THE SCOPE AND LIMITS OF SEBI'S REGULATORY POWER UNDER SECTIONS 11 AND 11B OF THE SEBI ACT, 1992

Retail Participation Restriction in India's Derivatives Market

by

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1. Introduction and Problem

Retail participation in India's equity futures and options (F&O) market has grown sharply, helped by digital platforms, easier broker access and lower costs. The growth has brought heavy losses. SEBI's January 2023 analysis found that 89 per cent of individual F&O traders lost money in 2021-22, and a later study covering 2021-22 to 2023-24 found that 93 per cent lost money over three years, with aggregate losses above ₹1.8 lakh crore.

In response, SEBI changed contract sizes, expiry-day products, option premium collection, margins and position limits during 2024-25. None of these prohibits retail trading, but several raise the cost of entry. The central legal question is whether measures framed as investor protection can curtail access to an otherwise lawful market. SEBI's authority comes from Sections 11 and 11B of the SEBI Act, 1992, and Section 11(4)(b) allows it to restrain specific persons from the market. The 2024-25 measures, however, apply to retail investors as a class, not to identified wrongdoers.

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The study asks not whether retail F&O trading is desirable, but whether SEBI's approach lies within its statutory powers and balances protection with access. Article 19(1)(g), which protects the freedom to carry on a trade or business subject to reasonable restrictions under Article 19(6), adds a constitutional side.

2. Research Design

Questions. The study asks: (1) what is the statutory scope of Sections 11 and 11B, and how did the 1995 and 2002 amendments shape it; (2) can a general power to protect investors restrict retail participation market-wide, and where does regulating how people participate end and restricting whether they can begin; (3) how have the courts and the Securities Appellate Tribunal (SAT) set the limits; (4) do the 2024-25 measures meet reasonableness and

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proportionality under Articles 14 and 19(1)(g); (5) were circulars, rather than Section 30 regulations, a sound instrument; and (6) what can India learn from other jurisdictions.

Hypothesis. SEBI's power is wide but bounded by the objects of the Act and by Articles 14 and 19(1)(g). SEBI can regulate how retail investors participate, through margins, position limits and risk controls, but cannot impose class-wide structural restrictions that in effect shut them out unless the measure is clearly linked to investor protection, is proportionate and is adopted through a reasoned process. Each measure is expected to be within SEBI's authority, but their combined effect and the use of circulars is expected to raise a real question of proportionality and legality.

Method, gap and scope. The study is doctrinal with comparative analysis, drawing on the SEBI Act, the Securities Contracts (Regulation) Act, 1956 (SCRA), circulars, the Constitution, judgments, and secondary literature. No survey was conducted. The gap is that existing work debates whether the curbs are desirable or effective but rarely asks the prior question of statutory authority under Sections 11 and 11B. The scope is equity derivatives, mainly 2023-2025, and selected foreign jurisdictions.

Literature. Committee reports, notably the Shah Committee (2001) and the Sodhi Committee (2014), expose weaknesses in earlier regulation and the need to balance enforcement with fairness. Scholarship (Bose 2005; Uppal and Kumar 2007; Picciotto 2017; van Driel 2019; Gupta 2025) covers regulatory discretion, speculation and fraud, and Salve and Rajepandhare (2024) address the tension between curbing speculation and preserving participation. None asks how far Sections 11 and 11B stretch.

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3. Background

SEBI's powers. SEBI was set up on 12 April 1988 as a non-statutory advisory body, and its weakness was exposed by the Harshad Mehta scam of 1991-92. The SEBI Act, 1992 then gave it statutory status and a threefold mandate: to protect investors, promote the securities market and regulate it. Section 11B, inserted in 1995, lets SEBI issue binding directions without prior Central Government approval. The 2002 amendment added Section 11(4), with interim measures such as restraining persons from the market. Courts read Sections 11 and 11B as one composite power, with Section 11 supplying the object and Section 11B the tool of directions.

Derivatives and retail growth. After the L.C. Gupta and J.R. Varma Committees (1998), Parliament amended the SCRA in 1999 to treat derivatives as securities, and trading began in

June 2000. Retail participation then surged from 2018, driven by discount brokers and weekly expiries. Individuals' share of index-options turnover rose from about 2 per cent to around 41 per cent by March 2024.

SEBI's response. SEBI's study for 2024-25 found that about 91 per cent of individual traders were in loss, with aggregate losses up about 41 per cent to about ₹1.05 lakh crore. After a consultation paper of July 2024, SEBI announced six measures on 1 October 2024: a higher minimum contract size (from about ₹5 lakh to ₹15-20 lakh); one weekly expiry per exchange; upfront option premium; removal of calendar-spread benefit on expiry day; an extra 2 per cent extreme loss margin on expiry day; and intraday monitoring of position limits. Circulars in 2025 fixed expiry days and added entity-level intraday position limits. Active individual options traders fell from about 4.4 million in September 2024 to about 3 million in March 2025, then rebounded above 3.2 million by October 2025. All measures were issued as circulars under Sections 11(1) and 11B, without new legislation.

4. Legal Framework

Sections 11 and 11B. Section 11(1) makes it SEBI's duty to protect investors and to promote and regulate the market 'by such measures as it thinks fit'; the functions in Section 11(2) are illustrative, and Section 11(4) adds interim tools. The power is preventive, not punitive, depends on SEBI's own satisfaction (reviewable for arbitrariness) and covers both individual and market-wide action. Section 11B permits directions to exchanges, intermediaries and persons associated with the market where necessary in the interest of investors or for the orderly development of the market. Courts treat the market as a single system, so directions to exchanges are a legitimate way to protect investors even where the effect falls on traders. SEBI is given deference for its expertise, but mala fides, absence of material or gross disproportion can still invalidate its action.

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The instrument question. SEBI can act through regulations under Section 30, which are laid before Parliament, through directions under Section 11B, or through circulars. The 2024 measures took the last form, for speed. Whether a circular can validly introduce a measure of this scale, without parliamentary laying, has not been judicially tested. The counter-view is that requiring regulations for every market-structure change would cripple SEBI's ability to respond quickly.

Procedure and appeal. For market-wide measures, SEBI substituted public consultation, an expert working group and the Secondary Market Advisory Committee, which matches the

administrative-law standard for delegated legislation. Appeals lie to the SAT under Section 15T, but only against an order passed against a person, so a circular addressed to exchanges would be challenged by writ under Articles 226 and 32.

5. Constitutional Perspective

Article 19(1)(g). A higher contract size or fewer expiries restricts trading and must be a reasonable restriction in the public interest under Article 19(6). Reasonableness depends on whether the evidence of loss justifies restrictions on all retail traders rather than only those trading imprudently. An occasional speculator may not be carrying on a trade at all, but the study assumes Article 19(1)(g) applies, since professional traders are affected too.

Article 14. The measures are neutral on their face, but their burden falls mainly on small traders, and the Act sets no threshold of risk that must be crossed before the power is used. Courts have upheld broad standards such as 'interest of investors', so this challenge is comparatively weak.

Proportionality. Modern Dental College v. State of Madhya Pradesh (2016) adopted a four-part test: legitimate purpose, rational connection, necessity (no equally effective, less restrictive alternative) and balance between benefit and burden, and K.S. Puttaswamy (2019) applied the same structure. The necessity limb is where the 2024-25 measures are most exposed.

Paternalism. Critics say capable adults may take informed speculative risks, so uniform entry barriers are paternalistic. Defenders point to leverage, behavioural biases and the scale of household loss. The gambling analogy (Chamarbaugwalla, 1957, places gambling outside Article 19(1)(g)) is hard to sustain because the SCRA, since 1999, declares exchange-traded derivatives valid and not wagering contracts.

6. Comparative Perspective

Jurisdictions fall into two clusters. The first restricts the product for all retail investors. The EU's ESMA, under Article 40 of MiFIR, imposed leverage limits from 30:1 to 2:1 on contracts for difference in 2018; the UK made similar rules permanent and added an appropriateness test. Australia's ASIC made a product intervention order under Section 1023D of the Corporations Act, effective 29 March 2021, and found that retail CFD losses fell by about 91 per cent, then renewed it in 2022 for five years. The second cluster screens the investor: the United States uses tiered options approval by brokers and is replacing its Pattern Day Trader capital threshold with real-time intraday margin; Singapore and Hong Kong require knowledge and experience

assessments; and China requires experience, net assets and an examination before options trading.

SEBI's measures belong to the first cluster, but use contract value and expiry design and do not distinguish a novice from an experienced investor. Peer jurisdictions generally use dedicated product-intervention powers with renewal periods and formally notified instruments, whereas India relies on a general power exercised by circular, with no sunset. All rely on quantified evidence of retail loss, as SEBI did. Australia's review gave a clear result, while India's data are ambiguous. The two techniques can be combined, as the UK does. In India the displacement risk is towards unregistered finfluencer schemes and unlicensed platforms.

7. Judicial Response

Breadth of the power. In Sahara India Real Estate Corp. Ltd. v. SEBI (2012) 10 SCC 603 the Supreme Court described SEBI's powers as having 'no prearranged limits' and upheld a refund direction under Section 11B. SEBI v. Rakhi Trading (2018) confirmed that exchange-traded derivatives are within SEBI's reach. The Gujarat High Court in SEBI v. Alka Synthetics said SEBI must be able to meet unforeseen situations in a speculative market, and the SAT in Sterlite Industries held Section 11B preventive.

Limits. Anand Rathi v. SEBI (Bombay High Court, 2002) allows ad interim orders without prior hearing if an effective post-decisional hearing follows, but cautions that the power is not 'unrestricted, unchannelled and unguided'. In every case the person before the court had violated the Act, and none considered a general measure affecting all retail participants. The 2025 Jane Street proceedings, in which SEBI impounded ₹4,843.57 crore, concern individual enforcement and do not test the structural measures.

Review of regulatory measures. Courts defer to expert economic regulation (Peerless, BALCO, Swiss Ribbons), and in Vishal Tiwari (2024) the Supreme Court stressed that its entry into SEBI's domain is narrow. Yet deference weakens when a regulator changes the conditions of a lawful activity for everyone. Cellular Operators Association v. TRAI (2016) struck down a regulation for lack of data showing a rational relation to the harm, and Internet and Mobile Association of India v. RBI (2020) accepted the RBI's power but set aside its virtual currency circular as disproportionate, because no harm to regulated entities was shown and less restrictive options existed. SEBI's position is stronger, but the argument on less restrictive alternatives remains open. The case law is generous on power and reticent on limits.

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8. Analysis of the 2024-25 Measures

Power. The measures sit on a scale. First-level measures are conventional risk tools (margins, extreme loss margin, upfront premium, position limits), whose legality is unlikely to be disputed. Second-level measures change product design (higher contract value, limited expiries) and need a proportionality justification. Third-level measures, conditioning access on investor characteristics such as net worth, have not been adopted and would need clearer statutory backing. Since millions still trade, the measures regulate the manner of participation and do not exclude a class.

Purpose and evidence. The purposes fall within the Act, and SEBI's loss studies are a far stronger foundation than the RBI had in IMAI. But the evidence is better on the existence of harm than on the fit of the response. The studies do not show that any particular measure will reduce losses, and the 2024-25 study cannot test the measures, which were phased in between November 2024 and April 2025. The first year that can be judged is 2025-26. The trader-number rebound suggests the effect was partly temporary.

Proportionality. Legitimate purpose and rational connection are likely satisfied. Necessity is the exposed point, since the same contract value applies to a first-time trader and an experienced investor although suitability testing, volatility-based leverage limits or disclosure tools were available. SEBI has fair answers: suitability testing depends on brokers who earn from volume, and disclosure had not reduced losses. The higher contract value is the most exposed measure. On balancing, the benefit is likely to outweigh a moderate burden, since no one is excluded. The Article 14 challenge is weak, because capacity to bear risk is rationally related to protecting those who cannot.

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Process, instrument and 2025 measures. The consultation was elaborate, and the final framework was narrower than the July 2024 draft. Using circulars for measures that restructure a product indefinitely is a governance concern more than a question of legality, but there is no review requirement, sunset or published impact assessment. The 2025 entity-level position limits target positions only institutions can hold and are easier to justify. Each measure should state whether it serves market integrity or protects retail investors from their own losses.

Hypothesis. The power is wide, and it is bounded, but the limit has not been crossed. It would be reached by an effect amounting to exclusion of a class, a measure going to investor eligibility rather than product design, or lack of a demonstrated nexus with the harm. The first two are absent and the third is present in part. The measures are probably valid but not secure.

9. Findings, Recommendations and Conclusion

SEBI's power under Sections 11 and 11B is wide and preventive, extends to market-wide directions to exchanges, and is limited by its statutory objects, the need for material and the Constitution. The courts have defined its breadth but not its limit, and none has ruled on the derivatives circulars.

Recommendations. (1) Parliament should insert a dedicated product-intervention power (an illustrative Section 11BA), modelled on the EU and Australian provisions, requiring a written finding with evidence, consideration of less restrictive options, at least thirty days' consultation, regulations under Section 30 and a three-year sunset unless renewed after published review. (2) Section 15T should allow appeals to the SAT against directions of general application. (3) SEBI should adopt a published procedure and impact assessment for market-wide measures. (4) SEBI should consult on graded access to index options based on experience, financial capacity and an understanding test, with a pilot and review date. (5) The October 2024 measures should be reviewed on a full year of data including 2025-26, starting with the contract value. (6) SEBI should keep supervising finfluencers, and brokers should disclose client loss rates.

Conclusion.

A regulator that ignored such evidence of loss would not have done its duty, so the real question is whether SEBI should be required to act in a particular way when its action affects a large class that has done no wrong. Constitutional principle, comparative practice and case law suggest that it should. Evidence-based, consulted and reviewable measures protect investors, protect the regulator from challenge and preserve access to a lawful market. The framework should now supply the conditions that make SEBI's intervention reasoned, reviewable and proportionate to the freedom it affects.

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