these reports and temporarily halt trading of the affected stocks for a defined duration. Nonetheless, the execution of such a framework is expected to be a challenging undertaking, given the persistent circulation of dubious and manipulative recommendations within the stock market.

Furthermore, there is a requirement for a structured framework that facilitates international collaboration, allowing various nations to collectively implement corrective measures. It is crucial to address the potential challenge of

---

<sup>172</sup> *Adani Probe Wraps up as India Tightens Disclosure for Big Firms*, THE HINDU, August 14, 2023, available at <https://www.thehindubusinessline.com/companies/adani-probe-wraps-up-as-india-tightens-disclosure-for-big-firms/article67192927.ece> (Last visited on August 20, 2023).



jurisdiction effectively, ensuring that market regulators and countries can globally tackle this issue in a coordinated manner.

The current framework of SEBI works on three key pillars of investment protection, the foremost being the disclosure by all listed enterprises. However, the same is not accessible to the public. Further, SEBI must ensure efficient market system, which it failed to do during Adani-Hindenburg Saga that led to a substantial reduction in market capitalisation, resulting in the erosion of billions of dollars from the targeted stocks.

Calling it a classic case of ‘corporate espionage’, the authors expressly intend that regulatory bodies must establish robust legislation that effectively addresses the concerns of investors who suffer losses due to misinformation propagated by third-party interventions. While laws already exist for suing companies that provide deceptive or misleading information, such as presenting inflated profits or misrepresenting financial data, there is a need for an extended legal framework to promptly address manipulative trading strategies. It is vital to recognise that those behind such reports may harbour ulterior motives aimed at disrupting the market for personal gains.

Developing such a legal framework is crucial in instilling investor confidence and ensuring a prioritised mechanism for addressing their grievances when confronted with dubious reports. Additionally, regulatory authorities must emphasise the importance of educating investors about the existence and potential impact of such misleading reports and publications. This collective effort would raise awareness among investors, encouraging them to make investment decisions based on verified sources rather than relying on uncorroborated reports.

In conclusion, the paper underscores the necessity for a comprehensive legal framework that guards against deceptive practices and safeguards investor interests. Furthermore, education and awareness initiatives must be a focal point for regulatory bodies to empower investors with the knowledge needed to make well-informed decisions and, consequently, strengthen the overall integrity of the financial markets.