

ROLE PLAYED
BY SEBI
IN
RESTRICTING
INSIDER
TRADING

Coverage

1. Background & History
2. Governing Regulations
3. Objectives
4. Definitions
5. Duties of Compliance Officer
6. Restrictions on communication and trading by insiders
7. Trading Plans
8. Disclosure of Trading by Insiders
9. Code of Fair disclosures and conduct
10. Code of Conduct
11. Trading Window
12. Pre dealing approval
13. Penalties
14. References

HISTORY BEHIND INSIDER TRADING IN INDIA:

Insider trading in India was unhindered in its 130 year old stock market till about 1970.

The earliest record of dealings in securities in India traces back to East India Company. The first Indian legislature to regulate securities market was Bombay Securities Contract Act, 1925, it was enacted to regulate purchase and sale of securities. However, the legislature had several shortcomings which resulted into investors making huge losses during the period 1928 to 1938. Therefore government was compelled to appoint certain committees to assess the shortcomings of the legislation.

The Defense of India Act, 1939 included a provision relation to Capital Issue which stipulated that prior Government approval was mandatory for capital issue. When India got independence in 1947 the same rule was incorporated in **Capital Issue (Control) Act, 1947**. Under this act, the office of Controller of Capital issue was set up, which was authority to approve issue of securities, the amount, type and price of securities etc. The Act was however, repealed in 1992 and the office of CCI was abolished in 1992, as a part of liberalization process.

The Stock Market witnessed different phases during 1946-1947. Stock Market being an integral part of country's Financial system there was a need for tightening government control on stock markets. In the view of foregoing government constituted the Thomas Committee under the Chairmanship of P.J. Thomas the adviser to Finance Ministry. The Committee advised that an Independent and quasi-judicial authority with the fullest powers of supervision could only discharge such a function and thus, recommended setting up of National Investment Commission.

Instances of Insider Trading in India were 1st reported in 1940s. Directors, Agents, Auditors and other officers were found to be using insider information for profitably speculating in securities of their own Company. Thomas Committee had analysed these instances and observed that insider trading occurred due to (i) the possession of information by these people; (ii) before everybody else; (iii) regarding the changes in the Economic condition of Companies and particularly, regarding the size of dividends to be declared, or issue of Bonus shares.

Thomas Committee had pointed out the lack of a special legislation to deal with “unfair use of insider information” in 1948 itself, it took a few decades to actually formulate a legislation to curb insider trading.

In 1979, the Sachar Committee recommended amendments to the companies Act, 1956 to restrict prohibit the dealings of employees. Penalties were also suggested to prevent the insider trading.

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

GOVERNING REGULATIONS:

- Securities & Exchange Board Of India Act, 1992
- SEBI (Insider Trading) Regulations, 1992
- SEBI (Prohibition of Insider Trading) (Amendment) Regulations, 2002
- SEBI (Prohibition of Insider Trading) (Amendment) Regulations, 2003
- SEBI (Prohibition of Insider Trading) (Amendment) Regulations, 2008
- SEBI (Prohibition of Insider Trading) (Amendment) Regulations, 2011
- SEBI (Prohibition of Insider Trading) Regulations, 2015

REGULATORY ASPECTS OF PROHIBITION OF INSIDER TRADING:

- SEBI (Prohibition of Insider Trading) Regulations 2015.

WHY THERE IS NEED FOR PROHIBITION OF INSIDER TRADING???

As per SEBI the Prohibition of Insider Trading is required to make securities market:

- Fair and Transparent.
- To have a Level Playing Field for all the participants in the market.
- For free flow of information and avoid information asymmetry

DEFINITIONS

1. INSIDER Regulation 2(g)

Insider is the person who is “connected” with the company, who could have the unpublished price sensitive information or receive the information from somebody in the company.

Under the new definition, an insider would mean a person in possession of or has access to price-sensitive information or Connected Person.

SEBI defines ‘Insider’ to include persons connected on the basis of being in any contractual, fiduciary or employment relationship that allows such people access to unpublished price sensitive information (UPSI).

2. TRADING Regulation 2(1)

Trading means and includes

- Subscribing

- Buying
- Selling
- Dealing
- Agreeing to buy sell, subscribe, deal in any securities

3. INSIDER TRADING

Insider trading is dealing in securities of a listed company by any person who has knowledge of material “inside” information which is not known to the general public.

4. CONNECTED PERSON Regulation 2(d)

- Any person who is or has been associated with company, in any manner, during the six months prior to the concerned act,
- An immediate relative to the connected person,
- A banker of the company,
- An official of stock Exchange or of clearing corporation,
- A holding/associate/subsidiary company,

This is a new definition included in the new regulations by SEBI, where in, it defines “connected person” as anyone who is or has during the six months prior to the act been associated with a company, directly or indirectly in any capacity, including by reason of frequent communication with its officers or by being in any contractual, fiduciary or employment relationship or by being a director, officer or employee. It also covers persons holding any position that allows access to unpublished price-sensitive information.

The above definition of connected person also brings into its ambit of those persons who may not seemingly occupy any position in a company but are in regular touch with the company and its officers who are involved in the day to day operations of the Company.

5. INSIDER TRADERS

Corporate officers, directors, and employees who traded the corporate securities after learning of significant, confidential corporate developments.

Friends, business associates, family members and employees of law, banking and brokerage firms who were given such information to provide services to the corporation whose securities they traded.

6. GENERALLY AVAILABLE INFORMATION

Regulations 2(e)

Information that is accessible to the public on a non-discriminatory basis.

Note: It is intended to define what constitutes generally available information so that it is easier to crystallize and appreciate what unpublished price sensitive information is. Information published on the website of a stock exchange, would ordinarily be considered generally available.

Threshold Limit for Disclosures [including KMP's and Employees]:

The Disclosures shall be made by Promoter's/ Director's/ KMP as well as employees on crossing the threshold of Rs. 10 Lakhs in value as prescribed within two trading days of such transaction, if the value of the securities traded, whether in one transactions or a serious of transactions over any calendar quarter.

7. UNPUBLISHED PRICE SENSITIVE INFORMATION

Regulation 2(n)

Information, relating to a company or its securities, directly or indirectly, that is not generally available which upon becoming generally available, is likely to materially affect the price of the securities and shall, ordinarily but not restricted to, information relating to the following:

- 1) Financial results
- 2) Dividends
- 3) Change in capital structure
- 4) Mergers, de-mergers, acquisitions, delisting, disposals and expansion of business and such other transactions
- 5) Changes in key managerial personnel and
- 6) Material events in accordance with the listing agreement.

Communication or procurement of unpublished price sensitive information:

- I. No insider shall communicate, provide or allow access to any UPSI except where such communication is in furtherance of legitimate purposes, performance of duties or discharge of legal obligations, likewise
- II. No person shall procure from or cause the communication by any insider of UPSI except in furtherance of legitimate purposes, performance of duties or discharge of legal obligations.
- III. Unpublished PSI may be communicated, provided, allowed access to or procured, in connection with a transaction that would entail an obligation to make an open offer under the takeover regulations where the board of directors of the company is of informed opinion that the proposed transaction is in the best interests of the company. In such cases, the board of directors shall require the parties to execute agreements to contract confidentiality and non-disclosure obligations.
- IV. Unpublished PSI may be communicated, provided, allowed access to or procured where the board of directors of the company is of informed opinion that the proposed transaction is in the best interests of the company and UPSI is disseminated to be made generally available at least 2 working days prior to the proposed transaction being effected in such form as the Board of Directors may determine.

8. IMMEDIATE RELATIVE Regulation 2(f)

Means a spouse of a person, and includes parent, sibling, and child on such person or of spouse, any of whom is either dependent financially on such person, or consults such person in taking decisions relating to trading in securities.

DUTIES OF COMPLIANCE OFFICER:

The new SEBI (Prohibition of Insider Trading) Regulations, 2015 defines compliance officer under Regulation 2 (c) which means any senior officer, designated so and reporting to the board of directors or head of organization in case board is not there, who is financially literate and capable of appreciating the requirements of legal and regulatory compliance under these regulations and who shall be responsible for compliance of policies, procedures, maintenance of records, monitoring adherence to the rules of preservation of unpublished price sensitive information, monitoring of trades and the implementation of codes

specified in this regulation under the overall supervision of board of directors or the head of the organization, as the case may be .

The new SEBI (Prohibition of Insider Trading) Regulations, 2015 cast certain duties on the Compliance Officer of the company who is appointed under the regulations including monitoring and compliances of requirements under these regulations. Such duties are to be undertaken very prudently.

For instance, in case of employees where there is no requirement of initial disclosure but continual disclosure is required to be made in case of triggering the threshold. In such a case, it would be difficult for the compliance officer to check whether compliances are made or not. Above this, the regulations also put an onus on the company to intimate trading crossing a threshold of Rs. 10 Lakh in value irrespective of the disclosure receive by the employee as the Regulation 7(2)(b) states as follows:

“Every Company shall notify the particulars of such trading to the stock exchange on which the securities are listed within two trading days of receipt of the disclosure or from becoming aware of such information.”

As per the new SEBI (Prohibition of Insider Trading) 2015, it is very clear that the company shall put in a place a system to monitor trading of all its employees unlike of designated persons as were required under earlier regulations.

RESTRICTIONS ON COMMUNICATION:

- 1) No insider shall communicate, provide, or allow access to any unpublished price sensitive information, relating to a company or securities listed or proposed to be listed, to any person including other insiders except where such communication is in furtherance of legitimate purposes performance of duties or discharge of legal obligations.
- 2) No person shall 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, except in furtherance of legitimate purposes, performance of duties or discharge of legal obligations

- 3) Notwithstanding anything contained in this regulation, an unpublished price sensitive information may be communicated, provided, allowed access to or procured, in connection with a transaction that would:-
- (i) entail an obligation to make an open offer under the takeover regulations where the board of directors of the company is of informed opinion that the proposed transaction is in the best interests of the company
 - (ii) not attract the obligation to make an open offer under the takeover regulations but where the board of directors of the company is of informed opinion that the proposed transaction is in the best interests of the company and the information that constitute unpublished price sensitive information is disseminated to be made generally available at least two trading days prior to the proposed transaction being effected in such form as the board of directors may determine.

Trading when in possession of unpublished price sensitive information.

- 1) No insider shall trade in securities that are listed or proposed to be listed on a stock exchange when in possession of unpublished price sensitive information:

Provided that the insider may prove his innocence by demonstrating the circumstances including the following: -

- (i) the transaction is an off-market inter-se transfer between promoters who were in possession of the same unpublished price sensitive information without being in breach of regulation 3 and both parties had made a conscious and informed trade decision;
- (ii) in the case of non-individual insiders: -
 - a) the individuals who were in possession of such unpublished price sensitive information were different from the individuals taking trading decisions and such decision-making individuals were not in possession of such unpublished price sensitive information when they took the decision to trade; and
 - b) appropriate and adequate arrangements were in place to ensure that these regulations are not violated and no unpublished price sensitive information was communicated by the individuals possessing the information to the individuals taking trading decisions and there is no evidence of such arrangements having been breached;

- (iii) the trades were pursuant to a trading plan set up in accordance with regulation 5.
- 2) In the case of connected persons the onus of establishing, that they were not in possession of unpublished price sensitive information, shall be on such connected persons and in other cases, the onus would be on the Board.
- 3) The Board may specify such standards and requirements, from time to time, as it may deem necessary for the purpose of these regulations.

TRADING PLANS: Regulation 5

An insider shall be entitled to formulate a trading plan and present it to the compliance officer for approval and public disclosure pursuant to which trades may be carried out on his behalf in accordance with such plan.

This provision intends to give an option to persons who may be perpetually in possession of unpublished price sensitive information and enabling them to trade in securities in a compliant manner. This provision would enable the formulation of a trading plan by an insider to enable him to plan for trades to be executed in future. By doing so, the insider who is in possession of unpublished price sensitive information and formulated a Trading Plan approved by the Compliance Officer subsequently would not be prohibited from execution of such trades as per the trading plan approved by the Compliance Officer on such stand that he/she had pre-decided the trade even before such unpublished price sensitive information available to them.

The Trading plan shall comply with the requirements as follows:

- i) It shall be submitted for a minimum period of 12 months.
- ii) No Overlapping of plan with the existing plan submitted by Insider
- iii) It shall set out either the value of trades to be effected or the number of securities to be traded along with the nature of the trade and the intervals at, or dates on which such trades shall be effected.

iv) Trading can only commence only after 6 months from public disclosure of plan.

v) No trading between 20th day prior to closure of financial period and 2nd trading day after disclosure of financial results.

vi) Compliance Officer to approve the plan.

vii) The trading plan once approved shall be irrevocable and the insider shall mandatorily have to implement the plan, without being entitled to either deviate from it or to execute any trade in the securities outside the scope of the trading plan. (Except in few case like where insider is in possession of price sensitive information at the time of formulations of the plan and such information has not become generally available at the time of the commencement of implementation.)

viii) Upon approval of the trading plan, the compliance officer shall notify the plan to the stock exchanges on which the securities are listed.

DISCLOSURE OF TRADING BY INSIDERS:

Regulation 6

The disclosure to be made by any person shall also include those persons who are immediate relatives to such person who have made the trading, and it also includes any other person for whom such person takes trading decisions.

The disclosures of trading in securities shall also include trading in derivatives of securities and the traded value of the derivatives shall be taken into account. (please note that section 194 of CA, 2013 prohibits Director or KMP from entering into forward dealings etc.)

Duration of Maintenance of Disclosures:

The disclosures made under these regulations shall be maintained by the company for a minimum period of five years.

Classification of Disclosures:

- a) Initial Disclosures
- b) Continual Disclosures

Disclosures by certain persons: Regulation 7

1) Initial Disclosure:

- a) Every promoter, KMP and Director of every company whose securities are listed on any recognized stock exchange shall disclose his/her holding of securities of the company as on the date of these regulations taking effect, to the company within 30 days of these regulations taking effect. (Effective Date: May 15, 2015, Due Date: June 14, 2015)
- b) Every person on appointment as a KMP or a director of the company or upon becoming a promoter shall disclose his holding of securities of the company as on the date of appointment or becoming a promoter to the company within seven days of such appointment or becoming a promoter.

2) Continual Disclosures:

- a) Every promoter, employee and Director of every company shall disclose to the company the number of such securities acquired or disposed of within two working days of such transaction if the value of the securities traded, whether in one transaction or a series of transactions over any calendar quarter, aggregates to a traded value in excess of ten lakh rupees or such other value as may be specified.
- b) Every company shall notify the particulars of such trading to the Stock Exchanges on which the securities are listed within two trading days of receipt of the disclosure or from becoming aware of such information.

DISCLOSURE BY OTHER CONNECTED PERSONS: regulation 7 (3)

Any company whose securities are listed on a stock exchange may, at its discretion require any other connected person or class of connected persons to make disclosures of holding and trading in securities of the company in such form and

at such frequency as may be determined by the company in order to monitor compliance with these regulations.

Disclosures:

WHO	WHAT	WHEN
7 (1) (a) (b) Promoter, director & KMP of listed company and any other person as may be determined by the Company	Disclose its holdings of securities including transaction in derivatives to the company as on the date of regulation coming into force or date of appointment or becoming promoter	Within 30 days from these regulations taking effect & Within 7 days of appointment or becoming a promoter
7 (2) (a) Promoter, director or employee of company and any other person as may be determined by the Company	Securities including transaction in derivatives acquired or disposed by promoter, director or employee of company and by immediate relative of their and on behalf of person for whom such person takes decision shall disclose to the company.	In any calendar quarter, value of traded securities exceeds Rs 10 lakh with single or series of transaction.

Code of Fair Disclosure and conduct: regulation 8

Companies need to establish a code of practices and procedures for fair disclosures of unpublished price sensitive information.

The new SEBI (Prohibition of Insider Trading) Regulations, 2015 intends the listed entities to formulate a stated framework and policy for fair disclosure of events and occurrences that could impact price discovery in the market for its securities.

The principles as set out in the schedule are:

- i) Equality of access to information.

- ii) Publication of policies such as dividend, inorganic growth pursuits, calls and meeting with analysts.
- iii) Publication of such calls and meeting etc.

The Code of practices and procedures for fair disclosures of unpublished price sensitive information and every amendment thereto shall be promptly intimated to the stock exchanges where the securities are listed.

CODE OF CONDUCT: Regulation 9

Every Listed Company shall formulate a code of conduct to regulate, monitor and report trading by its employees and other connected persons towards achieving compliance with these regulations.

Every listed company formulating a code of conduct shall identify and designate a compliance officer to administer the code of conduct and other requirements under these regulations.

TRADING WINDOW

- “Trading window” means a period for trading in Company's securities as specified by the Company from time to time.
- Other than the period for which trading window is closed, the same shall remain open for dealing in securities of the Company.
- Trading window is closed for the following reasons:
 - a) Declaration of Financial results
 - b) Declaration of dividend
 - c) Issue of securities
 - d) Major expansion plans
 - e) Amalgamations, mergers, takeovers and buybacks
 - f) Disposal of undertaking
 - g) Any significant changes

PRE - DEALING APPROVAL

- Designated Person or his Dependents Who intend to deal in securities of the Company Who have access to price sensitive information of the company whose cumulative dealing exceeds 25,000 Shares per month and/or trade in Non - convertible Debentures exceeds Rs. 1 mn (market value), in a month have to take Pre dealing Approval from the Compliance officer of the Company.

PENALTIES:

Monetary Penalty: Section 15G of SEBI Act, 1992 imposes penalty of at least Rs.10 lacs, which may extend to Rs.25 Crore or three times of profits made from insider trading whichever is higher.

Imprisonment: Section 24 of SEBI Act, 1992 even goes to the extent of imprisonment upto 10 years or fine upto 25 Crore, or both, for any offences pertaining to contravention of the provisions of the Act.

NAME OF THE COMPANY	VIOLATION	ACTION TAKEN BY SEBI
Multi Commodity Exchange (MCX) and Financial Technologies (Now, 63 Moons)	13 individuals including promoters and KMP traded in the shares of MCX and FTIL based on UPSI	Impounded 126 crore benefitted from trading Not to dispose of or alienate any of their assets till the penalty is credited to an escrow account
Piramal Enterprises Ltd	Directors did not announce the mandatory closure of trading window	Has imposed a fine of 6 lakh on them.
MAN Industries Ltd	Failure of dissemination of price sensitive information to the stock exchanges on time	Joint penalty of 25 lakh on MAN Industries, its chairman and four officials for alleged violations

Mahindra & Mahindra Ltd	Sale of shares during closure of the trading window	Imposed a fine of 2 lakh on a general manager
ITC Ltd	Failure in disclosure of sale of shares to Stock Exchanges	Has imposed a fine of 5 lakh on HR manager who failed to disclose
Satyam Computer Services Ltd	Failure to announce the mandatory closure of trading window during UPSI activity	Barred Ramalinga Raju and four others from accessing securities markets for 14 years in 2014

References:

SEBI (Prohibition of Insider Trading) Regulations, 2015