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THE EXPERTS' VOICE

A COMPENDIUM OF ARTICLES

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To Regulate or not to Regulate: Finfluencers

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With the advent of social media, especially in the backdrop of digitization fueled by the COVID-19 pandemic lockdowns, in line with global trends, the community of *'influencers'* has proliferated across geographical and economic strata in the country. In the borderless world of social media, *'influencers'* through their content are seen to be influencing consumer habits and behaviours across a broad spectrum such as consumer products, education, trivia, and entertainment, including the financial markets - the last lot, notoriously labelled as *'finfluencers'*.

'Influencers' are, in essence, digital content creators with access to an audience and the power to affect their purchasing decisions at the back of their own knowledge, position, or relationship with the audience. By extension, *'finfluencers'* seem to have become unwitting albeit unregistered participants in products and services in the financial markets on matters like securities trading, investment advice, portfolio management, banking products, insurance, real estate investment, etc.

The menace of unregulated finfluencers came to the notice of the Securities and Exchange Board of India (SEBI) over the last several months based on complaints raised by aggrieved retail investors lured, trapped, and duped by finfluencers:

- claiming to be experts and leaders in the field and giving investment advice cloaked in educational courses related to trading and investing;
- to invest in specific stocks, promoted by such finfluencers at the behest of brokers or companies; and/or
- to participate in 'pump and dump' schemes.

While the finfluencers' kitty remains flush with payments accruing from referral charges, hits / promotional content, non-cash benefits, profit-sharing opportunities, etc., retail investors ostensibly suffer significant losses in the process.

SEBI Regulatory & Jurisprudential Framework

At present, under the umbrella of SEBI regulations, the recourse against false and misleading statements made by finfluencers, to induce investors to invest in securities markets, is not specifically provided for. Such contraventions are seen to be adjudicated through SEBI's

general powers under the provisions of the Securities and Exchange Board of India Act, 1992 (SEBI Act) read with certain provisions of the Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 (PFUTP Regulations) with reliance on Securities and Exchange Board of India (Investment Advisers) Regulations, 2013 (IA Regulations) and SEBI (Research Analyst) Regulations 2014 (RA Regulations) in relation to the scope of terms such as *'investment advice'* and *'research analysts'*. While these provisions do enable recourse against illegitimate finfluencer activities, the ever-increasing proliferation of finfluencers in the market warrants a more nuanced approach that addresses and regulates finfluencer activities specifically.

SEBI's investigations into and adjudication of *inter alia* stock recommendation and unregistered investment advisory activity in the matters of Sadhna Broadcast Limited, Sharpline Broadcast Limited, and Baap of Charts under the ambit of the legal framework referred above have led to relevant finluencers being held accountable through orders imposing securities trading ban, orders directing refund of money and/or compounding of money in bank accounts, orders directing cease and desist from acting as an investment advisor or engaging in any fraudulent activity, and/or orders directing withdrawal of public access of content in matters.

In the wake of these cases involving finfluencer contraventions, and following the Guidelines for Influencer Advertising in Digital Media released by the Advertising Standards Council of India (ASCI Guidelines), SEBI, in August 2023, introduced the:

- Consultation Paper on Association of SEBI Registered Intermediaries/ Regulated Entities with Unregistered Entities (including Finfluencers) to inter alia reduce the perverse incentives available to finfluencers by disrupting their revenue model (Consultation Paper 1); and
- Consultation Paper on Collection by SEBI Registered Investment Advisers and Research Analysts to create a closed fee collection ecosystem for SEBI registered investment advisers and research analysts (Consultation Paper 2).

This follows the guidelines and directives issued by SEBI and other bodies, towards the end of 2022 and early 2023, which appeared to be focused on restricting and regulating the participation of *'celebrities'* in advertisements made by SEBI registered intermediaries. Under these guidelines and directives, the term *'celebrity'* has been defined to include any person who is an influencer with more than 10 lakh followers/subscribers (per social media handle) on any social media platform that

includes but is not limited to YouTube, Instagram, Facebook, X (formerly known as Twitter), etc.

Regulation v Prohibition

In stipulating that registered finfluencers must display appropriate registration and contact details and make appropriate disclosures and disclaimers on any post, Consultation Paper 1 presupposes that some finfluencers might already be registered as SEBI intermediaries, however practically, that may not be the case. In fact, recent trends are to the contrary - finfluencers are reported to be taking SEBI registration number on rent from registered investment advisers to not fall foul of the ASCI Guidelines.

Further, while Consultation Paper 1 aims to limit the incentives finfluencers receive from SEBI registered intermediaries/regulated entities, the proposed measures fall short in that not all incentives to finfluencers come from SEBI registered intermediaries or regulated entities. For instance, compensation received by finfluencers directly from social media or other platform where they share their content would continue to remain accessible to them.

Furthermore, since SEBI is only trying to regulate what comes within its purview, the models which are used by the finfluencers which require no collaboration with anyone are still untouched such as giving deceitful advice under the guise of education - as was the case in the matter of Baap of Charts, where the finfluencer presenting himself as a stock market guru across multiple social media platforms, lured investors, and clients to join his 'educational courses.' Subscribers to these courses were subsequently invited into exclusive groups where they received buy-and-sell recommendations promising profits. These courses came with a fee, as well as a share in the users' profits.

The Consultation Papers appear to focus on compliance obligations on SEBI registered intermediaries to take active measures to dissociate themselves from unregistered entities. Whilst this would address a part of the issue, given the concerns discussed in the foregoing paragraphs, and in light of the eligibility criteria applicable to existing SEBI intermediary categories, it may be worthwhile for SEBI to introduce a separate category for finfluencers with specific eligibility criteria and disclosure and disclaimer requirements and consider narrowing the already available exemption for educational activities and knowledge sharing in the context of the above recommendation for a separate category and criteria for finfluencers.

Need for Clarity

Consultation Paper 1 refers to the definition of *'influencers'* as set out in the ASCI Guidelines which is considerably broad - *"someone having access to an audience and power to affect such audiences' purchasing decisions or opinions about a product, service, brand or experience, because of the influencer's authority, knowledge, position, or relation with their audience"*. While it is certainly not the intent, in drafting the relevant regulations, SEBI should consider specifically addressing and defining the term finfluencer so as to *inter alia* avoid any overlap or unintended exclusion of marketing agencies in the ordinary course and also clarifying the interplay between the terms *'finfluencer'* and *'celebrity'* as discussed above.

As per the IA Regulations, *'investment advice'* given through newspapers, magazines, any electronic or broadcasting, or telecommunications medium, which is widely available to the public shall not be considered as investment advice. With respect to regulating activities of the finfluencers, SEBI may consider amending this exception to be available finfluencers only subject to compliance with their disclosure and disclaimer requirements (such as including disclosure of proprietary trading interests, conflict of interests) as is the case of investment advisers.

The Consultation Papers appear to be silent on the potential consequences of non-compliance by SEBI registered intermediaries. For instance, at present, in case of non-compliance with the provisions of the IA Regulations, SEBI is entitled to issue directions at its discretion which may include restricting or altogether prohibiting operations for a specified time period and/or, requiring refund any money collected as fees, charges, commissions etc. Given the limited nature of additional compliances proposed in the Consultation Papers, SEBI could consider whether non-compliance of the provisions set forth in the Consultation Papers should be penalized in a similar manner.

Reporting Mechanism

Consultation Paper 1 stipulates that all SEBI registered intermediaries must take active measures to dissociate themselves from any

unregistered entity and report them to the concerned enforcement agency. Registered intermediaries are also directed to notify enforcement agencies to take appropriate action (including, by way of filing a criminal complaint for fraud under section 420 of the Indian Penal Code, 1860 (IPC)). Impersonation or fraud perpetrated by finfluencers, on or in connection with, registered intermediaries does not find a place within the SEBI Act or the relevant underlying regulations which is PFUTP Regulations. Accordingly, SEBI's mandate to registered intermediaries to take up these matters of impersonation or fraud through as criminal complaints under IPC are appropriate. This also appears to be in consonance with SEBI's direction to the Commissioner of Police, Delhi (in 2012) where it highlighted the need to sensitize officers manning the police stations about the grievance redressal mechanism already in place for dealing with complaints of civil nature against intermediaries.

The aforesaid, however, does not address any potential instances of manipulative, fraudulent, or unfair trade practices by and between finfluencers and retail investors. PFUTP Regulations, being a specific legislation and under a specific authority (i.e. SEBI) puts in place a mechanism pursuant to which retail investors can seek recourse from SEBI if and when the aforementioned issues arise - retail investors, in such cases, also would not need to rely on general criminal law for the enforcement of their complaints (provided SEBI sets up and actively addresses their complaints against such unregistered entities / finfluencers).

Further, while SEBI has introduced the SEBI Complaints Redress System (SCORES Platform) for lodging online complaints pertaining to securities market, this platform:

- is only available to retail investors (i.e., not SEBI registered intermediaries); and

- only enables complaints against listed companies and SEBI registered intermediaries (i.e., not unregistered entities).

SEBI to consider procedural changes such that complaints against finfluencer activities to the extent pertaining to securities trading can be communicated by anyone (including, SEBI registered intermediaries) with SEBI through an updated and robust SCORES Platform - this would discourage aggrieved retail investors against spam mailing various SEBI officials or tagging SEBI to posts on X (formerly known as Twitter).

Comprehensive Regulation

Last but definitely not the least, since finfluencers' activities are not restricted to securities markets and they also provide information and/or advice on other financial topics such as investing banking products, insurance, real estate investment, etc. their activities also bear relevance for other regulators such as the Reserve Bank of India (RBI), Insurance Regulatory and Development Authority of India (IRDAI) and Pension Fund Regulatory and Development Authority (PFRDA). Accordingly, in time, a more comprehensive framework to regulate finfluencer activities would be essential and may entail collaboration amongst various regulators.

Conclusion

SEBI's efforts in this direction are commendable and appear to be in line with global practices adopted to contain illegitimate finfluencer activities such as in the European Union and Australia. If implemented well, this could harken a regulatory framework for finfluencer activities as opposed to a prohibitory regime.