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The Inside Scoop: Exploring Insider Trading in the Indian Market

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ABSTRACT

Insider trading is a term used to describe the buying or selling of securities by individuals who have access to confidential information about a company. This practice is illegal in many countries, including India, where it is regulated by the Securities and Exchange Board of India (SEBI). This research work is undertaken to study, and examine the legal mechanism prevalent in India and assess the extent to which it has been implemented by interpreting cases taken up by the Courts. The research shall demonstrate and analyse various aspects of Insider trading, and evaluate the effect of this practice on the fidelity of a company towards the securities market and the common investor. The project aims to identify the legal and economic consequences of such practices with a detailed aspect of rules and regulations that are made to control such practices. Further, the research shall focus on some of the landmark cases in the history of Insider trading in India and will try to contemplate the outcomes of those cases.

Keywords: *Insider trading, corporate governance, India, Mandatory disclosure, SEBI, NSE, Fraud, Investigating officer.*

I. INTRODUCTION

A country's capital market is dominated by its stock exchanges. If stock exchanges are properly regulated, a thriving capital market can be developed. The active enforcement of criminal laws and regulations has intensified its emphasis on prosecuting and deterring insider trading and market abuse in the current economic climate around the world.

Insider trading, often known as "unpublished price sensitive information," is the practice of trading in a firm's stocks based on specific confidential corporate information that has not been publicized or made generally available. Such information includes information relating to the company's periodic financial results, any significant expansion plans, new projects, mergers, takeovers, amalgamations, the issuance or buyback of securities, significant changes in policy, etc., and, had it been published, would have materially affected the price and worth of the securities of that company.²

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² THE CONCEPT OF INSIDER TRADING IN INDIA *PROF. KAMLESH M. PANDYA,

Insider trading wasn't widely accepted as the unfairness it was, or even as a crime against shareholders and markets in general, until only about three decades ago. Previously, not too long ago, insider information and its use for personal Profits were seen as a perk of office and an advantage of having attained success in life. The phrase used to express this attitude was first used in 1973 by the Sunday Times of the UK. Insider trading was perceived as "the crime of being anything in the city," legislation against insider trading was sometimes seen to be equivalent to a prohibition against excellence.³

"Insider trading" is a term subject to many definitions and connotations and it encompasses both legal and prohibited activity. Insider trading takes place legally every day when corporate insiders – officers, directors, or employees – buy or sell stock in their own companies within the confines of company policy and the regulations governing this trading.

It is the trading that takes place when those privileged with confidential information about important events use the special advantage of that knowledge to reap profits or avoid losses on the stock market, to the detriment of the source of the information and to the typical investors who buy or sell their stock without the advantage of "inside" information.⁴

(A) Background

An 'insider' is someone who has received or had access to such information or is so connected with the company that it is reasonable to expect that he would have access to such information. For instance, if the director of a company, has information that the company has discovered oil on lands owned by it before such information is released to the public, and thereafter, in anticipation of the increase in the market value of the securities of the company once such information is made public, purchases a large number of shares of the company, he would be guilty of and liable for insider trading. Traditionally, insider trading has involved executives of a firm or linked parties such as merchant bankers, share transfer agents, trustees, brokers, investment advisers, bankers, brokers, sub-brokers, etc. breaching their fiduciary duties. An insider has a fiduciary obligation to the company to not abuse his position and misuse the knowledge once he obtains unpublished price-sensitive information as a result of his affiliation with the company or position inside the organization. Additionally, insider trading calls for the

https://www.worldwidejournals.com/paripex/recent_issues_pdf/2013/August/the-concept-of-insider-trading-in-india_August_2013_8024176091_8204571.pdf (last visited Aug 9, 2023).

³ Dr. K. R. Chandratre, COMPENDIUM OF KEY ISSUES UNDER CORPORATE LAW, 1E GOOGLE BOOKS (2021), https://books.google.com/books/about/Compendium_of_Key_Issues_Under_Corporate.html?id=FNP5DwAAQB_AJ (last visited Aug 9, 2023).

⁴ OVERVIEW OF SEBI'S PROHIBITION OF INSIDER TRADING REGULATIONS (PIT REGULATIONS) TAXMANN BLOG, <https://www.taxmann.com/post/blog/overview-of-sebis-prohibition-of-insider-trading-regulations/> (last visited Aug 27, 2023)

insider to have exploited the knowledge to generate illicit personal advantage or to manipulate the market in some other way. Insider trading is considered lawful when the insiders (i.e., directors, employees, officers, executives) of the Company who have price-sensitive information, buy or sell securities of their own Company within the confines of the Company's policy and regulations governing this trade.⁵

The Modus operandi initiates when insiders act as initiators of price change by receiving the information much earlier than others. An insider, first of all, buys the stock of the Company at the existing market price. He then spreads some price-sensitive information relating to the Company to a select group of people, who based on such information will buy such stocks and would further spread the information. When this information reaches a large number of people, it pushes up the sales volume and price of the stock. After a certain price of the stock is reached, an insider sells his stock, as do the ones close to him before others do the same. As now everyone tries to sell his or her stock, its price will fall. When information is available to everyone, the stock returns to its realistic price level, resulting in a huge loss for common investors.⁶

The reasoning for the prohibition on insider trading is "the obvious need, the understandable concern about the harm that insider dealing is likely to do to public confidence, and the clear intention to prevent, to the extent possible, what amounts to cheating when those with inside knowledge use that knowledge to make a profit in their dealings with others."⁷

If firms and their directors engage in manipulative and deceptive practices, insider trading, etc., SEBI, the market regulator, will be failing in its role to encourage the orderly and healthy expansion of the securities market. People in this country should be aware that economic offence is a severe crime that, if not handled correctly, would negatively impact India's securities market as well as the nation's economic progress. It will also delay the influx of real foreign investment.⁸

II. HISTORICAL BACKGROUND

The United States of America was the first to publicly implement legislation to address the

⁵ SEBI ON INSIDER TRADING LEGAL SERVICE INDIA, <https://www.legalserviceindia.com/article/I268-SEBI-on-Insider-Trading.html> (last visited Aug 27, 2023)

⁶ insider trading in India: regulations and controlling authority inventiva (2022), <https://www.inventiva.co.in/trends/insider-trading-in-india/> (last visited Jun 16, 2023).

⁷ THE KNOW-ALL OF INSIDER TRADING – DECADES OF CORRUPTIVE PREVENTION ACADEMIKE (2015), <https://www.lawctopus.com/academike/know-insider-trading-decades-corruptive-prevention/> (last visited Jun 16, 2023).

⁸ ALL YOU WANTED TO KNOW ABOUT INSIDER TRADING THE HINDU BUSINESS LINE (2021), <https://www.thehindubusinessline.com/opinion/columns/slate/all-you-wanted-to-know-about/article34755136.ece> (last visited Jun 16, 2023).

threat of insider trading. Most governments across the world have recognized the need to prevent insider trading in some form or another throughout the years and have put in place legislative measures to that effect to protect investor trust in the capital market. India was not slow to recognize the negative consequences of insider trading.⁹ The history of insider trading in India dates back to the 1940s, with the formation of government committees such as the Thomas Committee, chaired by Mr. P.J. Thomas, to evaluate restrictions that can be imposed on short swing profits of 1948, which evaluated, among other things, the regulations in the US on short-swing profits (profits made by the simultaneous purchase and sale of the company's securities) under Section 16 of the Securities Exchange Act of 1934.¹⁰

Up until around 1970, India's 125-year-old stock market allowed for unrestricted insider trading. This practice was acknowledged as unfair in the late 1970s. According to the **Sachar committee's** report from 1979, staff of businesses, such as directors, auditors, company secretaries, etc., may have access to price-sensitive information that might be used to manipulate stock prices, putting the investing public at risk of suffering financial losses. The business proposed changes to the Companies Act of 1956 to limit or outlaw the interactions between employees and insiders. Also proposed were penalties to stop insider trading.¹¹

In 1986 the **Patel committee** recommended that the securities contracts (Regulations) Act, of 1956 may be amended to make exchanges curb insider trading and unfair stock deals. It suggested heavy fines including imprisonment apart from refunding the profit made or the losses averted to the stock exchanges.¹²

In 1989 the **Abid Hussain Committee** recommended that insider trading activities may be penalized by civil and criminal proceedings and also suggested that the SEBI formulate the regulations and governing codes to prevent unfair dealings.¹³

Following the recommendations by the committees, SEBI has, in the exercise of the powers conferred on them by section 30 of the Securities and Exchange Board of India Act 1992, made regulations which are known as the Securities and Exchange Board of India (Insider Trading) Regulations 1992.

⁹ CRITICAL ANALYSIS ON LAWS RELATING TO INSIDER TRADING, <https://shodhganga.inflibnet.ac.in/jspui/handle/10603/13173> (last visited Jun 16, 2023)

¹⁰ Carlton, D.W. and Fischel, D.R. (1983), "The regulation of insider trading", *Stanford Law Review*, Vol. 35 No. 5, p. 860

¹¹ Implementation Of Sachar Committee Recommendations, http://www.minorityaffairs.gov.in/sites/default/files/Sachar-Committee-Status_0.pdf (last visited May 7, 2023)

¹² INSIDER TRADING: JOURNEY OF LEGAL FRAMEWORK TO CHECK THE PRACTICE INDIAN LAW WATCH, <https://indianlawwatch.com/practice/insider-trading/> (last visited Aug 27, 2023)

¹³ RECOMMENDATION OF ABID HUSSAIN COMMITTEE PARLIAMENT DIGITAL LIBRARY: HOME, https://eparlib.nic.in/handle/123456789/465418?view_type=browse (last visited Aug 27, 2023)

This regulation of 1992 has prohibited this fraudulent practice and a person convicted of this offense is punishable under Section 24 and Section 15 G of the SEBI Act 1992. These regulations were drastically amended in 2002 and renamed SEBI (Prohibition of Insider Trading) Regulations 1992.

Both the Insider Trading Regulations are essentially punitive in that they define what insider trading is and then attempt to penalize this behaviour in several different ways. More crucially, all listed companies, all market intermediaries (including brokers), and all advisers must adhere to them (such as merchant bankers, professional firms, etc.).

There were no particular laws against insider trading in India before the creation of this legislation. Now, thanks to the aforementioned legislation, it is forbidden to engage in, communicate with, or offer advice regarding insider trading. Definitions of what constitutes an "insider" have also been supplied.

III. DEFINING INSIDER AND INSIDER TRADING

Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 1992, does not directly define the term "insider trading". But it defines the terms-

- "insider" or who is an "insider";
- who is a "connected person";
- What is "price sensitive information".

Regulation 2(e) provides for the definition of an 'insider' which has been defined in two clauses: firstly, a person who is or was connected with the company or is deemed to have been connected with the company and who is reasonably expected to have access to unpublished price sensitive information in respect of securities of a company, and secondly, a person who has received or has had access to such unpublished price sensitive information.¹⁴ To qualify within the first clause of the definition, it appears that one must be (a) either a 'connected person within the scope of Regulation 2(c) or a 'person deemed to be a connected person within the scope of Regulation 2(h) and (b) must be reasonably expected to have access to unpublished price sensitive information.¹⁵

Regulation 2(c) has defined a 'connected person' to include firstly, a director or a person deemed

¹⁴ SEBI (PROHIBITION OF INSIDER TRADING) REGULATIONS, 2015 (ISSUED ON 15 JAN 2015) SEBI, https://www.sebi.gov.in/legal/regulations/jan-2015/sebi-prohibition-of-insider-trading-regulations-2015-issued-on-15-jan-2015-_28884.html (last visited Aug 27, 2023)

¹⁵ HISTORICAL TIMELINE PROCONORG HEADLINES, <https://insidertrading.procon.org/view.resource.php?resourceID=002391> (last visited Aug 27, 2023)

to be a director or secondly, any person who—

- a) occupies the position of an officer of the company,
- b) occupies the position of an employee of the company
- c) any person who holds a position involving a professional or business relationship between himself and the company, whether temporary or permanent, and who may reasonably be expected to have access to unpublished price-sensitive information about that company.

Secondly, the definition has as previously mentioned, by the 2002 amendment, brought within its ambit intermediaries, investment companies, trustee companies, asset management companies or their employees or directors, or an official of a stock exchange, clearing house, or corporation.¹⁶

Thirdly, the definition specifically brings within its ambit the following intermediaries: merchant banker, share transfer agent, registrar to an issue, debenture trustee, broker, portfolio manager, investment advisor, sub-broker, investment company or an employee thereof, a member of the Board of Trustees of a mutual fund, a member of the Board of Directors of the Asset Management Company of a mutual fund and any employee thereof who has a fiduciary relationship with the company.¹⁷

IV. UNPUBLISHED PRICE-SENSITIVE INFORMATION

It is crucial to first define what exactly constitutes "unpublished price sensitive information" before analysing the legal rules that specify what would constitute "insider trading." Unlike before the 2002 amendment regulations, the SEBI regulations as they currently stand do not specify "unpublished price sensitive information," instead defining "price sensitive information" and "unpublished" separately. Regulation 2 (ha) defines 'price sensitive information' to mean any information which relates directly or indirectly to a company and which if published is likely to materially affect the price of securities of a company.¹⁸

Further, certain information has been deemed to be price-sensitive information—

1. periodical financial results of the company;

¹⁶ Umakanth Varottil, *The Long and Short of Insider Trading Regulation in India*, NSE CENTRE FOR EXCELLENCE IN CORPORATE GOVERNANCE

¹⁷ COMPANY SECRETARIAL PRACTICE - THE INSTITUTE OF COMPANY SECRETARIES M.MOAM.INFO, <https://mafiadoc.com/company-secretarial-practice-the-institute-of-company-secretaries-5a2311231723dd22f10429ca.html> (last visited Aug 27, 2023)

¹⁸ Michael P. Dooley, *Enforcement of insider trading restrictions*, 66 VIRGINIA LAW REVIEW, 1 (1980)

2. intended declaration of dividends (both interim and final);
3. issue of securities or buy-back of securities;
4. any major expansion plans or execution of new projects;
5. amalgamation, mergers, or takeovers;
6. disposal of the whole or substantial part of the undertaking;¹⁹
7. significant changes in policies, plans, or operations of the company.

Furthermore, "unpublished" information is defined in Regulation 2(k) as information that is not specific in nature and is not publicized by the corporation or its agents. Furthermore, it is expressly stated in the Regulation's Explanation that speculative reports published in print or electronic media are not to be regarded as "published information."²⁰ As a result, the 2002 amendment aimed to eliminate the defines offered by the definition as it stood, namely that any information that was widely publicized in the media or was otherwise widely known could not have qualified as unpublished price-sensitive information.²¹

V. REGULATORY FRAMEWORK

1. Securities and Exchange Board of India Act, 1992

According to Section 12A of the SEBI Act: No person shall directly or indirectly— engage in insider trading; deal in securities while in possession of material or non-public information or communicate such material or non-public information to any other person, in a manner that is in contravention of the provisions of this Act or the rules or the regulations made thereunder.

According to Section 15 G of SEBI Act,1992: Penalty for insider trading: If any insider who,— either on his behalf or behalf of any other person, deals in securities of a body; corporate listed on any stock exchange based on any unpublished price-sensitive information; or communicates any unpublished price-sensitive information to any person, with or without his request for such information except as required in the ordinary course of business or under any law; or counsels, or procures for any other person to deal in any securities of anybody corporate

¹⁹ INSIDER INFORMATION - OVERVIEW, INSIDER TRADING, AND EXAMPLE, CORPORATE FINANCE INSTITUTE (2019), CORPORATE FINANCE INSTITUTE, <https://corporatefinanceinstitute.com/resources/knowledge/trading-investing/insider> (last visited Aug 28, 2023)

²⁰ SECURITIES AND EXCHANGE BOARD OF INDIA (PROHIBITION OF INSIDER TRADING) REGULATIONS, 2015 [LAST AMENDED ON AUGUST 05, 2021] SEBI, https://www.sebi.gov.in/legal/regulations/aug-2021/securities-and-exchange-board-of-india-prohibition-of-insider-trading-regulations-2015-last-amended-on-august-05-2021-_41717.html (last visited Aug 28, 2023)

²¹ Vyas, Amit K, 'SEBI (Prohibition of Insider Trading) Regulations, 1992: the concept of unpublished price sensitive information radically amended', Chartered Secretary, The Institute of Company Secretaries of India, Vol. 32, 2002 (May) 597-9p, 598.

based on unpublished price-sensitive information, shall be liable to a penalty [which shall not be less than ten lakh rupees but which may extend to twenty-five crore rupees or three times the amount of profits made out of insider trading, whichever is higher.

2. SEBI (Prohibition of Insider Trading) REGULATION, 2018

Before analysing the provisions of the SEBI (Prohibition of Insider Trading) Regulation, 2018, it is important to understand the key definitions and meanings of the terms which have been used in the regulation.²² Key definitions are.

a) Compliance officer:

Any senior officer appointed as such and reporting to the board of directors or the head of the organization in the absence of a board, who is financially literate and capable of recognizing the needs for legal and regulatory compliance under these laws, and who is responsible for: (a) Compliance of policies, procedures, maintenance of records, monitoring adherence to the rules for the preservation of unpublished price sensitive information (b) Monitoring of trades and the implementation of the codes specified in these regulations under the overall supervision of the board of directors of the listed company or the head of an organization as the case may be.²³

b) Connected person: Connected person means:

- any person who is or has during six months before the concerned Act has been associated with a company, directly or indirectly;
- in any capacity (including because of frequent communication with its officers or by being in any contractual, fiduciary, or employment relationship); or
- is a director, officer, or an employee of the company or holds any position including a professional or business relationship between himself and the company, whether temporary or permanent; or that allows such person, directly or indirectly, access to unpublished price-sensitive information or reasonably expected to allow such access.²⁴

VI. COMMUNICATION OR PROCUREMENT OF UNPUBLISHED PRICE-SENSITIVE INFORMATION

Regulation 3 provides that any person shall not: – communicate, provide, or allow access to

²² THE SECURITIES AND EXCHANGE BOARD OF INDIA ACT, 1992 NO.15 OF 1992 <https://www.sebi.gov.in/acts/act15ac.pdf> (last visited Aug 29, 2023)

²³ SEBI (PROHIBITION OF INSIDER TRADING) REGULATIONS, 2015 (ISSUED ON 15 JAN 2015) SEBI, https://www.sebi.gov.in/legal/regulations/jan-2015/sebi-prohibition-of-insider-trading-regulations-2015-issued-on-15-jan-2015-_28884.html (last visited Aug 29, 2023)

²⁴ SECURITIES AND EXCHANGE BOARD OF INDIA, <https://www.sebi.gov.in/acts/insidereg.pdf> (last visited Aug 29, 2023).

any unpublished price-sensitive information or – procure from or cause the communication by any insider of unpublished price-sensitive information, relating to a company or securities listed or proposed to be listed or proposed to be listed except in furtherance of legitimate purposes, the performance of duties or discharge of legal obligations.²⁵ A listed company's board of directors should establish a policy for determining "Legitimate intentions" as part of the "Codes of Fair Disclosure and Conduct" defined under regulation. [For example, the term "legitimate purpose" shall include an insider sharing UPSI in the ordinary course of business with partners, collaborators, lenders, customers, suppliers, merchant bankers, legal advisors, auditors, insolvency professionals, or other advisors or consultants, provided that such sharing was not done to evade or circumvent the prohibitions of these regulations.] Any individual receiving UPSI for a "legitimate purpose" shall be regarded as an "insider" for these rules, and such persons shall be provided appropriate warning to safeguard the secrecy of such UPSI by these regulations.

VII. TRADING WHEN IN POSSESSION OF UNPUBLISHED PRICE-SENSITIVE INFORMATION (UPSI)

Regulation 4 prescribes that an insider shall not trade in securities, which are listed or proposed to be listed on the stock exchange when in possession of unpublished price-sensitive information. However, there are certain exemptions:²⁶

1. When there is an off-market transfer between insiders or the transaction was carried through the block deal window mechanism between a person

(i.) who was in the possession of the UPSI;

(ii.) Both parties had made a conscious and informed trade decision;

(iii.) there should be no breach of Regulation 3;

(iv.) UPSI should not have been obtained under Regulation (3).

2. The transaction in question was carried out under a statutory or regulatory obligation to carry out a bonafide transaction,

²⁵ SECURITIES AND EXCHANGE BOARD OF INDIA (PROHIBITION OF INSIDER TRADING) REGULATIONS, 2015 [LAST AMENDED ON AUGUST 05, 2021] SEBI, https://www.sebi.gov.in/legal/regulations/aug-2021/securities-and-exchange-board-of-india-prohibition-of-insider-trading-regulations-2015-last-amended-on-august-05-2021-_41717.html (last visited Aug 28, 2023)

²⁶ Securities and Exchange Board of India (prohibition of insider trading) regulations, 2015 [last amended on August 05, 2021], SEBI, Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015 [Last amended on August 05, 2021] (last visited Sep 9, 2023).

3. the transaction in question, was undertaken under the exercise of stock options in respect of which the exercise price was pre-determined in compliance with applicable regulations.²⁷

4. In the case of non-individual insiders:

- i. The individuals who had such unpublished price-sensitive information were different from the individuals taking trading decisions and
- ii. Such decision-making individuals did not have such unpublished price-sensitive information when they decided to trade; and
- iii. Appropriate and adequate arrangements were in place to ensure that these regulations are not violated and
- iv. There is no evidence of such arrangements having been breached;

VIII. TRADING PLANS

According to Regulation 5, an insider must submit a trading strategy to the compliance officer for approval in advance. The compliance officer is also authorized to get extra commitments from insiders to approve the trading strategy. Following approval, such a trading strategy will be published on the stock exchanges where the company's securities are listed. However, pre-clearance of transactions is not necessary for trades done by an approved trading strategy.²⁸ Furthermore, trading window standards and contra-trade limits will not apply to trades carried out in line with an approved trading strategy. The trading plan shall comply with the requirements as follows—

- It shall be submitted for a minimum period of 12 months. No overlapping of the plan with the existing plan submitted by the Insider Compliance officer to approve the plan.
- It must specify either the amount of the trades to be executed or the number of securities to be exchanged, as well as: - the kind of the trade and - the intervals or days on which such trades must be executed.
- Trading can begin just six months following the plan's public publication. There will be no trading between the 20th day before the end of the fiscal period and the 2nd trading day after the financial figures are released.

²⁷ SECURITIES MARKET REGULATIONS: LESSONS FROM US AND INDIAN EXPERIENCE, https://www.researchgate.net/publication/228209974_Securities_Market_Regulations_Lessons_from_US_and_Indian_Experience (last visited Sep 9, 2023).

²⁸ Securities and Exchange Board of India (prohibition of insider trading) regulations, 2015 [last amended on August 05, 2021], SEBI, Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015 [Last amended on August 05, 2021] (last visited Sep 9, 2023).

- Once authorized, the trading plan is irrevocable, and the insider is required to follow it without the ability to depart from it or execute any deal in the securities outside the boundaries of the trading plan. (Except in rare cases where an insider has price-sensitive information at the time of plan formulation and such information has not become generally available at the time of plan implementation)
- Upon approval of the trading plan, the compliance officer shall notify the stock exchanges on which the securities are listed.

IX. PENALTY FOR INSIDER TRADING

- As per the Section 15g and 24 of the SEBI ACT, insiders, who violate the 2015 regulations, are liable to a penalty that may be imposed by SEBI of Rs. 25 crores or 3 times the amount of profit made out of the insider trading, whichever is higher and shall also punishable with imprisonment for a term extending to 10 years or a fine up to 25 crores or both.²⁹
- As per Section 11(c) (6) of the SEBI ACT, if any person without justifiable reason, refuses to co-operate in any investigation by SEBI concerning insider trading, then he shall be punishable with imprisonment for a term extending up to one year, or with fine up to Rs1 crore or with both, and also with a further fine up to Rs. 5 lakhs for every day of such non-co-operation.
- As per section 11(4) (b) of SEBI ACT, SEBI is also empowered to pass directions to such insider not to deal in the concerned securities in any particular manner and/or prohibit him from disposing of the concerned securities and /or declaring the concerned transaction(s) of securities as null and void, restraining the insider from communicating or counselling any person to deal in securities.
- As per section 195 of the Companies Act, 2013 any insider contravenes the provisions of this section, he/she shall be punishable with imprisonment for a term which may extend to five years or with a fine which shall not be less than five lakhs rupees but which may extend to twenty-five crore rupees or three times the number of profits made out of insider trading, whichever is higher, or with both

X. DUTIES/ OBLIGATIONS OF THE COMPANY

Every listed company has the following obligations under the SEBI(Prohibition of Insider

²⁹ Sheshank Dubey, GIST OF INSIDER TRADING REGULATION TAXGURU (2022), <https://taxguru.in/sebi/gist-insider-trading-regulation.html> (last visited Sep 9, 2023).

Trading)Regulations, 1992.³⁰

- To appoint a senior level employee generally the Company Secretary, as the Compliance Officers;
- To set up an appropriate mechanism and to frame and enforce a code of conduct for internal procedures,
- To abide by the Code of Corporate Disclosure practices as specified in Schedule ii to the SEBI (Prohibition of Insider Trading)Regulations, 1992
- To initiate the information received under the initial and continual disclosures to the Stock Exchange within 5 days of their receipts;
- To specify the close period;
- To identify the Price Sensitive Information
- To ensure adequate data security of confidential information stored on the computer;
- To prescribe the procedure for the pre-clearance of trade and entrusted the Compliance Officers with the responsibility of strict adherence to the same.³¹

XI. CASE STUDIES

1. The Hindustan Lever Ltd. Case

The case of Hindustan Lever Ltd. v. SEBI³² was one of the first ever cases of Insider Trading in India where SEBI scrutinized the involvement of a big Company (HLL) in Insider Trading. This case relates to Hindustan Lever Ltd which was alleged to be involved in Insider Trading transactions when it purchased 8 lac shares of Brooke Bond Lipton India Ltd (BBLIL) from Unit Trust of India (UTI) based on unpublished price-sensitive information regarding the impending merger of HLL and BBLIL.

However, SAT reversed the order of SEBI *on the ground that the proposed merger was generally known and cited press reports which revealed the prior market knowledge* of the proposed merger. The most significant fallout of this case was the subsequent amendment introduced in the SEBI Regulations, which was aimed at removing the loophole in the law that any information which was generally known in the media could not constitute unpublished

³⁰ Securities and Exchange Board of India (prohibition of insider trading) regulations, 2015 [last amended on August 05, 2021], SEBI, Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015 [Last amended on August 05, 2021] (last visited Sep 10, 2023).

³¹ Author(s):Journal of Legal Studies and Research, ANTICIPATIVE AND STATISTICAL ANALYSIS OF INSIDER TRADING THE LAW BRIGADE PUBLISHERS (INDIA) (2022), <http://thelawbrigade.com/company-law/anticipative-and-statistical-analysis-of-insider-trading/> (last visited Sep 10, 2023).

³² [1998] 18 SCL 311 (SAT).

price-sensitive information. *The amendment to Regulation 2(k) introduced in 2002, clearly provided that speculative reports in the print or electronic media would not be considered 'published' information.*

2. The Rakesh Agrawal Case

The case of Rakesh Agrawal v. SEBI³³ has been a major milestone in developing the insider trading laws prevalent in India. This case relates to the alleged involvement of Mr. Rakesh Agrawal, who was the then Managing Director of ABS Industries Ltd., in Insider Trading transactions while he had access to the price-sensitive information regarding the merger of ABS Industries Ltd. to Bayer AG. After a detailed consideration of issues and evidence, the *SAT found that his intention in acquiring the share was to facilitate the entry of Bayer and not to gain unfair personal gain. SAT held that although it was true that in the process the shares purchased at a lower price fetched a higher price when offered in the public offer, this gain was only incidental, and certainly not to cheat.*

Thus, SAT held that Rakesh Agrawal was not guilty of insider trading. SEBI appealed the decision of SAT to the Hon'ble Supreme Court which has settled the matter by its consent order whereby Mr. Rakesh Agrawal has agreed to pay Rs. 48,00,000 towards the settlement²³. Also concerning the prosecution initiated by SEBI in 2001, the offense was compounded by a payment of Rs. 4,90,000 by the accused to SEBI.

3. The Samir Arora Case

The case of Samir Arora v. SEBI³⁴ was another important case in the evolution of insider trading laws in India. The case relates to 2003 wherein Samir C. Arora, the fund manager of Alliance Capital Mutual Fund was alleged to be involved in Insider Trading transactions when he disposed of the entire scrip of Digital Global Soft (DGL) held by him based on the alleged unpublished price sensitive information of the merger ratio of DGL with HPI (Hewlett Packard). It was alleged that based on inside information, Samir Arora had first moved up the price of the scrip from Rs. 537.55 on 2nd May 2003 to Rs. 597.25 on May 7, 2003, with *certain statements made by him to the Business Standard* on April 30, 2003, which was published on May 5, 2003, and then sold all the holdings of the funds managed by him over the next four trading days thereby averting a loss of about Rs. 23 crores to the Funds managed by him. The SEBI found that he was prima facie guilty of the offense of insider trading. SEBI passed orders debarring him from accessing the securities market for five years. On an appeal to the SAT, after carefully

³³ [2004] 49 SCL 351 (SAT).

³⁴ [2005] 59 SCL 96 (SAT).

analysing the contentions of both parties concluded that the price-sensitive information which Samir Arora was alleged to have accessed was not correct information because the merger was not announced on May 12, 2003.

It held that information that finally turns out to be false or at least uncertain cannot be labelled as information. Thus, it was concluded by the SAT that the sale of securities before the board meeting could only be considered to be based on Samir Arora's analysis and assessment of the information available in the public domain.

4. Indiabulls Insider Trading Case

This case is one of the latest case laws which is related to insider trading. In this case, the executive director of India bulls was accused of making Rs. 87 lakhs unlawfully by trading in India bulls when they had access to unpublished secret information about the sale of land and property privately which is the subsidiary of India bulls venture limited. According to the regulator, the executive director of India bulls venture limited was on the management committee of India bulls, therefore she was an insider and her husband too was an insider. These unlawful gains were made in the year 2017-19.

The SEBI ordered that strict criminal action be taken against the IVF and both the executive director of the company and her husband have to impound Rs. 87.4 lakhs both jointly and severally. It was further directed that no debts shall be made without the prior permission of SEBI.³⁵

XII. EFFECTS OF INSIDER TRADING

The effect of insider trading is borne by those who are not aware of the confidential information. Due to this, they do not deal in securities. Insider trading is unethical and amounts to a breach of fiduciary position as it involves a breach of trust and confidence. The misuse of insider information is discouraged for numerous reasons:

- a) Insider takes unfair advantage of the information-deprived person;
- b) It results in a conflict of interest as it is beneficial for the insider's self-interest and not in the company's best interest;
- c) It lowers the market reputation and acts as a disincentive to investment.

The conditional buying or selling of securities by the advantageous person only when in

³⁵ India bulls HSG case: HC quashes Ed Proceedings, THE ECONOMIC TIMES, <https://economictimes.indiatimes.com/industry/banking/finance/delhi-hc-quashes-eds-ecir-against-ihfl-and-its-employees-says-no-further-coercive-action/articleshow/94488444.cms> (last visited Sep 10, 2023).

possession of confidential information affects the determination of the value of those securities. Also, the possession of confidential information in question implies that the advantageous person has some connection in the corporation who is yielding the essential information to that person. He may be a director, employee, or professional adviser of that company. This is disadvantageous for the corporation as well.³⁶

Let us suppose a hypothetical scenario of insider trading activity in which a director of a merchant bank was advising a company regarding the process of mounting a takeover of another company. It was known that the publication of the information of a takeover offer could result in an immediate rise in the prices of shares of the target company or the acquiring company. The acquisition of some shares by the merchant banker in advance of publication, at the pre-bid price, and disposing of them immediately after the announcement of the bid, would constitute the act of insider trading.³⁷

It is essential for a fair trade that insider information must not be utilised by the directors or employees to further their interests. Doing such an act would amount to a breach of their obligation towards the company. People will lose interest in such companies. There should be a continuous check on such practices to ensure the integrity of the market is not degraded by the loss of confidence of investors. These practices are immoral, and unethical and can cause damage to a large number of innocent investors.

Over time, countries have expressed their objections to such practices. The USA was the first country to tackle the problem of insider trading effectively. The United Kingdom has imposed a lot of obligations and duties on the Directors to control the transfer of confidential information. India has also developed various regulations in this regard. The Companies Act and SEBI Regulations 1992, are examples of such regulations. However, the country has not been effective in fighting such practices.

XIII. CONCLUSION

The core of securities regulations is the implementation of the purpose that all investors should have equal access to the rewards of participation in securities transactions. In other words, all members of the investing public should be subject to identical market risks. Inequities based upon unequal access to knowledge should not be shrugged off as inevitable in our way of life.

³⁶ REGULATION OF INSIDER TRADING IN INDIA: DISSECTING THE DIFFICULTIES AND ..., <https://jcil.lsyndicate.com/wp-content/uploads/2023/06/Roopanshi-Dr.-Afzal.pdf> (last visited Sep 10, 2023).

³⁷ A QUESTION OF INTEGRITY: PROMOTING INVESTOR CONFIDENCE BY FIGHTING ..., <https://www.proquest.com/openview/2da4677d1b0bbbd3291dea2a80aa2986/1.pdf?pq-origsite=gscholar&cbl=41532> (last visited Sep 10, 2023).

It is therefore important for there to be markets free from all types of fraud and in particular insider trading which disenchant the common investor from the workings of the markets as if he is being invited to play a game of crap with loaded dice. The SEBI has been operating now as the securities markets regulator since 1991 and has appeared to have done a commendable task in upholding the mandate it was charged with, in a period of high growth and reasonably heightened levels of economic volatility. The principles based on which the entity was created have stood it in good stead. Some of these principles include clarity on the mandate it was to deliver on, non-interference from the government, and statutory powers to issue subordinate legislation which can be notified expeditiously to accommodate the rapid changes that take place in the equities markets in India and the powers to enforce the regulatory mandate.

Thus, the problems in establishing charges of insider trading are largely related to the unavailability of sufficient proof to establish mental intent and whether or not access to unpublished price-sensitive material was possible in the facts and circumstances of a particular case. In an analysis of the regulatory mechanism in India, the only conclusion that can be reached is that the laws prevalent in India are ill-equipped to combat insider trading and are not conducive to the needs of a rapidly changing economy and corporate structure.

Irrespective of the outcome of the HLL case it would be more equitable if the regulations were amended to require SEBI to prima facie establish that insider trading has indeed occurred and then shift the onus of proof onto the defendant to establish his bonafide.

In the contemporary scenario securities markets around the world are competing for the fixed pool of capital. Investors will surely prefer markets where the regulatory agencies are most effective. Protecting the investors, enforcing securities laws, and creating confidence in the system by ensuring the fairness and integrity of the market should therefore be a priority. Investor confidence is extremely fragile and should be maintained with care. The securities markets should therefore be treated like Caesar's wife; they must not only be above suspicion but must also be perceived to be so.

(A) Recommendations

Based on the research work done to write this article following recommendations are proposed though these recommendations are not exhaustive and more feedback can be sought from the masses yet the author proposes the following recommendations.

Though the legal regime in India would have to develop and evolve significantly. Moreover, the regulatory mechanism in India must be vigilant to evolve itself to keep pace with the fast-growing securities market to prevent unfair practices like insider trading from hampering its

balanced growth and shaking the confidence of the common investor.

The current study's shortcomings leave room for future investigation. Future studies may be conducted by taking into account the recently implemented SEBI (Prohibition of Insider Trading) Regulations, 2021. Insiders are classified into many categories under the new SEBI laws, including Director/Directors Immediate Relative, Employee/Employees Immediate Relative, Key Managerial Person, Promoter, Promoter and Director, and Promoters Immediate Relative. To measure the impact of the change in insider trading restrictions, future research might examine the profitability of each category of insiders and their information content.

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