ANTICIPATIVE AND STATISTICAL ANALYSIS OF INSIDER TRADING

*Written by **Javish Valecha***

5th Year BBA LLB Student, School of Law, KIIT University, Bhubaneswar

ABSTRACT

It was only about thirty years back and not recently that insider trading was identified in many developed countries as what it was - a prejudice; in fact, it is an offence in opposition to the shareholders and markets. Once, not so far in the past, inside information or details and its use for one's own welfare was considered as an advantage of office and a perk of having reached a high and tremendous phase in life. It was the Sunday Times of UK that fabricated the classic phrase in 1973 to describe this conception - "the crime of being something in the city", interpreted that insider trading was trusted as legitimate at one time and a law opposing insider trading was like a rule or regulation against high victory or realization. "Insider trading" is a term subject to innumerable definitions, connotations and interpretations and it also consists of legal activity. It's the buying and selling that transpires when those privileged unpublished with private information about paramount events use the special benefit of that knowledge to earn gains or dodge damages on the stock market. It is also a disadvantage to the origin of the information and to the investors who trade in their stock beyond the privilege of "inside" knowledge. Practically eight years ago, India's capital markets' watchdog – the Securities and Exchange Board of India put in order an international seminar on capital market regulations. Admittedly, insider trading is also a crucial part of the business transaction, and that the laws relating to it was last notified in the year 1992 and have not changed since then. This lead to objections in the smooth transactions of listed securities. The new regulations propounded current dynamics of the capital market. Apart from introducing some basic rules of insider trading, the new regulations have brought some **faultless and significant changes in the world of insider trading**. The new regulation has increased the scope of the definition “connected person”, now it covers all persons who are in connection or is associated with the company or an organization, even by a discussion with an employee which gives a reason to believe that UPSI can be exchanged. SEBI has remodelled the entire formation of the insider

trading mechanism, which is seen to be a very deep-seated problem in India. This action of SEBI will provide a much-needed fillip and exposure to the players of Indian capital market and facilitate further economic expansion

INTRODUCTION

Attribution of personality to corporations have enabled them to enjoy certain freedoms and legal rights and obligation across the globe in any legal framework. A corporation is a legal entity that is separate and distinct from its owners. One of the most enjoyed rights and responsibilities of a corporation is that what an individual possesses, i.e., a corporation has the right to participate or enter into contracts, loan and borrow money, sue and be sued, hire employees, own assets and pay taxes. And one of the principal features of the corporation is limited liability, i.e., the shareholders have a right to be engaged in the profits but are not held personally liable for the company's debt.[1]

Corporate - the commercial vehicle has seen various forms of systemic reforms and adjustments, initially with the main concern of establishment of distinct personality for the enterprise, secondly limiting the liability and third, managing the company by a few representatives for the company as its agents and also as the agent of the shareholders. In the last about 75 years there have been serious challenges to the management of the corporate establishments especially on ethical grounds. Insider Trading becomes a most serious problem now-a-days faced by the corporations. The US economy was one of the leading economies to formulate insider trading regulations following UK and many other developed and developing countries.

Share market speculation is the act of getting involved in trading of an asset, or having a financial dealing that has a serious possibility of losing most or all of the initial investment, in presumption of a substantial gain. With speculation, the risk of loss is more than offset by the prospect of a huge profit; otherwise, there would be very little motivation or incentive to speculate. On the other hand Investment is actively using of money to make more money or, to say it another way, you make your money work for you. When you invest, you are purchasing an asset like shares, real estate or gold. The basic idea is to trade it at a future date when the value of these assets appreciates. While trading is a more short term activity than investment.

[1] Investopedia, http://www.investopedia.com/terms/c/corporation.asp (last visited on Apr. 26, 2016)

It's buying something at very low prices and selling it for a gain. Trading can be done in many fields and in divergent ways but the most important factor that distinguishes a trade from an investment is the length of time you hold on to the assets.

Insider Trading is a problem which predominantly implicates the nexus of the corporation behind such trading of stocks. A corporation includes buying and selling of shares in the open market, hence the trading on inside information becomes more easy and earlier it was subject to less stringent trade-disclosure rules. Not surprisingly, insiders exploit these rules to engage in indirect insider trading. Insider Trading is a term which has many definitions and significance. Insider trading takes place lawfully each and every day, when corporate insiders like the Officers, Directors or employees purchase or sell stock in their own companies within the purview of company policy and the regulations administering this trading. The category or variety of Insider trading we discuss here is the illegal sorts.[2]

Insider trading means to deal in a company's securities, such as stocks or options, by corporate insiders or their associates based on information emanating within the firm that would, once publically revealed, affect the prices of such security. Corporate insiders are persons whose employment with the firm (as executives, directors, or sometimes rank and file employees) or whose privileged ingress to the firms internal affairs (as large shareholders, consultants, accountants, lawyers, etc.) gives them valuable information.[3]

INSIDER TRADING LAWS IN US

Regulation and control of insider trading was initiated in the United States at the time of the twentieth century, when judges in several states became willing to remove corporate insiders' transactions with uninformed shareholders. Americans have counted largely on their courts to advance the law prohibiting and controlling insider trading. Although Congress gave Americans the directive to protect investors and keep their markets devoid of fraud, it has been the jurists, albeit at the counselling of the Commission and the United States Department of Justice, who have played the greatest and most important role in stipulating the law of insider trading. One of the earliest and abortive federal attempts to control insider trading arose after

[2] Thomas C. Newkirk and Melissa A. Robertson, *Insider Trading – A U.S. Perspective,* SPEECH BY SEC STAFF (Apr 19, 2016, 6:46PM), https://www.sec.gov/news/speech/speecharchive/1998/spch221.htm
[3] Stanislav Dolgopolov, *Insider Trading,* LIB. OF ECONOMICS AND LIBERTY (Apr 19, 2016, 6:54PM), http://www.econlib.org/library/Enc/InsiderTrading.html

the 1912-1913 congressional hearings in front of the Pujo Committee, which said that "the improper method of officers and directors in speculating upon inside and advanced information in relation to the action of their corporations may be restricted if not stopped."
After the United States stock market crash of 1929, Congress enacted two acts i.e. Securities Act,1933 and the Securities Exchange Act,1934, focused at supervising the abuses assumed to have contributed to the crash. The 1934 Act mentioned insider trading directly through Section 16(b)[4] and indirectly through Section 10(b)[5].

To implement section 10(b), the SEC adopted Rule 10b-5[6]. To establish a claim under Rule 10b-5, plaintiffs (including the SEC) must need to show the (i) Manipulation or Deception (through misrepresentation and/or omission); (ii) Materiality; (iii) "In Connection With" the purchase or sale of securities; (iv) Scienter- Private plaintiffs have the auxiliary burden of proving; (v) Standing - Purchaser/Seller Requirement; (vi) Reliance (presumed if there was an omission); (vii) Loss Causation; and (viii) Damages.

Broader Enforcement of Restrictions on insider trading began only in the 1960s, when the US Securities and Exchange Commission (SEC) gave their decisions in the cases *In re Cady Roberts &Co.*[7]and *SEC v. Texas Gulf Sulphur Co.*[8] using Rule 10b-5, a catch-all provision against securities fraud. In those and in the subsequent cases that shaped the assessment of the general insider trading prohibition, the SEC based its justification for regulation on the unjustness of dissimilar access to information, the breach and violation of fiduciary duties by insiders, and the misappropriation of the information as a form of property.[9]

---

[4] *Section16(b)*- prohibits short swing profits (profits realised in any period less than six months) by corporate insiders in their own corporation's stock except in very limited circumstances. It applies only to directors or officers of the corporation and those holding greater than 10 % of the stock and is designed to prevent insider trading by those most likely to be privy to important corporate information, Securities Exchange Act,1934.
[5] *Section 10(b)*- makes it unlawful for any person "to use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the [SEC] may prescribe, Securities Exchange Act,1934.
[6]*Rule 10b-5*- It shall be unlawful for any person, directly or indirectly
(a) to employ any device, scheme, or artifice to defraud,
(b) to make any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or
(c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of a security.
[7] 40 SEC 907 (1961).
[8] 401 F. 2d 833.
[9] Supra note 2.

Recent insider trading enforcement efforts have been unparalleled in their scope and impact, producing the lengthiest insider trading sentences in history and pushing the boundaries of existing law. Largely because of these efforts, insider trading law and practice could well be on the brink of substantial transformation. In a potentially landmark verdict the Second Circuit Court in *United States v. Newman*[10] sought to clarify insider trading law. In particular, the verdict takes a greater step in returning insider trading doctrine to its core concept: because insider trading liability is established in the specific intent crime of common law fraud, such liability requires both a breach of duty and intentional behaviour with respect to that breach.[11]

BREACH OF FIDUCIARY DUTY

Insider trading is the trading of the company's stocks and securities by individuals having access to confidential or non public information of the company. Taking advantage of this privileged access with the ulterior motive to derive unfair advantage or benefit is contemplated as a breach of the one's fiduciary duty. Congress has criminalised these insiders' misuse of non public information under the theory that the use fraudulently contravenes a fiduciary duty with which the company has charged the insider.[12]

A fiduciary duty is an agreement or commitment to act in the most suitable interest of another party. For example, a corporation's board member has a fiduciary duty towards the shareholders, a trustee has a fiduciary duty to the trust's beneficiaries, and an attorney has a fiduciary duty towards his client. A fiduciary duty exists whenever the association with the client involves a special trust or confidence. When a person agrees to act for another person in a fiduciary relationship, the law restrains the fiduciary from acting in any manner adverse or contrary or detrimental to the interest of the client.

Fiduciary Relationship and the Classical Theory of Insider Trading

The first theory under which a person can be held liable for insider trading under Rule 10b-5 is the so called "Classical Theory" of insider trading.[13] Under the classical theory, a person is

---

[10] 773 F.3d 438.

[11] J. Kelly Strader, *(Re)Conceptualizing Insider Trading: United States v. Newman and the Intent to Defraud*, 80 Brook. L. Rev. 1419 (2014-2015) (Apr 20, 2016, 7:30PM), http://heinonline.org/HOL/LandingPage?handle=hein.journals/brklr80&div=45&id=&page= last seen on Apr 20, 2016.

[12] LII, https://www.law.cornell.edu/wex/insider_trading (Last visited on Apr 21, 2016).

[13] See United States V. O'Hagan, 521 U.S. 642, 651-52 (1997) (stating the "classical theory" nomenclature was sanctioned by the court).

liable for insider trading if, on the basis of non public material information in his or her possession, he or she trades with persons to whom they owe a fiduciary duty to divulge the information. The duty of disclosure is generally premised on some type of relationship of trust and confidence, generally shorthanded as a "Fiduciary Relationship" between the person in possession of the material non public information and the buyer or seller of the securities.[14]

Fiduciary Relationships and the Tipper/Tippee Theory of Insider Trading

Another theory has approached the 'insider trading' form the perspective that a person who has received a tip in the form of material non public corporate information is liable which has been formalized in U.S. under Rule10b-5[15] of Securities Exchange Act, 1934. Such liability of insider trading is generally called the tipper/tippee theory of liability.[16]

Fiduciary Relationship and the Misappropriation Theory of Insider Trading

The third theory of liability for insider trading under Rule10b-5 is the "Misappropriation Theory". The essence of this theory is that a person is accountable for trading on the basis of material non public information if he has secured the information through trickery practiced on the source of the information.[17]

The "Misappropriation Theory" holds that a person commits deceit or fraud "in connection with" a security dealing, and infringes Section 10(b) and Rule 10b-5, when he misappropriates private information for securities trading purposes, in breach of a duty owed to the source of the information. Under this theory, a fiduciary's concealed, self serving use of a principal's information to deal in securities, in breach of a duty of loyalty and confidentiality, defrauds the principal of the exclusive use of that information.

INSIDER TRADING LAWS IN INDIA

---

[14] Harry S. Gerla, *Confidentiality agreements and the misappropriation theory of Insider Trading: Avoiding the fiduciary duty fetish,* UNIVERSITY OF DAYTON LAW REVIEW VOL 39:3 (Apr 20, 2016, 8:43PM), https://www.udayton.edu/law/_resources/documents/law_review/vol39_no3/avoiding_the_fiduciary_duty_fetish.pdf

[15] U.S. Securities Exchange Act, 1934, § 10b-5:
a) he or she trades on the basis of the information ;
b) the tipper is in breach of fiduciary duty owed to the corporation by supplying the information;
c) he or she knows or should have known of the tipper's breach of fiduciary duty.

[16] Dirks v. SEC, 463 U.S. 646 n.14 (1983), Id, at 661 (citing In re Investors Mgmt. Co., 44 SEC 633, 651 (1971) (Smith, Comm'r, concurring in result).

[17] United States v. O'Hagan, 521 U.S. 642, 652 (1997).

India was not very late in recognising the sabotage that insider trading can extort upon the rights of the public shareholders, corporate governance in India and the financial markets. In the view of the forgoing events the government established the Thomas Committee at its first attempt to regulate insider trading in the year 1948 under the chairmanship of P. J. Thomas. He was the then Economic Advisor to the Finance Ministry. Pursuant to the recommendation of the Thomas Committee, Sections 307[18] and 308[19] were introduced.[20] Thus this change paved the way for certain obligatory and compulsory disclosures by the directors and the managers, but was not very successful in achieving the aim of preventing the harm caused by insider trading. Eventually, the Sachar Committee and the Patel Committee were established in the years 1979 and 1986, to recommend measures for managing insider trading in India. The Patel Committee defined insider trading as "the trading in the shares of the company by the person who are in the management of the company or are close to them on the basis of undisclosed price sensitive information regarding the working of the company, which they posses but which is not available to others." The Committee also recommended for the amendment of SCRA,1956 to make exchanges to curb insider trading, unfair insider trading and unfair stock deals. However, Abid Hussain Committee, established in 1989, said that a person guilty of insider trading should be penalised both in the form of civil and criminal proceeding. The most important recommendation made by this committee was enactment of a separate statute for prevention of insider trading.

The recommendations made by these various committees led to the formulation of a comprehensive Regulation, i.e., SEBI(Insider Trading) Regulations,1992. This regulation was considerably amended in the year 2002 to cure certain escape clauses revealed in the cases of *Hindustan Liver Ltd v. SEBI*[21] & *Rakesh Agarwal v. SEBI*[22] and was renamed as the SEBI(Prohibition of Insider Trading)Regulations,1992. As on date, SEBI acts as a watchdog and regulates insider trading through the Insider Trading Regulations and the SEBI Act. The

[18] Companies Act, 1956, Section-307: Provides for the maintenance of a register by the companies to record the director's shareholding in the company.
[19] Companies Act, 1956, Section-308: Incorporates mandatory duty of the directors and persons deemed to be the directors to make disclosure of their shareholdings.
[20] P.J. Thomas, *Report on: The Regulation of the Stock Exchanges in India – 1948,* (Apr 21, 2016, 7:54PM) http://www.sebi.gov.in/History/HistoryReport1948.pdf
[21] (1998) 18 S.C.L. 311AA
[22] (2004) 1 Comp L. J. 193 SAT, 2004 49 SCL 351 SAT

SEBI(Prohibition of Insider Trading)Regulations,1992 prohibited fraudulent practice and a person involved in insider trading to be held guilty for such malpractice.

PROHIBITION OF INSIDER TRADING

Keeping pace with the policy of 'liberalized economy' the radical changes made in the Companies (Amendment) Act, 2013 has included 'insider trading' in particular to promote the effective compliance thereof. For example, Section 195 of the Companies Act, 2013 has made necessary provisions to define the expressions 'insider trading' and the punishment thereof on detection of the same[23].

THE ELEMENT OF MENS REA AND INSIDER TRADING

Mens Rea and Insider Trading in UK: The fundamental tenets of criminal law is that a crime consists of both mental and physical element. An act, hence, alone could not create the criminal liability unless it was associated with guilty state of mind.

In U. K. Insider Dealing Act, the offence of insider dealing requires a proof that the accused has intentionally exploit his position to engage in insider dealing. In other words, the accused must be shown to have been knowingly connected with the company in order that he is convicted of an offence of insider dealing.[24] The essential requirement that he/she is consciously connected or associated with the company means that if the accused is not aware of his connection with the company in whose securities or stocks he has traded in, he will not be accountable to be convicted and punished. Therefore, it will be necessary for the prosecution

---

[23] Companies Act, 2013, Section-195:
(1)- No person including any director or key managerial personnel of a company shall enter into insider trading: Provided that nothing contained in this sub-section shall apply to any communication required in the ordinary course of business or profession or employment or under any law.
(2)- If any person contravenes the provisions of this section, he shall be punishable with imprisonment for a term which may extend to five years or fine which shall not be less than five 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, or with both.
[24] JONATHAN R. MACEY, "INSIDER TRADING: ECONOMICS,POLITICS,AND POLICY, University Press of America (1st ed. 2000).

to institute that the individual charged with the offence of insider dealing has mindfully dealt in the securities knowing that he is linked with the company.[25]

Mens Rea and Insider Trading in US: Till the Great depression and subsequent stock market crash of 1929, the securities market in the United States is largely uncontrolled. For the first time in an attempt to control the market, the Securities Act and the Securities Exchange Act were sanctioned in 1933 and 1934 respectively. The Securities Exchange Act 1934 provided that a person would be held criminally liable for the violation of Section 10(b) prohibiting insider trading, the defendant's action must be expressly considered to contain a "wilful" violation of the securities crimes under Section 32(a) of the Act, thereby absolutely recognising the principle of mens rea. Subsequently, the SEC adopted Rule 10b-5, which made it illegal to engage in fraud or misrepresentation in connection with the purchase and sale of securities and imposed criminal liability for wilful contravention thereof.

However, the Supreme Court in the case of *US v. Murdock*[26], interpreted "wilfulness" as "an act which is intentional, or knowing, or voluntary, as distinguished from accidental" and "when it is used in a criminal statute it most of the time means an act done with a bad purpose" and "without justifiable excuse". Again in the case of *United States v. Chiarella*[27] the significance of mens rea as recognised by way of the misappropriation theory propounded for the very first time, which was described as a theory requiring a breach of fiduciary duty before dealing on inside information becomes unlawful. The US Supreme Court declared that trading on material non public information in itself was not enough to trigger the liability in the absence of breach of fiduciary duty[28].

RAJAT GUPTA SCAM: A BREAK THROUGH FOR INSIDER TRADING LAWS

Rajat Gupta was a member of the Board of Directors of The Goldman Sachs Group, Inc., the global financial services firm the headquarter of which is in New York. He was also the CEO of management consultancy firm Mckinsey & Company. Gupta and Rajratnam had a very close alliance. Gupta described Rajratnam as a "close friend" and was in frequent communication

[25] Bose Jaishree, "Insider trading perspectives and cases "The ICFAI University Press Publication, (1st ed., 2007) at 35-55.
[26] 290 U.S. 389 (1933)
[27] 445 U.S. 222 (1980)
[28] Ibid.

with him. Gupta was also involved in several financial ventures with Rajratnam who was the founder of The Galleon Group, a family of hedge funds that used to invest billions of dollars for its principals and clients. On September 23, 2008, at 3:15 pm Goldman Sachs held a special meeting of its Board of Directors. The meeting was to approve an investment of 5 billion dollars by Warren Buffett, who was the chairman, CEO and the largest shareholder of Berkshire Hathaway. Gupta participated in the board meeting via telephone. Ten minutes prior to 4:00 pm, at which the market closes, Rajratnam called Gupta and had around a 30-35 seconds call. Immediately after the phone call Rajratnam summoned Galleon Cofounder Gary Rosenbach after which Rosenbach started shouting "buy Goldman Sachs." In all the Goldman Sachs stock bought at the request of Rajratnam in the concluding minutes of the trading day cost more than $33 million and later that day $5 billion investment in Goldman Sachs was announced through Warren Buffett.

On October 23,2008, Goldman's chairman convened an unofficial board meeting to inform the board that the company's fourth-quarter result would be a loss. Gupta's telephone was connected to Rajratnam's direct line for some 12 minutes where Gupta disclosed information concerning Goldman's negative interim earnings. The next morning, on October 24, 2008, Rajratnam sold a total of 1,50,000 shares of Goldman Sachs stock, avoiding a loss of more than $3.8 million.

Verdict

The jury found Gupta guilty on four of the six allegations against him. One was conspiracy to commit securities fraud in violation of conspiracy to commit offence or to defraud United States[29], three substantive counts of securities fraud in violation of manipulative and deceptive practices[30] and penalties for using manipulative and deceptive practices.[31] Gupta was sentenced principally to 24 months' and was ordered to pay a $5 million fine. This Court granted his motion for bail pending appeal.

Mens Rea for Criminal Liability in India: Traditionally, criminal law requires the existence of mens rea for a person to be convicted of an offence. The requirement of mens rea embodies the fundamental principle that punishment requires personal fault. However, in the legal

---

[29] 18 U.S.C. § 371
[30] 15 U.S.C. § 78j
[31] 15 U.S.C. § 78ff

framework of India it does not seem to take the intent of the offender into account. Under the SEBI Act it is not obligatory to prove that the insider knowingly engaged in insider trading, i.e., mens rea is not an vital ingredient of the offence of insider trading. The focal point of culpability is on 'reasonable likelihood of access'. Consequently, a person may be convicted of insider trading as an offence regardless of whether he has committed it knowingly, deliberately or intentionally.

Section 24 of the Securities Exchange Board of India (SEBI) Act 1992, read with SEBI (Prohibition of Insider Trading) Regulations,1992, provides the basis for criminal liability for insider trading in India. The SEBI is empowered to lodge criminal prosecution under section 24 of the SEBI Act to ensure full compliance of the rules and regulations. Again, section 15G under chapter VIA of the SEBI Act provides for the penalty in case of insider trading in contravention of the SEBI Act and the SEBI Regulations passed under it.

One of such landmark decisions on criminal liability for insider trading is *Hindustan Lever Ltd. v. SEBI*[32]. Shortly before HLL revealed that it was merging with Brooke Bond Lipton Limited, HLL purchased eight hundred thousand shares of the latter company from Unit Trust of India (UTI). In this case the SAT concluded that that the purchase of shares was persuaded by the knowledge of the impending merger, SEBI was hardly put to prove that the transaction must actually be on the basis of inside information. Therefore the Companies Amendment Act, 2002 was brought which changed the requirement while in possession of unpublished price sensitive information from on the ground of UPSI. It was argued that for insider trading it is necessary to prove the misuse of fiduciary possession and that the transaction was undertaken to make a gain, profit or to avoid loss. These contentions were argued by the SAT and this case was held to be that of insider trading.

MAJOR DIFFERENCES IN THE INSIDER TRADING LAWS OF US, UK AND INDIA

The US has been one of the major and dominant country in enforcing the Insider Trading Regulations around the world. Although certain features of the insider trading regime in the UK are similar to their US counterpart, the UK statutes exhibit a great amount of difference

[32] (1998) 18 SCL 311 (AA).

than the US Insider Trading Regulations. These differences can have very significant practical consequences.

1. There are two laws governing the concept of Insider Trading in US i.e. the Securities Act of 1933 and the Securities Exchange Act of 1934 whilst there is only one law governing the problem of insider trading in UK i.e. Financial Service and Markets Act, 2000.
2. Insider Trading is both a civil and a criminal offence in US and UK but the difference lies on proving the *Mens Rea* and the Scienter. In US it is a necessary criteria to prove *Mens Rea* to establish a criminal liability and a scienter to civil liability but in UK scienter is not a necessary criteria to make a person liable of a civil offence.
3. The Securities Exchange Commission is the regulatory authority which looks after the problem of insider trading in US while in UK the regulatory authority is Financial Services Authority.
4. The punishment in United States for committing the offence of insider trading is twenty years in prison and a fine of five million US Dollars. The punishment for insider trading in UK is seven years imprisonment and unlimited fine.

INSIDER TRADING REGULATIONS 2015: AN OVERVIEW

India has put its effort and has made a move towards the ratification of the new insider trading regulations with the view to coordinate its laws on insider trading with that of the developed countries. SEBI in order to revise the law on insider trading and ensure that it is in consonance with the global best practices, constituted a committee under the chairmanship of Justice N.K Sodhi who drafted the Prohibition of Insider Trading Regulations,2015 containing thereof five chapters, two schedules and twelve sections. The Sodhi committee has made a wide range of recommendations for prohibition of insider trading in India and concentrated on making this area of regulation more predictable, precise and clear by suggesting a combination of principle based regulations.

The proposed regulations seek to extent the applicability of the regulations to any entity that has issued securities which are listed on stock exchange or intended to be so listed. The existing regulations are limited in their extent as they only extent to companies listed on a stock exchange in India.

The salient features of the new proposed regulations are[33]:

a. *Who is an Insider?* In the efforts to bring out a clearer and less enigmatic law, the proposed regulation have tailored the definition of "insider" into two categories of persons i.e. a connected person and those that have unpublished price sensitive information. The definition of an "insider" under the existing regulations also includes "a person deemed to be a connected person". This category includes a company under the same management or group, intermediaries, members, board of directors, etc. With the simplification of the definition of an insider, this category of "persons deemed to be connected persons" has been eliminated. The proposed regulations also seek to restrict this definition to those who are "in possession of" UPSI.

b. *Who is a Connected Person?* Any person associated with the company in a capacity that would allow such person to have access to unpublished price sensitive information relating to the company or whose association is reasonably expected to allow such access to the UPSI would be a "Connected Person". Hence, it can be deduced that the fact as to the actual possession of the unpublished price sensitive information is irrelevant to bring a charge as long as a reasonable expectation can be established.[34] The definition of 'Connected Person' under the 2015 Regulation also comprises of persons deemed to be connected persons. This combines two different and separate definitions of the 1992 Regulations. Additionally in the 2015 Regulations, anyone who has been in frequent contact with an officer of a company is termed as 'connected person'. The new definition of a 'connected person' comes through the curtailment of the scope of the definition "Relatives". The 2015 Regulations only covers immediate relatives such as spouse, parents, siblings, children's, person financially dependent.

c. *Definition of UPSI:* The New Regulation, 2015 has modified the definition of 'Unpublished Price Sensitive Information'. It has been defined to mean any information that is not generally available, which upon becoming generally available, is likely to materially affect the price of the securities to which it relates to. As per the definition of generally available information in the 2015 Regulations, that is accessible to the public on a non-discriminatory basis would be considered generally available.

[33] SEBI, http://www.sebi.gov.in/cms/sebi_data/attachdocs/1421319519608.pdf (Last visited on Apr 25, 2016).
[34] CS Swetha Subramanian, *Introduction of Insider Trading Regulations 2015,* Issue No. 18, Volume 02, February 16, 2015 (Apr 26, 2016, 4:56PM) http://www.icsi.edu/portals/0/e_cs_nitor_feb_2_issue_2015.pdf

Generally available information will ordinarily include information relating to the following:

- financial results
- Dividends
- change in the capital structure
- merger, demerger, acquisitions, delisting, disposals and expansion of business and such other transactions.
- changes in key management personnel

The 2015 Regulations asserts on the fact that the list of information given in the definition is only an illustrative guidance and to see whether a piece of information is UPSI or not. The examples in 2015 Regulations have two new entries as compared to the 1992 Regulations, being change in key managerial personnel and material events in accordance with the listing agreement.[35]

d. *Trading Plans:* Trading Plans are new concepts introduced under the 2015 Regulations, wherein insiders who are bound to possess UPSI all-round the year are permitted to formulate trading plans with proper safeguards. It has been introduced in accordance with Rule 10b-5 of the Securities Exchange Act, 1934. While the concept of trading plan is novel to India it has already been enforced in other jurisdictions like USA but in Indian context only efficacious implementation shall ensure whether the trading plans will really bring about compliant trading or not.

e. *Code of Conduct and Code of Fair Disclosure:* In the 1992 Regulation, Regulation-12 requires all listed companies; intermediaries correlated with the securities market and professional firms to frame and adopt the code of internal proceedings and conduct. Similarly, the 2015 Regulation obligates that all listed companies, organisations, intermediaries, self-regulatory organisations, clearing houses and public financial institutions should frame and adopt a “Code of Conduct" prescribed in Schedule B of the new Regulation.

In addition to this the 2015 Regulation prescribes a "Code of Fair Disclosure", which provides for practices and procedures to fair disclosure about appearance of UPSI that warrants public dissemination. As per Regulation- 8 of 2015 Regulation, the Board of

[35] Supra note 24.

Directors of every listed company shall compose and publish a code of fair disclosure on its website as per the format prescribed in Schedule A.

Types of disclosures in the 2015 Regulation are as follows[36]:

- Initial Disclosure- Required by every promoter, key managerial personnel and director of each and every company whose securities are listed on any of the recognised stock exchange to mandatorily disclose his holding of securities of the company as on the time of these regulations taking effect, to the company within thirty days of these regulations coming into force.
- Continuous Disclosure- Required by every promoter, employee and director of every company to mandatorily disclose to the company the number of such securities acquired or disposed of within two trading days of such transactions if the value of securities traded, whether in one transaction or a series of transactions over any calendar quarter, which aggregates to a traded value in excess of ten lakh rupees or such other value as may be specified.
- Additional Disclosure- also required for all holdings in securities of that company held by any other connected person or class of connected persons. Such disclosures shall be made at the periodic frequency as determined by the company with the purpose of monitoring compliance with the present 2015 Regulation.

f. Notional Trading : Another important development in relation to notional trading windows which are used as an instrument to monitor complaint trading by designated persons within the company. The concept of notional trading windows has also been implemented to external agencies having contractual or fiduciary relationships with the company such as law firms, accountancy firms etc. The time period for such re- opening of trading windows has been set to 48 hours after the UPSI becomes generally available.

CONCLUSION

Insider Trading is crafty for many number of reasons. However, although most argue their protest to insider trading because it is simply inequitable, perhaps the greatest outcome is that insider trading makes the market less efficient. Although there are many other competing

[36] Kashyap, Amit K, *Financial Market Regulations and Legal Challenges in South Asia* (Apr 23, 2016, 6:44PM)

avenues for market inefficiency, new financial instruments and insights increasingly allow us to solve these competing inefficiencies. The secretive nature of insider trading makes detection difficult, conviction more difficult, and the huge sums involved difficult to deter. Insider trading is one of the most disputable facets of securities regulation, even among the law and economics faction. One set of scholars favours deregulation of insider trading, permitting corporations to set their own insider trading policies by contract. Another set of law and economics scholars, in distinction, contends that the property right to inside information should be assigned to the corporation and not excused upon contractual reassignment. Deregulatory arguments are typically premised on the claims that insider trading assists market efficiency or that assigning the property right to inside information to managers is an methodical reimbursement scheme. Public choice analysis is also a predominant of the deregulatory literature, arguing that the insider trading disallowance benefits market professionals and managers rather than investors. The argument in favour of regulating insider trading traditionally was found and based on fairness issues, which predictably have had little resistance in the law and economics fraternity. Instead, the economic argument in favour of mandatory insider trading prohibitions has typically rested on some alternative of the economics of property rights in information.

To downsize the gaps and to make the existing norms more secure, the Securities and Exchange Board of India (SEBI), on May 15, 2015 introduced the SEBI (Prohibition of Insider Trading) Regulations, 2015, that replaced the existing SEBI (Prohibition of Insider Trading) Regulations, 1992. The 2015 regulations appear to be promising, favourable, more practical, and largely in line with the global outlook to insider trading. They also seem to furnish and provide better compliance and enforcement. It is, therefore, only unsurprising for everyone to be talking about the new norms. Most financial regulations require persistent and constant modifications to keep pace with the ever developing and progressing market dynamics. Insider trading is no different at all. The existing regulations came into force in 1992. In the past two decades, the laws and perception of insider trading (both global and domestic) have evolved significantly. Although compliance with these codes appears to be unmanageable and inconvenient, especially for companies and business houses with large shareholder and employee bases. For illustration, in a company with 10,000 staff, it would require dedicated resources just to monitor trading activities of the employees. However, there’s hope that the

regulations are interpreted by courts and authorities in an ongoing manner and timely clarifications are issued by the capital market regulator.