Whether India Needs a Super Regulatory Body

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Abstract: In India there are multiple financial market regulatory bodies and recently there was conflict between the Securities and Exchange Board of India and the Insurance Regulatory and Development Authority. This issue regarding jurisdiction between IRDA and SEBI puts a question before us to think whether India requires a mega-regulatory body? In India High Level Coordination Committee on Financial Markets is working but recently we have seen that it has not been satisfactory to resolve the dispute between SEBI and IRDA. Therefore, the author suggests to constitute a separate body so as to prevent the jurisdictional conflict between regulatory bodies. The objective of the paper is to identify whether India needs a mega-regulatory body or the multiple regulatory system is one of the best solutions. The writer has adopted qualitative methodology to find out the truth. The author is opined that the multiple regulatory systems exist in India which have created certain jurisdictional problems. For better presentation of the subject the author has to answer the following questions i.e. how jurisdictional problems arising among regulatory bodies may be resolved? and whether Mega-regulatory system in India may be considered as a good solution to avoid jurisdictional issues?

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1. Introduction

Where there is multiple-jurisdiction, conflict is bound to take place. In India there are multiple financial market regulatory bodies and recently we have seen the conflict between SEBI (to be called the Securities and Exchange Board of India) and IRDA(to be called the Insurance Regulatory and Development Authority). This issue regarding jurisdiction between IRDA and SEBI puts a question before us to think whether India requires a mega-regulatory body? In India High Level Coordination Committee on Financial Markets is working but recently we have seen that it has not been satisfactory to resolve the dispute between SEBI and IRDA. Therefore, the author suggests to constitute a separate Commission i.e. FMRCI (to be called Financial Market Regulatory Commission of India) in place of HLCCFM (to be called the High Level Coordination Committee on Financial Markets). Subject to the provisions of any law made by Parliament, the conditions of service and tenure of office of the Chairman of FMRCI and of other two Members shall be such as the President may by rule determine; Provided that the Chairman of FMRCI shall not be removed from his office except in like manner and on the like grounds as a Judge of the Supreme Court and the conditions of service of the Chairman of FMRCI shall not be varied to his disadvantage after his appointment: Provided further that other two Members shall not be removed from office except on the recommendation of the Chairman of FMRCI.

2. Financial Market Regulatory Bodies:

In India in relation to financial market several regulatory bodies are playing different role. Such regulatory bodies have been mentioned below.

i. Securities and Exchange Board of India (SEBI)
ii. Insurance Regulatory and Development Authority(IRDA)
iii. Reserve Bank of India(RBI)
iv. Telecom Regulatory Authority of India(TRAI)
v. Competition Commission of India (CCI)

i. Securities and Exchange Board of India (SEBI)

SEBI is the regulator for the Securities Market in India. Before SEBI the securities markets were regulated according to the provisions of Securities Contracts (Regulation) Act, 1956. Harshad Mehta Scam case compelled the Parliament to establish a new and separate body to regulate the Securities Market. It was formed officially by the Government of India in 1992 with SEBI Act 1992 being passed by the Indian Parliament. Chaired by C B Bhave, SEBI is headquartered in the popular business district of Bandra-Kurla complex in Mumbai, and has Northern, Eastern, Southern and Western regional offices in New Delhi, Kolkata, Chennai and Ahmedabad. SEBI's power has been mentioned under Section 55A of the Companies Act, 1956 as well as Securities Laws (Amendment) Act, 1999 and Securities Laws (Amendment) Act, 2004 give other power under Securities Contracts (Regulation) Act.

ii. Insurance Regulatory and Development Authority(IRDA)

The Insurance Regulatory and Development Authority (IRDA) is a national agency of the Government of India, based in Hyderabad. It was formed by an act of Indian Parliament known as IRDA Act 1999, which was amended in 2002 to incorporate some emerging requirements. The object of IRDA as stated in the Act is "to protect the interests of the policyholders, to regulate, promote and ensure orderly growth of the insurance industry and for matters connected therewith or incidental thereto." Section 14 of IRDA Act, 1999 lays down the duties, powers and functions of IRDA.

iii. Reserve Bank of India

The Reserve Bank of India is the central bank of India and controls the monetary policy of the rupee as well as 287.37 billion US-Dollar (2009) currency reserves. The institution was established on 1 April 1935 during the British-Raj in accordance with the provisions of the Reserve Bank of India Act, 1934 and plays an important part in the development strategy of the government.

iv. Telecom Regulatory Authority of India(TRAI):

The Telecom Regulatory Authority of India or TRAI is the independent regulator established by the Government of India to regulate the telecommunications business in India. It was established in 1997.

v. Competition Commission of India (CCI):

The Competition Commission of India has been established under the provisions of The Competition Act, 2002.

Objective of CCI:

An Act to provide, keeping in view of the economic development of the country, for the establishment of a Commission to prevent practices having adverse effect on competition, to promote and sustain competition in markets, to protect the interests of consumers and to ensure freedom of trade carried on by other participants in markets, in India, and for matters connected therewith or incidental thereto. In case of anticompetitive agreement within the meaning of Section 3 of The Competition Act, 2002 and if it affects the competition, the Competition Commission of India is empowered to take initiative.

3. Conflict Of Jurisdiction Between Irda And Sebi

Directions issued by SEBI under Sections 11 and 11B of the Securities and Exchange Board of India Act, 1992 read with Section 12(1B) on 9 April, 2010.

By this direction SEBI prohibited 14 insurance companies not to issue any offer document.

Before considering the issues involved in the matter, I refer to the relevant provision of the SEBI Act. Section 12(1B) of the SEBI Act provides as under:

"No person shall sponsor or cause to be sponsored or carry on or caused to be carried on any venture capital funds or collective investment schemes including mutual funds, unless he obtains a certificate of registration from the Board in accordance with the regulations."

The question that arises for my consideration is whether ULIPs offered by the said entities are a combination of investment and insurance and if so whether the investment components are in the nature of mutual funds which can only be offered/launched after obtaining registration from SEBI under section 12(1B) of the SEBI Act? To carry out the purposes of sections 11 and 12(1B), SEBI has framed various regulations including the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996 and the Securities and Exchange Board of India (Collective Investment Scheme) Regulations, 1999. The SEBI Act and the regulations made thereunder are also special laws made/laid before the Parliament and any investment product or investment contract having any characteristic of securities or exposing investors to securities market risks is under the jurisdiction of SEBI under the SEBI Act. I find that in terms of section 12(1B) of the SEBI Act "no person" can sponsor or cause to be sponsored a collective investment scheme including a mutual fund unless he has been registered with SEBI under the SEBI Act. Therefore, an entity which is not established in the form of a trust cannot launch or offer an investment product in the nature of mutual fund without being registered with SEBI.

However, the said entities have not obtained any certificate of registration from SEBI though the ULIPs launched by them had an investment component in the nature of mutual funds, as mandated by section 12(1B) of the SEBI Act. It is, therefore, necessary to restrain the entities mentioned in para 1 of this order from raising further monies/subscription, new and/or additional, from the investors for any product (including ULIPs) having an investment component in the nature of mutual funds till they obtain registration from SEBI. Accordingly, in exercise of the powers conferred upon me by virtue of section 19 of the SEBI Act read with sections 11, 11B and 12(1B) thereof, I hereby direct the entities mentioned in para 1 of this order not to issue any offer document, advertisement, brochure soliciting money from investors or raise money from investors by way of new and/or additional subscription for any product (including ULIPs) having an investment component in the nature of mutual funds, till they obtain the requisite certificate of registration from SEBI.

Proceedings of the Chairman, Insurance Regulatory and Development Authority of India (IRDA)

This proceeding is undertaken in relation to the order issued by SEBI. The IRDA Act, 1999 is specifically enacted to provide for an Authority to protect the interests of holders of insurance policies, to regulate, promote and ensure the orderly growth of the insurance industry and for matters connected therewith or incidental thereto. The mentioned direction of the SEBI to insurance companies not to raise money by way of new or additional subscription apart from other restrictions will seriously jeopardize and adversely the interests of the policyholders and the interests of the insurers.

The IRDA, in the light of the above, is satisfied that the order of the SEBI mentioned above will bring the insurance industry to a standstill which would not be in public interest and would be detrimental to the interests of the policyholders and prejudicial to the interests of the insurers.

Therefore, in exercise of the powers vested in the Authority under Section 34(1) (a) and (b) of the Insurance Act, 1938 , and after due consultation with the members of the Consultative Committee , all the 14 insurance companies which are mentioned in the order of SEBI are directed to note that notwithstanding the said Order of the SEBI, they shall continue to carry out insurance business as usual including offering, marketing and servicing ULIPs in accordance with the Insurance Act, 1938, Rules, Regulations and Guidelines issued there-under by the IRDA.

Mega-regulatory Body Working in UK

The Financial Services Authority (FSA) is an independent non-governmental body, quasi-judicial body and a company limited by guarantee that regulates the financial services industry in the United Kingdom. Its board is appointed by the Treasury. Financial services includes Financial services refer to services provided by the finance industry. The finance industry encompasses a broad range of organizations that deal with the management of money. Among these organizations are banks, credit card companies, insurance companies, consumer finance companies, stock brokerages, investment funds and some government sponsored enterprises.

In the UK, which has opted for a single super-regulatory model, each of the specialised areas of operation is headed by persons who, for all practical purposes, function like regulators of their respective areas. There are a few managing directors, each in charge of one aspect. But it needs to be stated that if a scandal were to hit the UK's financial services market, the House of Commons will ask for the head of Sir Howard and not of his deputies. I point this out specifically, for this is the crux of the concept of the single regulator. In UK “"coordination and avoidance of friction is done through mutual consultations and wherever necessary through the intervention of the 'boss' and/or the board of the regulatory body, cannot be expected if we continue with the existing fragmented regulatory structures.

In an article in The Guardian (November 30, 2001), the FSA's powers were summed up. It also gave the perception of each segment. A perusal of this summation will indicate how useful such an organisation could be for our financial services industry.

(1) Four new objectives: maintaining confidence in the financial system; promoting public understanding of the financial system; securing the appropriate degree of protection for consumers; reducing financial crime.

(2) For the first time, there is a responsibility to the consumer of financial products and for teaching them about the products they are buying, and protecting them.

(3) It has powers to tackle money laundering and is able to prosecute financial firms for failure to maintain stringent controls.

(4) Powers to fight" market abuse", which is defined in three ways: misuse of information; creating false or misleading impressions; market distortion. The regulator will be able to issue public censure or impose an unlimited fine on anyone, who breaks the rules, whether or not it is an authorised firm.

(5) Powers to fine a company or company director for breaking the 'listing rules' with which all stock market listed firms must comply.

(6) An independent Lord Chancellor's Tribunal, which can hear any disputed case from scratch, the counter-balance to FSA's new authority, preventing it from imposing fines unfairly.

(7) A single compensation scheme and single ombudsman to consider representations from consumers.

4. Pros And Cons Of Single And Multiple Regulators

The usual argument in favour of a single regulator is that the financial sector is an integrated whole and a single regulator can avoid the emergence of possible conflicting regulations that different regulators frame keeping primarily their jurisdictional area in view. Since a number of important players in the financial system are operating in multiple areas that fall within the jurisdiction of more than one regulator they are likely to face many avoidable problems.

Commercial banks, for example, are increasingly assuming roles that stretch across the

traditional boundaries of commercial banking. When one of their customers wants to raise funds from the market either by way of equities or debt instruments, banks would like to play a supportive role by taking up activities such as underwriting o f the issue or acting as banker to the issue. The concerned bank Will have to be in conformity with all the public issue guidelines framed by SEBI. Or the bank itself may be a listed company and hence subject to the listing guidelines, which contain several provisions that have also some bearing on RBI regulations. For example, corporate governance require-ments as stipulated in the listing agreement signed with the stock exchange may have to be in conformity with relevant RBI regulations for commercial banks. The bank will not be in a position to play an effective role in the capital market areas unless the regulations of SEBI and RBI are non-conflicting. Several such examples could be cited as to how a number of important players in the financial system get subjected to the jurisdiction of more than one regulator. Besides RBI and SEBI, we have today one more regulator in the IRDA. Shortly we will have the pension regulator. When different regulators frame their regulations to meet the fast changing needs of the financial sector it is possible that there could be several areas of conflict. Hence it is being suggested that a single regulator on the lines of the UK will help in resolving the problems arising from multiple independent regulators. However, the problem is not as simple as it appears and the single regulator solution may create new problems.

There are good reasons why it may not be appropriate to concentrate too many powers in any single authority unless there are overriding justifications for it. A single regulator may not always view the problem from different dimensions and from the viewpoint of different players in the financial system. Those who argue in favour of a single super-regulator should be able to provide strong justifications for setting up such a body. They should also provide a convincing argument that there is a grave risk to the financial system and that a sound financial system cannot be built up in the absence of a single regulator. The only strong argument in favour of a super-regulator is that it is possible to avoid the framing of conflicting regulations by different regulators or ensure mechanisms for quick resolution of the unanticipated conflicting regulations when they come to light.

The Indian financial sector is getting increasingly deregulated and it is also being opened to foreign players. It is felt that a single monolithic regulatory organisation may not be nimble and quick enough to respond to the continuous changes that are taking place. Further, for the regulations to become effective and purposeful for each of the areas under its jurisdiction the super-regulatory body needs to ensure that a high level of area-wise expertise and specialisation is built up within the organisation. While the conflicts between two independent regulators may be fully visible to the market players, the same may not necessarily happen to an equal extent in the case of two deputy regulators. There is therefore no reason to believe that a super-regulatory organisation is a more effective solution for resolving problems that may be faced by the market players and institutions when regulations are framed for widely different and specialised activities such as banking, insurance and the securities market. It is not correct to argue that problems arising from egos of different independent regulators could be better resolved if all of them are brought under the single umbrella of a super-regulatory body. These problems relating to friction and conflicting regulations may continue with undiminished intensity even under a single regulatory body. It may not necessarily be a matter of ego if one of the independent regulators sincerely believes that the other regulator has not fully appreciated all the nuances of his regulations. Such differences in perceptions may be genuine and not necessarily due to ego problems. To sum up, creation of single super-regulator may be viewed as an amalgamation of different regulators into a single organisation. The results of such an amalgamation should lead to value addition in the process. In other words, the whole should be more than merely a sum of the parts.

Financial sector players may also face problems with other authorities as a result of conflicts between other laws and regulations framed by their regulators. Merely because there are possibilities of avoidable frictions due to conflicting regulations of different regulators or laws administered by other authorities, it is not convincing to argue in favour of bringing all such authorities and regulators under one roof.

At present 13 economies have opted for a single 'super' regulator. At the heart of the current debate in Germany's planned financial sector reforms is the proposal for the creation of a single independent regulatory authority that would continue the tasks currently performed by three separate organisations, for stock markets, banks and insurance. They have realised the 'need for one all-compassing regulator'. Australia's Wallis Report also recommended a single authority.

5. Why Indian Financial Market Needs A Single Regulator?

Financial Market needs a single regulator due to conflicts among regulators. For e.g. the conflict between SEBI and IRDA is going on in relation to ULIP. Single or mega-regulator may regulate all the financial regulators.

The growing complexity of financial markets and the growth of financial conglomerates has placed an enormous strain on the existing system with multiple and often overlapping' regulatory and supervisory structures. Many economists and financial experts are stressing the need for a single or unitary regulator not only to achieve economies of scale, but to improve the financial market functioning by avoiding issues relating to jurisdiction. In the recent past, in several instances these issues have played a major role. For example:

(1) When listed companies were changing their names to resemble those of techno-logy companies at the height of the dotcom boom, it was not clear which regulator would be responsible - SEBI or Company Affairs (Registrar of Companies).

(2) When banks were lending money to brokers beyond permissible limits once again there was a lack of clarity between the RBI and SEBI4 and the SEBI felt that it was entirely the RBI's responsibility.

(3) The recent conflict which is going on between IRDA and SEBI in relation to ULIP.

RBI former deputy governor, Y V Reddy has emphasised the need to review the Indian regulatory frame-work, though he feels that there is no point in creating new bureaucracies. He has proposed an umbrella regulatory legislation, creating an apex regulatory authority without disturbing the existing jurisdiction, with the governor of the RBI as its chairman and with the three regulatory chiefs as its members.

Narasimham Committee Report:

Narasimham Committee II recommended in 1998 that an integrated system of regulation and supervision be put in place to regulate and supervise the

78 activities of banks, financial institutions and NBFCs with a body called Board for Financial Regulation and Supervision (BFRS).

Khan Working Group:

In view of the increasing overlap in the functions being performed by various participants in the financial system, the Khan Working Group had explicitly recommended in April 1998 the establishment of a super-regulator to supervise and coordinate the activities of the multiple regulators, in order to ensure uniformity in regulatory treatment to different entities.

Global Scenario:

The current international thinking on the subject of regulation suggests that the only way to effectively supervise the financial system of a country is to have a single regulator for all financial services. Only then will the regulator be able to take a holistic view of the risk the financial entity is bearing. The current international thinking on the subject of regulation suggests that the only way to effectively supervise the financial system of a country is to have a single regulator for all financial services. Only then will the regulator be able to take a holistic view of the risk the financial entity is bearing. World over, a trend towards national integrated regulators or 'super regulators', covering deposit-taking and other financial activities such as insurance, pensions and/or securities dealers, is emerging. Canada, the UK, Sweden, Norway, Den-mark, Australia, Mexico, Japan and Hungary have adopted the 'super regulator' concept and it has also been considered for relatively smaller nations like Korea, Singapore and Latvia. World over, a trend towards national integrated regulators or 'super regulators', covering deposit-taking and other financial activities such as insurance, pensions and/or securities dealers, is emerging. Canada, the UK, Sweden, Norway, Den-mark, Australia, Mexico, Japan and Hungary have adopted the 'super regulator' concept and it has also been considered for relatively smaller nations like Korea, Singapore and Latvia.

Benefits of Single Regulator:

Streamlined regulatory oversight by a single regulator may be viewed as a mechanism to deliver more effective and efficient supervision at a lower cost. This can happen in a number of ways. A single regulatory body is in a better position to provide diversified financial groups with better coordinated and more consistent supervision based on a single, rationally constructed set of principles and rules. Goodhart, Taylor and others (1997) have argued that there is a clear need for consolidated regulation of financial conglomerates as there may be "risks arising within the group that are not adequately addressed by any of the specialist prudential supervisory agencies that undertake their work on a solo basis"

Challenges in Single Regulator:

Bringing together existing supervisory agencies is a difficult task, in terms of both organisational structures as well as human resources. A strong 'change management' process and the creation of a new organisational structure is needed for the effective integration of human resources.

Conclusion & Suggestions

In India the single regulatory body cannot be adopted as it has been adopted in UK because in UK the Financial Services Authority regulates the banks, credit card companies, insurance companies, consumer finance companies, stock brokerages, investment funds and some government sponsored enterprises. But in India a separate Commission can be established which can exercise the jurisdiction only when there is jurisdictional conflict among the regulatory bodies. Therefore, according to the writer

there is a need to establish Financial Market Regulatory Commission of India (FMRCI) consisting of one Chairman and two members.

Appointment and removal of Chairman and Members of Financial Market Regulatory Commission of India (FMRCI):

Subject to the provisions of any law made by Parliament, the conditions of service and tenure of office of the Chairman of FMRCI and of other two Members shall be such as the President may by rule determine; Provided that the Chairman of FMRCI shall not be removed from his office except in like manner and on the like grounds as a Judge of the Supreme Court and the conditions of service of the Chairman of FMRCI shall not be varied to his disadvantage after his appointment: Provided further that other two Members shall not be removed from office except on the recommendation of the Chairman of FMRCI.

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