

An Analytical Takeaway on Structured Digital Database

The Structured Digital Database (SDD) was introduced by SEBI under the SEBI (Prohibition of Insider Trading) Regulations, 2015 to track the flow of Unpublished Price Sensitive Information (UPSI) and curb insider trading. Though unique to India, the SDD framework mirrors global efforts to protect investors and maintain market integrity, positioning itself as a vital tool against insider trading. In this article, the author intend to portray this through an analysis of the SDD framework by highlighting some of the practical issues faced by companies. Further, the author has also tried to resolve some of these practical issues by enlisting few recommendations which include developing SOPs, decentralizing responsibility through AI integration, regular departmental declarations, NDAs at resignation, and forming internal compliance committees for furthering the regulatory mandate.



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INTRODUCTION

HISTORICAL BACKGROUND OF STRUCTURED DIGITAL DATABASE (SDD)

In today's information age the power struggles emanate from having access to relevant information at the earliest and power lies with one who has relevant information. Thus, procuring of information is the power struggle in today's day and age. The white-collar crime of insider trading also stems from this power struggle of getting to know the information before anyone else so as to leverage that information *vis a vis* the listed companies to make gains in the

stock market.¹ This crime was first recognized in the United States of America by the Securities Exchange commission (SEC) under the Securities Exchange Act, 1934² *vide* the Rule 10b-5 which is commonly used as the charging section for insider trading.

Subsequently, the Indian watchdog- the Securities Exchange Board of India ("SEBI") enacted the SEBI (Prohibition of Insider trading) Regulations, 1992. Over the years with the enhancement and development in technology and capital markets in India, the regulations on prohibition of insider trading were amended and superseded by new set of regulations- SEBI (Prohibition of Insider trading) Regulations 2015 (hereinafter referred to as PIT regulations) so to limit the ambiguity and control the dynamic changes occurred in the securities market space.

Essentially, insider trading can be committed in three ways, the basis of all three ways is due to access of some information which is confidential information and is unknown to the general public. As per Regulation 3 of the PIT Regulations communication or procurement of unpublished price sensitive information related to the company or securities ("UPSI") is prohibited in manner that disallows any insider to (i) communicate, (ii) provide, or (iii) allow access to any UPSI except where such communication is in furtherance of legitimate purposes performance of duties or discharge of legal obligations. Many jurists believe that insider trading is the cancer of the capital market as it leads to information asymmetry which is extremely detrimental for the retail individual investor, the protection of which is one of the core objects of any regulator of capital markets.³

With this background in mind, the Committee on Fair Market Conduct first discoursed the requirement of introducing Structured Digital Database (SDD). The Committee particularly highlighted the concerns raised by listed companies at the time of sharing of UPSI for legitimate purposes being misused for conducting insider trading violations. Therefore, it recommended the need for establishing a clear link between the germination point till the last stage until the UPSI becomes public.

¹ Michael Seitzinger, *Federal Securities law: Insider Trading*, Congressional Research Service, (Jan 30th 2002, 12:00 PM), <http://pennyhill.com>

² Securities Exchange Act, 15 U.S.C §§ 1-39 (1934)

³ Nidhi Tandon, *Insider Trading-Is it an absolute Liability offence?* Corporate Law Academy, (May 15th 2004, 12:30 PM), <http://www-claonline.in>.

In line with this recommendation, the SEBI brought in SEBI (Prohibition of Insider Trading) (Amendment) Regulations, 2018, effective the 1st April, 2019 by virtue of which the regulatory mandate first came into picture under Regulation 3(5) and Regulation 3(6). However, albeit there was regulatory force in the mandate for maintaining SDD, there were lot of hurdles in implementing the same. Therefore, SEBI brought in further amendments in the year 2020 and additionally issued a set of comprehensive FAQs to iron out the difficulties. Further to this, regulatory clarity a lot of listed companies weren't complying with the requirement of having an SDD in place. Therefore, the stock exchanges were advised by SEBI to issue emails seeking from listed companies a quarterly compliance certificate pertaining to maintenance of SDD in a prescribed format.

INTRODUCTION TO STRUCTURED DIGITAL DATABASE

Structured Digital Database (SDD) is a digital surveillance toolkit that acts as a noble addition for SEBI to track the process flow of UPSI between insiders. By virtue of this initiative, SEBI seamlessly monitors the flow by ascertaining not only the germination point of UPSI but also the interim circulation of information between different hands of insiders.

With this innovative framework of recording and maintaining a repository of UPSI amongst insiders, SEBI intends to ensure confidentiality and integrity in the securities market. The data entry in the SDD is structured in a manner that encompasses details of not only the parties sharing the information but also the parties receiving it. Thereby, increasing the ambit of confidentiality and strictness to external parties not directly related to the company such as consultants, auditors and merchant bankers etc.

APPLICABLE LEGAL FRAMEWORK

In accordance with this rationale the enabling provision has been drafted that emanates as stated above from Regulation 3(5) & Regulation 3(6) of the PIT Regulations. Regulation 3(5) essentially mandates that either the Board of Directors or head of the organisation of every person required to handle unpublished price sensitive information shall ensure that SDD is maintained internally with adequate internal controls and checks such as time stamping and audit trails to ensure non-tampering of the database.

Gleaning from the above regulatory mandate it can be understood that recording of UPSI has to be as soon as possible-this may work in case the UPSI is germinated within the organisation, however for UPSI which stems externally it seems practically impossible to comply with the mandate to record UPSI therefore the proviso to Regulation 3(5) gives a certain levy to the listed entity by providing a two calendar day window from the receipt of such external UPSI to make relevant entries in the SDD.

Coming to Regulation 3(6) the other statutory force for SDD, essentially provides for the preservation of SDD for a minimum period of eight years post completion of the relevant transaction. The responsibility for preservation has been bestowed on the Board of Directors or the head of every organization.

MANDATORY CONTENTS

The SDD which essentially acts as an electronic ledger of UPSI shall contain the name and PAN/ any other identifier

authorized by law where PAN is not available, of persons who have shared UPSI, the nature of UPSI and persons or entities with whom UPSI is shared.

PRACTICAL ISSUES

SEBI's regulatory mandate of maintaining the SDD has certainly acted as a potent tool in the hands of the investigations wings while culling it certain key lacks in maintaining confidentiality and leaking of information leading to information asymmetry. Although it has helped the securities market watchdog to get hold of malpractices in the securities market, however there have been key challenges that Listed entities have faced in the implementation of this framework.

A. Reach

One of the key developments pertaining to SDD has been the inclusion of various other entities within the regulatory sphere of maintaining the SDD. Such entities generally come within the sphere of fiduciaries as defined under the PIT Regulations-who receive such UPSI in the course of their association with the listed entity for rendering their professional services.

B. Awareness & Centralised decision making

One of the key practical challenges faced by companies is the effective tracking and documentation of the flow of UPSI originating from top management. For instance, when the company proposes to declare a dividend, this UPSI often first comes into the knowledge of senior personnel such as the Chief Financial Officer (CFO) or other members of the top management. Subsequently, this information may be shared with other departments, such as the Secretarial team, for further action or compliance. Tracking this internal flow of UPSI and ensuring that it is appropriately recorded in the Structured Digital Database (SDD) in real time poses a significant challenge for many organizations firstly due to lack of awareness at the top level and secondly due to centralised manner in which such key decisions are taken. Generally, the person who germinates this information does not have the awareness or the access to the SDD as most listed entities have categorically authorised some person to enter such details in the SDD, therefore the intent of recording the entry in SDD from the germination point gets redundant.

The complexity further increases with the involvement of multiple stakeholders and departments, each of whom may handle the UPSI at different stages. Ensuring compliance with PIT Regulations, in such scenarios requires robust internal controls, clear SOPs, and an effective digital infrastructure to maintain accurate and tamper-proof records of UPSI sharing and access.

A notable and often under-discussed challenge in implementing the SEBI (Prohibition of Insider Trading) Regulations, 2015 (PIT Regulations), is the difficulty companies face in monitoring the securities trading activities of Designated Persons after they have resigned from the organization. While these individuals may no longer be on the company's payroll, their prior access to Unpublished Price Sensitive Information (UPSI) can continue to render them "Connected Persons" under the regulatory framework. As such, companies are expected to exercise due diligence even after the cessation of formal employment, particularly when the individual was in possession of material UPSI prior to departure.

In practical terms, this creates a grey area and a compliance dilemma. Once an employee resigns, the company's legal and operational capacity to monitor or influence that individual's trading behaviour diminishes significantly. The challenge is further compounded by the fact that any inadvertent or intentional misuse of UPSI by a former Designated Person may still be attributable to the company from a reputational standpoint, especially if adequate preventative mechanisms were not in place.

To address this issue, a proactive and preventive approach is recommended. One such measure that companies can adopt is the execution of a comprehensive Non-Disclosure and Undertaking Agreement (NDA) at the time of resignation. This agreement should include an explicit clause under which the resigning Designated Person undertakes not to trade in the securities of the company for a minimum period—typically six months—from the date of resignation. This cooling-off period serves two purposes: it provides a buffer during which the sensitivity of any UPSI the individual had access to may diminish, and it establishes a formal record of the company's effort to ensure compliance with the PIT Regulations.

Additionally, companies may also consider integrating such requirements into their Code of Conduct for Prevention of Insider Trading, ensuring that Designated Persons are made aware—at the time of appointment and again at the time of resignation—of their continuing obligations under the PIT Regulations. While this approach may not entirely eliminate the risk, it does help to demonstrate the company's intent and effort to uphold regulatory compliance and corporate governance standards.

C. Ascertaining of UPSI

Another conundrum is the subjective definition of UPSI which leads to ambiguity in ascertaining what all constitutes as UPSI. Since, recording the entry in SDD is linked to ascertaining of UPSI, there are times where listed entities have had issues in recording the information in SDD due to varied interpretations surrounding the definition of UPSI. Additionally, once the information is ascertained as UPSI, there are understanding or practical issues in recording such information at each stage when it crosses amongst different hand which further leads to diverging from the intent of PIT regulations.

ROLE OF COMPANY SECRETARY IN COMPLIANCE OF STRUCTURED DIGITAL DATABASE

Company Secretaries acting as Compliance Officers of companies have one of the most critical responsibility to enable companies to comply with the requirements of structured digital database- starting from sensitizing to monitoring to in fact incorporating the entries manually in the database. They act as a sole agent for establishing the framework of storing the UPSI and further keeping the database intact in a transparent manner. Vested with the colour of governance- Company Secretaries have to ensure that the UPSI does not pass through unless and until the same is recorded in the database, thus creating an additional yet one of the most critical role in ensuring that insiders do not take advantage of their position in a manner that is detrimental to the public shareholders.

RECOMMENDATIONS

Some of the suggestive measures include preparing SOP surrounding the compliance pertaining to SDD, which captures safeguards in the form of responsibilities, strict timelines and the consequences that may arise in case of any deviation. Moreover, the responsibility for maintaining the SDD should not rest with only 1-2 particular individuals rather the same should be decentralized. This can be implemented with the implementation of artificial intelligence within the ambit of SDD wherein entries should be captured on real time basis without the need of any particular single individual being held responsible. The SOP should also mandate the other departments to quarterly provide for a declaration on the sensitization and the implementation of the SDD compliance framework.

Separately, as an additional governance tool, companies may also consider constituting a committee to monitor the compliance and undertake disciplinary actions as and when it arises for strict enforcement of the regulatory mandate. This committee shall include members from its senior management such as head HR, Compliance Officer, Chief Financial Officer which shall hold periodic meetings at least on a half yearly/ quarterly basis. Additionally, the monitoring committee should also be bestowed with the responsibility of conducting regular sensitization sessions amongst the concerned departments and the personnels.

CONCLUSION

This regulatory mandate is quite unique in India. Only jurisdictions such as UK and EU have a concept of "insider list" under their applicable securities market regulations. Certain practical issues as highlighted in the article are required to be ironed out to reinforce the underlying intent of protecting the investors and

preserving the integrity of the securities market in India. In this manner, companies would be able to eventually take better control of insider trading compliances which would further the regulatory intent and would result in limiting the insider trading violations.

REFERENCES:

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- v. *Securities Exchange Act, 15 U.S.C §§ 1-39 (1934)*

