COMPARATIVE ANALYSIS OF FRONT RUNNING REGULATIONS IN INDIA AND SINGAPORE

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INTRODUCTION

Front running is basically trading of the stock or any other financial asset by an intermediary (broker) who already has advance knowledge of future transaction that is bound to affect the price of that stock or financial asset.

Here the basic point is that brokers should not use the private information which they have regarding future transactions for their own personal advantage. Various judicial decisions have now included private individuals equally liable for prosecution at par with the intermediaries. Any gains on account of these transactions are illegal in Indian law and bound to attract punishment.

This practice if allowed uncheck disturbs the level playing field and is against the principle of a fair business practice. In India Securities and Exchange Board of India (SEBI) has been authorized to investigate these offences and impose penalties on persons violating the law. Any dispute arising out of the orders passed by SEBI can be challenged by individuals in the Securities Appellate Tribunal (SAT).

Definition of Front running as per Major Law Lexicon by P Ramanatha Aiyar

Buying or Selling securities ahead of a large order so as to benefit from subsequent price move.

This denotes persons dealing in the market, knowing that a large transaction will take place in the near future and the parties are likely to move in their favour.

The illegal private trading by a broker or market maker who has a prior knowledge of a forthcoming large movement in prices.

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UNDERSTANDING THE CONCEPT OF FRONT RUNNING

Many a times it has been seen that the concept of Front running is often confused with Insider trading. However both are different concepts altogether. Let us try to understand it with an example-

Suppose a broker receives a request to purchase 40,000 shares of a Company A. He keeps the order from the client and executes an order for his personal account before he makes transactions on behalf of his client. Now when he executes the order for his client of purchasing 40,000 shares, the price of shares automatically increases owing to increase in sudden demand. This rise creates a window of opportunity for the broker to make profits without actually doing anything. This type of profit is considered as a unfair trade practice and has legal consequences.

FRONT RUNNING UNDER INDIA LAW

In India Front running has been recognized as an undesirable and manipulative market practice. SEBI already was quick to recognize this issue in its Consultative Paper way back in March 1995. Subsequently it was brought within the ambit of the then SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations 1995.

Presently Front running in India is being regulated by SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003 (PFUTP Regulations) . According to Regulation 4(2)(q) of the PFUTP Regulations-

"An intermediary buying or selling securities in advance of a substantial client order or whereby a futures or option position is taken about an impending transaction in the same or related futures or options contract,"

Apart from this there are various other provisions specified in the SEBI Act 1992 which can used for penalising people indulging in Front Running-

a. Under SEBI Act, any person who indulges in fraudulent and unfair trade practices shall be liable with penalty which may extend to 25 crore Rupees, or three times the amount of profits generated through such transactions

b. Section 11 and 11B of the SEBI Act 1992 empowers the SEBI to restrict people from accessing the securities market to carry out any kind of transaction. It can suspend trading of any security which it suspects to be a part of front running.
c. Section 24 of the SEBI Act empowers SEBI to award penalty for the contravention of the Act. It also has a provision of a jail term along with a fine.
d. Also SEBI can initiate civil proceedings under SEBI (Intermediaries) Regulation, 2008.

As we can see above, we have ample legal provisions relating to Front Running in India. However there are certain issues as well. There is no clear definition of the term Front Running in any Act. It is being treated just as an unfair trade practice. Because of this lack of specific definition various court judgments in the past have tried to interpret various provisions of the law to make up for this.

Supreme Court in its order in 2018 had also pointed out the need for a well defined and a clear law on Front running. In the order SC judges, Justices NV Ramanna and Ranjan Gogoi highlighted the requirement of a comprehensive law with respect to SEBI Prevention of Fraudulent and Unfair Trade Practices (PFUTP) norms. According to the Apex Court the SEBI Regulations are not adequate to fulfill their original obligations.

The Supreme Court ruling said:

"SEBI's PFTUP norms do not explicitly list aspects pertaining to non-intermediary individual's liability in front running matters, whilst the front running is specifically defined under SEBI circular. The unfair and fraudulent practices have not been adequately defined by SEBI.

SEBI Act does not prescribe or specify as to which practice would be considered to be fraudulent and unfair trade practices. While the fraudulent and unfair trade practices are commonly understood, it would be desirable if these practices are defined specifically."

Justice Ranjan Gogoi said "an unclear picture emerged from undefined concepts contained in the Act and the Regulations framed there under, comprehensive legislations can bring about more clarity and certainty on these aspects."

Keeping in view of the Supreme Court order the government must bring appropriate amendments in the SEBI Act and regulations to make it more comprehensive.

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IMPORTANT CASES AND CASE LAWS

Vibha Sharma & Anr vs Securities and Exchange Board of India

Taking a different position from its earlier judgment the Securities and Appellate Tribunal (SAT) ruled that front running even by a person other than an intermediary is illegal. The important point to note here is SAT had given a contradictory judgment in the Dipak Patel vs SEBI back in 2012.

SEBI vs Shri Kanhaiyalal Baldevbhai Patel

The Supreme court in this land mark judgment held that front running by a non-intermediary has also been brought under the ambit of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations 2003.

Anandkumar Baldevi vs SEBI (2019)

The Supreme Court in its important judgment had categorized front running into 3 types-

TIPEE TRADING (Trading by third party after being tipped by a broker)

SELF FRONT RUNNING (Trading of stocks by the owners of blocks by indulging into hedging)

TRADING AHEAD (Trading of stocks by the broker who takes undue advantage of the knowledge of his customer's orders)

It has to kept in mind that for declaring any person guilty mens rea has to be established. Trades done in synchronization are not illegal per se, the parties must have the intention of manipulation. In *Shubhkam Securities Pvt Ltd vs SEBI* this was the important point which was highlighted.

Axis Mutual Fund (Case Study)

This is a very popular case related to front running where Axis Bank had terminated services of their top executives who were facing charges of front running.

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The Axis Bank AMF which is the Asset Management Wing of the Axis Bank is one of the largest fund houses in the country. Some reports broke out in the media regarding the private gains of some of the dealers of the fund house which caught the attention of regulating authorities. Recently the capital markets regulator SEBI carried out search and seizure at 16 entities including offices of Axis Mutual Fund, stock brokers and individuals as part of the current probe into alleged wrongdoings by two former fund managers of Axis Mutual Fund.

HDFC AMC (Case Study)

The case was concerned with Sections 11(1) , Section 11(4)(d) and Section 11B of the Securities and Exchange Board of India Act, 1992 with respect to front running of trades of HDFC Asset Management Company Limited by 'Sanghvi group' and 'Kalpana group'.

In the year 2007, SEBI unearthed numerous circumstances of front running by dealer of HDFC Asset Management Company. It was estimated that unlawful gains were 1.52 crores and 2.86 crores respectively. SEBI made a settlement with HDFC AMC and imposed a fine of 2 crore rupees on 4 entities in addition to penalty.

FRONT RUNNING UNDER SINGAPORE LAW

Singapore has very stringent provisions when it comes to white collar crimes. Front running in Singapore is regulated by Insider Trading laws of the country. The Monetary Authority of Singapore (MAS) functions not only as a Central Bank in Singapore but it also has the responsibility of financial regulations pertaining to money, banking, insurance and securities as well. Hence powers to investigate and award penalties for front running rests with the Central Bank. There have been various debates in Singapore regarding various aspects of the law against insider trading and front running practices. People and policy makers have expressed divergent views on this issue. These contrasting views were also highlighted by the Court of Appeal in *Lew Chee Fai Kevin vs Monetary Authority of Singapore (MAS).*

Information Connected Approach has been adopted in Singapore while dealing with matters of Insider Trading as liability can be found by identifying as to what qualifies as insider

information. It helps in establishment of a non-public information and it's link with person holding such information.

The various penal provisons in Singapore includes-

Section 218 of the Securities and Futures Act 2001(SFA) clearly sets out the offence of insider trading. However before applying this law certain points need to be analysed as to whether the person has intentionally kept the information which he knows to have material affect.

The law in Singapore has various Criminal and Civil provisions. For the occurrence of the same offence both civil and criminal proceedings are not conducted. Not every offence relating to insider trading leads to imprisonments.

Under Section 232(1) of the Securities and Futures Act, the Monetary Authority of Singapore can initiate civil proceedings against the wrong doers. Penalty upto three times the profit gained can be ordered by the court.

However if the wrongdoer could not make any profits or suffers a loss from his actions then he can penalized anything between 50,000$ to 2million$.

Section 221 of SFA provides for criminal penalties in contravention of the section 218 of the Act. A fine of 250,000$ or a sentence ut po 7 years or both can be given to the wrongdoers.

Section 333 of SFA elaborates as to how a corporation can be fined up to twice the maximum amount the relevant office has prescribed. When a Company is found to contravened provisions the Act, the director along with executive officer and secretary shall be held guilty if they had information about the illegal transaction.

Regulation 44 of Securities and Futures (licensing and conduct of Business) Regulations prohibits a representative of a holder of a capital markets service license, when acting on his own account or on behalf of a person associated with him or connected to him, from entering into a transaction for the purchase or sell shares in that same counter and he had not complied with those instructions. The penalty for contravention is a fine not exceeding $100,000 or imprisonment for a term not exceeding 12 months.

Insider Trading under Section 219(2)(a) of the Securities and Futures Act. It prohibits a person who is not connected to any corporation but is in possession of materially price sensitive

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information, which he is aware about and not generally available, and the information having material effect on the price from subscribing for, purchasing and selling, or entering into an agreement to subscribe for, purchase or sell these securities.

Insider Trading under Section 219(2)(b) of the Securities and Futures Act. It prohibits a person who is not connected to any corporation but is in possession of certain price sensitive information, which he knows or ought to know is materially price sensitive and not generally available, and the information would have a material effect on the price or value of securities, from procuring another person to subscribe for, purchase or sell, or to enter into an agreement to subscribe for, purchase or sell these securities. The penalty for contravention of section 219 of the SFA upon conviction is a fine not exceeding 250,000$ or imprisonment for a term not exceeding 7 years or both.

Section 109 of the Penal Code provides that anyone who abets an offence shall be punished with punishment for the offence abetted if the Penal Code has no expressed punishment set out.

CASE STUDY

The Monetary Authority of Singapore (MAS) in one its first front running cases being prosecuted as insider trading upheld more than 300 charges on three dealers from First State Investments Singapore. The three accused were sentences to 36 months, 30 months, 20 months respectively. They had carried out front running transactions for 7 long years. The news was followed world wide as it has been the first time that people were imprisoned in Singapore for this offence. The accused were primarily booked under Section 219(2)(b) and 219(2)(a) of Securities and Futures Act 2001.

CONCLUSION

As we can see India and Singapore have enacted various laws when it comes to front running but there is a lack of clearly defined specific law on the subject. Apart from regulations a lot also depends on the nature of law enforcement in both the countries. In India we need to make sure that our regulating agencies have access to various new technologies to monitor various

transactions. There must a mechanism of making a cordial environment for whistle blowers to come forward. As per the annual report of SEBI very few cases of front running have been taken up for scrutiny during the Covid time. Harsher punishments need to be introduced in India on the lines of Singapore. India cannot become a developed economy without proper regulators who provide level playing fields. The observations of Supreme Court judges must be considered in this regard.

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