
SCAMS IN MUTUAL INVESTMENT AT CORPORATE SOCIETY: A LEGAL REGULATORY PERSPECTIVE

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ABSTRACT

Mutual funds are regulated by Securities and Exchange Board of India (SEBI). SEBI is the primary regulatory body to control and govern Securities market. Several, scams in mutual fund involves deceitful, misleading information & fraudulent activities by the insiders, agents, financial advisors and managers of mutual fund. Some of the major scams that have happened are Ponzi and pyramid scheme, fake platforms and mutual fund apps, unscrupulous advisors, risk misrepresentation, unauthorized transaction and scams by social media influencers. The impact of such financial scams includes destroying the reputation of the involved parties and potentially undermining the stability of the market as a result of the degraded confidence and participation of investors. On a broader socio-economic level, this could lead to misallocation of resources, financial instability and also can involve in reducing of economic productivity. Regulatory efforts have increased from agencies like SEBI in the form of improved disclosure norms, increased penalties and compliance efforts in order to protect investors and restore trust in the financial system. The need for impactful corporate governance, proactive regulatory frameworks and increased investor consideration in terms of scams in mutual funds and protecting the interests of the corporate society have been highlighted in the study. The mutual fund industry is governed by integrated regulatory framework provided by the SEBI, which plays a significant importance on investor welfare, market transparency and overall market quality. Mutual funds are also required to have fraud detection mechanisms in place for frauds, such as front-running, insider trading and unauthorized transactions. Furthermore, SEBI has strong oversight of asset management companies (AMCs) and requires them to have surveillance and compliance mechanisms in place.

Keywords: Mutual fund, scams, corporate society, SEBI (Securities Exchange Board of India, investors)

LIST OF ABBREVIATION

SEBI - Securities Exchange Board of India MF - Mutual Funds

AMC - Asset Management Company UTI - Unit Trust of India

LIST OF CASES

Shriram Mutual Fund v. Securities and Exchange Board of India, (2006) 5 SCC 361 SEBI v. Sahara India Real Estate Corporation Ltd, (2012) 10 SCC 603

SEBI v. Motilal Oswal Securities Ltd, (2015) 9 SCC 303 SEBI v. Axis Mutual Fund (2025)

LIST OF STATUTES

Securities and Exchange Board of India (SEBI) Act, 1992 SEBI (Mutual Funds) Regulations, 1996 (last amended 2025) Securities Contracts (Regulation) Act, 1956

Information Technology Act, 2000

Companies Act, 2013

INTRODUCTION:

A mutual fund is an easy way for many people to invest their money together and have experts invest that money in stocks, bonds, and other assets so that all can benefit from the profits and risks collectively. The mutual fund industry is regulated and controlled by the Securities and Exchange Board of India (SEBI), which acts as the major authority to control and regulate the securities market. However, many scams have been reported in the mutual fund industry based on deceitful and misleading information and through fraudulent activities performed by insiders, agents, financial advisors, and fund managers. Some of the major types of scams that have been reported in the mutual fund industry include ponzi and pyramid schemes, where investors are paid back through money received from new investors until all money is exhausted and the scam is discovered; false schemes and mutual fund apps that pretend to be real and authentic schemes and disappear once people have deposited their money; unethical financial advisors who mislead people for personal gain and offer to invest in schemes that benefit them instead of the people who have approached them for investment advice; risk representation

scams, where people are misled to believe that there is less risk involved in investing in a particular scheme and that it is very lucrative for them to invest in that scheme; unauthorized transactions, where money is moved and invested without the knowledge and consent of the people involved and is performed by insiders and hackers who use poor security systems to gain access to people's money; and scams performed by social media influencers, where people use their social status to gain personal benefits and lead many people astray through false and unethical means.^{1,2,3}

STATEMENT OF PROBLEMS:

Mutual fund scams occur when insiders and advisors misuse or mislead investors by consulting with confidential information, make unauthorized trades that directly exploit investor trust. and this research deals with the main centric issue of how the scams are conducted by the insiders and the core issue lies in whether SEBI's existing regulatory framework has sufficient strength to curb such scams, or if loopholes in regulations are enabling these fraudulent practices to continue. Another dimension to this issue is the growing use of technology in trading and fund management. While digital evolution in tech has brought efficiency, it has also opened new ways for fraudulent activities such as fake online platforms and misleading digital campaigns. Therefore, the debate extends beyond just insider misconduct to whether the regulatory monitoring SEBI is equipped with both legal authority and technological capability to detect and prevent such sophisticated scams in real time.

OBJECTIVES :

1. Analysis of scams that are affecting mutual investment schemes in corporate societies, and how do current SEBI regulations address those risks.
2. What are the primary challenges faced by regulatory authorities in investigating and prosecuting mutual investment scams within corporate societies.
3. Examination and complete overlook on the previous real – life mutual fund scams.

¹ Securities and Exchange Board of India Act, No. 15 of 1992, § 11, India.

² Securities and Exchange Board of India (Mutual Funds) Regulations, 1996, Gazette of India, Extra., pt. III, sec. 4 (June 5, 1996).

³ Sec. & Exch. Bd. of India, Investor Awareness and Protection Guidelines (various circulars & reports).

RESEARCH QUESTIONS:

1. How effective are SEBI's existing regulatory frameworks and guidelines in preventing, detecting, and addressing mutual fund scams within corporate societies?
2. What legal and structural loopholes are being exploited by insiders, advisors, and financial managers in corporate mutual fund investments, and how can regulatory reforms minimize these risks?

RESEARCH METHODOLOGY:

This research is based *qualitative doctrinal approach* on scams that are occurred by insiders and their misleading input given to the investors and how their trust on investing in mutual fund gets decreased and the different types of scams that are conducted in mutual fund investment sector and how that impacts on corporate society. Also analysis on the previous real - life mutual fund scams that have been conducted.

This research is completely relayed on Secondary sources and information gathered from different sites.

A qualitative doctrinal research methodology involves a rigorous, subjective analysis of existing legal principles and sources to interpret and synthesize legal doctrine. This method focuses on "black letter" law by examining statutes, case law, and legal literature to identify legal rules, principles, and their underlying theories, rather than empirical or factual data.

REVIEW LITERATURE

Axis Mutual Fund: A Scam of Front Running" (January 15, 2025). SSRN:

The Axis Mutual Fund front-running scam was masterminded by none other than the former chief dealer of the mutual fund, Viresh Gangaram Joshi, who exploited the sensitive information available to him between 2018 and 2021 to make front-running trades through proxy accounts for his own benefit. By sharing sensitive information about the future big trades of Axis Mutual Fund with brokers like Deepak Agarwal, Joshi helped them make profitable trades ahead of the mutual fund, resulting in gains of over Rs 200 crore, which may have actually been Rs 300 crore. The gains were laundered through shell companies and family

accounts, undermining the integrity of the market and harming investors. The front-running scam was discovered in 2022 when suspicious trading activity was identified during internal audits, leading to investigations by SEBI, Mumbai Police, and the Enforcement Directorate, resulting in arrests and the freezing of assets⁴.

Shriram Mutual Fund v. Securities and Exchange Board of India, (2006) 5 SCC 361:

In the case of *Shriram Mutual Fund v. SEBI* [(2006) 5 SCC 361], penalties were imposed upon Shriram Mutual Fund and Shriram Asset Management Company for conducting business through brokers associated with them in excess of the prescribed limits under the SEBI (Mutual Funds) Regulation, 1996. The essential question that arose in this case was whether or not the mutual fund had contravened Regulation 25(7)(a) of the SEBI (Mutual Funds) Regulation, 1996, which regulates and restricts dealings with brokers associated with the sponsor within a certain percentage of aggregate transactions. The Supreme Court held that mens rea or guilty intention is not a requirement for violation of civil obligations under the SEBI Act, and violation of such regulations attracts penalties regardless of intent. The Supreme Court upheld the penalties imposed upon the mutual fund for such violations.⁵

Samir C. Arora, SEBI March 31, 2004, Securities Appellate Tribunal Appeal No. 83/2004:

In the case of *Samir Arora* (SEBI Order, 2004), the SEBI had to conduct an investigation on the charges of professional misconduct, market manipulation, and insider trading against Samir Arora, the former fund manager of Alliance Capital Mutual Fund (ACMF). In this case, the SEBI had to conduct the investigation on the grounds of the violations of the disclosure norms under the Takeover and Insider Trading Regulations of the SEBI due to the aggregated shareholdings of the ACMF and Alliance Capital Management (ACM). In this case, the SEBI had also found that Samir Arora had indulged in the violation of the norms of professional conduct due to the bid to buy ACMF, as he was the fund manager of the equity portfolio of ACMF. In this case, the SEBI had to bar Samir Arora from trading in securities for five years starting August 2003⁶.

⁴ Axis Mutual Fund: A Scam of Front Running, SSRN (Jan. 15, 2025).

⁵ *Shriram Mutual Fund v. Sec. & Exch. Bd. of India*, (2006) 5 S.C.C. 361 (India).

⁶ *Samir C. Arora v. Sec. & Exch. Bd. of India*, Appeal No. 83 of 2004 (Sec. App. Trib. Mar. 31, 2004) (India).

Choi, J., Kim, Y., & Lee, J. Financial Reporting Fraud and Delegated Investment, 2021:

The paper "Financial Reporting Fraud and Delegated Investment" (2021) analyzes the behavior of mutual fund managers in response to publicly disclosed financial reporting fraud in companies in which the fund has invested. The study reveals that mutual fund managers tend to reduce investments in stocks that have high potential for fraud and increase investments in stocks that have low potential for fraud. This behavior leads to a greater alignment of fund portfolios to the benchmark. This behavior is more visible in cases of high-impact fraud. It has also been observed that mutual fund managers who face high capital outflows and those who charge higher fees tend to rebalance their portfolios more. The study reveals that due to the constraint of scarce resources, mutual fund managers tend to devote fewer resources to managing fraud risk before the fraud is disclosed. However, after the fraud is disclosed to the public, they tend to devote more resources to managing fraud risk. This behavior of mutual fund managers in managing fraud risk is significantly different from that of individual investors⁷.

ISSUES IN SEBI'S REGULATIONS AND GUIDELINES ON ADDRESSING MUTUAL FUND SCAMS WITHIN CORPORATE SOCIETY

It is challenging to guarantee investors' total security and the stability of the mutual fund market, despite the rules and guidelines put in place by SEBI to combat and prevent mutual fund scams. Strong internal fraud detection systems are now required of Asset Management Companies (AMCs) by SEBI. These companies must set up advanced surveillance systems, open internal controls, and effective reporting procedures in order to spot front-running, insider trading, market manipulation, and unauthorized trading early on. The purpose of these regulations is to build up a stable system of transparency and accountability, thus protecting the investors' interests and the market's fairness. However, the truth is that frauds very often involve such highly advanced methods that even the best regulatory practices may not detect them, like in the case of Axis Mutual Fund's front-running which consisted of secret trades done through offshore platforms. The law and regulations are sometimes even hampered by delays in inquiries or court cases which in return lessen the deterrent impact on wrongdoers. The majority of AMCs, particularly the smaller ones, still do not catch up with the use of high-tech fraud detection devices and quality compliance culture, leaving the gaps. Furthermore, a huge portion of the investors simply lacks the adequate knowledge of the market that would allow them to

⁷ J. Choi, Y. Kim & J. Lee, *Financial Reporting Fraud and Delegated Investment* (2021).

spot or defend themselves against fraudulent schemes, thus making prevention very difficult even with regulatory assistance. The regular updates of the regulations by SEBI such as refining product classifications and imposing greater disclosures go to show that the fast-evolving nature of the financial markets and the complexity of their products add layers of risk that regulators simply cannot cover completely¹. In other words, although SEBI's framework and reforms provide a solid base for the fight against mutual fund fraud, the efficacy of these regulations relies mostly on the observing of rules, the use of technology by the fund managers, the education of investors and the quick actions against violations. Otherwise, the prevention of fraud in such events will continue to be a difficult challenge for the corporate world.⁸

This indicates that the mutual fund ecosystem requires the continuous development of regulatory technologies, the more powerful compliance of institutions, and the wise investor community to be fairly protected against fraud even during the times when strict SEBI regulations are imposed.

The intricate and evolving nature of mutual fund frauds, which can almost always find a way to stay one step ahead of the regulators, is one of the main challenges that SEBI has to deal with in its regulatory scheme. People with no morals are increasingly using very advanced methods such as front-running, where traders with inside information buy stocks before the price raises due to a large client order and then sell the same stocks to the client at a higher price. The Axis Mutual Fund scandal offers an unequivocal example of this as the participants had their malpractices covered by stacking trades through offshore accounts and brokerages' networks that made detection very difficult even for conventional monitoring systems. SEBI's rules, although very meticulous, are greatly challenged by the cunningness of such operations, requiring not only constant technological improvements but also very dynamic monitoring systems that are capable of keeping pace with fraudsters. While large Asset Management Companies (AMCs) would have no problem investing in the technology and IT infrastructure that SEBI requires for its internal controls and real-time monitoring of trades, the smaller ones are being left behind. The lack of technology standardization and rigorous monitoring, in some cases, have caused delays in the detection and reporting of suspicious transactions, thereby hindering SEBI from preventing scams in a proactive way. In addition, the penalty structure of the regulatory framework sometimes represents a failure as a deterrent due to vagueness and

⁸ SEBI urged mutual fund companies to stay alert against rising frauds like fake redemptions and impersonation and also the need for heightened vigilance by asset management companies (AMCs).

power of discretion in enforcement. The case of Shriram Mutual Fund illustrated that the imposition of penalties based on discretion could create an atmosphere of uncertainty and leniency perceived by the regulators, hence, likely driving the wrongdoers to continue their activities. SEBI's objective is to impose strict penalties for the violations, but the process of judgment and appeals that takes a long time often weakens the immediacy and impact of the penalties. The delays not only facilitate the perpetrators of fraudulent practices to carry on longer but also lead the investors to lose faith in the effectiveness of the regulatory system's deterrence.⁹

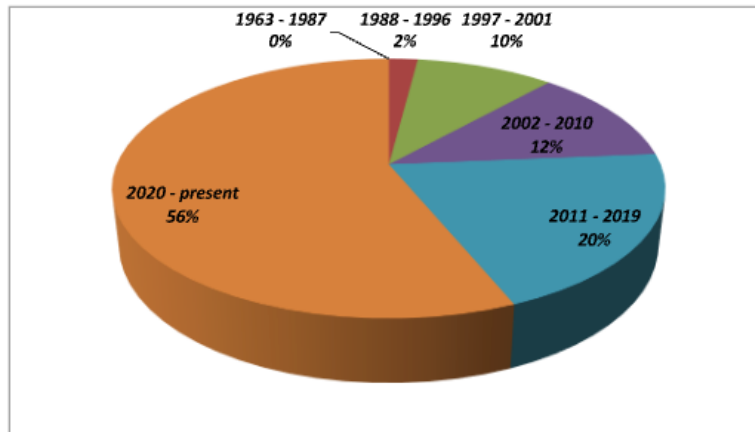
This problem emphasizes the need for clearer rules concerning the imposition of sanctions and speedier disposal of cases to maintain market discipline. Another area that is still of no less concern is investor enlightenment and awareness. Research shows that only a tiny bit of retail investors has the full comprehension to notice or steer clear of complicated scams which involve mutual funds. The came up of scammer trading apps and impostor frauds has even made the situation worse for the ignorant investors. In this respect, SEBI has run several campaigns and issued advisories to enlighten the investors, but the varied and complex socio-economic, as well as demographic, conditions of India, means, that large groups of investors are still unprotected. If a large-scale and efficient educational outreach is not done, even the toughest regulations can be bypassed by the social engineering and misinformation techniques aimed at retail investors.

Secondly, as mutual funds get more diversified into fresh money products and come up with new product development, SEBI is put to challenge to keep the rules dynamic without being overly liberal. Expanding product lines to include REITs, InvITs, and commodity ETFs brings in different risk issues and operational difficulties. On the one hand, this innovation is beneficial for market growth, but on the other hand, it demands more sophisticated risk management and transparency. If they are not supervised and managed properly, the innovations could unintentionally create chances for fraud and market manipulation which could then confuse SEBI's preventive goals. To sum up, although SEBI rules on mutual funds are very strict and constantly changing to tackle fraud risks, there are still some problems that reduce their overall effectiveness. These are the very advanced nature of frauds, the unequal diffusion of technology in mutual funds, the lengthy and uncertain punitive actions, the low level of investor education, and the rapid market innovation. Resolving these multifaceted problems requires a

⁹ SEBI warned investors to use only official channels and ensure proper KYC to avoid rising mutual fund frauds and fake redemption scams.

comprehensive approach that brings together regulatory awareness with advanced technology, investor education, institutional accountability, and fast legal processes to eliminate fraud in the mutual fund sector effectively.¹⁰

Mutual fund scam losses in India



1963 - 1987: 0.5 crore (mainly UTI monopoly phase with minimal public level scams but issues of transparency)

1988 - 1996: 1000 crore (CRB scam , Harshad Mehta scam and other small scams)

1997 - 2001: 4800 crore (UTI scams in early 2000s)

2002 – 2010: 6000 crore (includes effects from aftermath of Harshad mehta scam and other financial scams)

2011 – 2019: 10000 crore (notable chit fund scams like saradha ans sahara)

2020 – present: Axis Mutual Fund front-running scam, where illicit gains of around ₹30 crore were involved, and the large-scale frauds investigated by SEBI, totaling over ₹949 crore in disgorgements. ^{11, 12, 13}

¹⁰ SEBI mandates internal fraud detection mechanism for mutual funds. It mandates AMC's to put in place structured fraud detection mechanisms addressing insider trading , front –running , and unauthorized trading to strengthen internal controls and protect investors. PERSONAL FN 2025, SEPT 15AMC – Asset management system

¹¹ Saradha Chit Fund Scam, Central Bureau of Investigation (CBI) Investigation Reports (2013).

¹² Securities and Exchange Board of India Act, No. 15 of 1992, India.

¹³ Axis Mutual Fund Front-Running Case, Sec. & Exch. Bd. of India (SEBI) Investigation Orders &

Harshad mehta is also responsible for losses in mutual fund scams by - Misuse of bank receipts and diversion of funds, which indirectly affected mutual funds and investors who had invested through institutions tied to the manipulated stocks.

SEBI Regulatory Problems and Challenges

The SEBI regulations like Mutual Funds Regulations 1996 and Prohibition of Fraudulent Practices Regulations have not been successful in preventing scams like front-running from taking place undetected because of the existence of enforcement gaps. The lack of uniformity and the unclear idea of guidelines on the exercise of discretion in penalty imposition have resulted in inconsistent deterrence, as exemplified by the Shriram case. SEBI's monitoring capabilities are challenged by the massive frauds through digital and offshore channels (e.g., Dubai terminal in Axis scam). SEBI has recently enforced the imposition of structural, firm-specific fraud detection systems, but internal controls for fraud detection in funds are generally weak. The fraudulent activities of sophisticated nature along with delay in the court process have ruined investor protection and eroded market confidence. There is still a need for control measures for internal strengthening, transparency, regulation responsiveness, and investor education to be put in place continuously. The mutual fund sector must adopt advanced fraud detection technologies, ensure stricter compliance, promote swift enforcement actions, and prioritize investor awareness to rebuild trust and safeguard market stability. Without these measures, investor protection and market integrity will remain vulnerable. To truly restore confidence SEBI and fund houses must focus on rebuilding an ethical culture that values honesty over profit. Strengthening collaboration between regulators and financial institutions can help detect anomalies early. Investors should also be knowledgeable with accessible information and transparent grievance mechanisms. The use of AI-driven monitoring tools can improve fraud detection and early warning systems. Regular audits and public disclosure of fund performance will increase accountability. Ultimately, protecting investors is not just a regulatory duty but rather a moral obligation that defines the credibility of India's financial system.¹⁴

CONCLUSION

The mutual fund sector is more accessible and also a very promising investment option. Despite,

Disgorgement Proceedings (2020–present).

¹⁴ Disgorgement is the act of an entity being forced to give up illegal or unfair profits or gains, usually through a court order.

being regulated by SEBI it is still vulnerable to several fraudulent practices like ponzi scheme, fake investment platform, risk misrepresentation, unauthorized transactions and manipulative advisory services. These practices often threaten the investors' confidence and also affects the credibility of the Mutual fund sector. This can be rectified through in various ways such as SEBI and AMC should adopt digital based fraudulent detection mechanism periodic auditing must be conducted this often ensures ethical conduct and the financial intermediaries must be held strictly liable for their fraudulent actions. Furthermore, awareness programmes must be conducted to educate the investors and institutions on the mutual fund investments and its potential scams that are occurring in the society.

AMC's corporate governance has to be strengthened to protect the interest of the investors. Whistleblower mechanism should be adopted to uncover various fraudulent activities and unethical practices. Legal regulations has to be updated often to reduce the potential scams and also strict penalties has to be imposed to avoid scams in a broader way.incorporating these factors shall build a more reliable investment sector.

To truly safeguard investors and maintain market integrity, a multi-faceted approach is necessary one that includes continuous technological upgrades, vigorous regulatory enforcement, investor education, and faster resolution of violations. Only through such coordinated efforts can the mutual fund ecosystem be resilient against fraud and trustworthy for all investors. Smaller AMCs often struggle to meet technological standards, and prolonged legal processes weaken regulatory deterrence. Furthermore, many investors lack sufficient knowledge to identify or avoid complex scams. To effectively protect the mutual fund ecosystem, a balanced approach is essential one that combines strong regulations, cutting-edge technology, swift enforcement, and comprehensive investor education. This multi-pronged strategy is vital to build trust, ensure market stability, and safeguard investors amidst the dynamic and high-risk financial environment.

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