



Justice Sodhi Committee on Insider Trading Regulations submits report to SEBI

The High Level Committee to Review the SEBI (Prohibition of Insider Trading) Regulations, 1992 constituted under the Chairmanship of Justice (Shri.) N.K. Sodhi, former chief justice of Karnataka and Kerala High Courts and former presiding officer of the Securities Appellate Tribunal, submitted its report to SEBI Chairman, Shri U.K. Sinha, on December 7, 2013 at Chandigarh.

The Committee has made a range of recommendations to the legal framework for prohibition of insider trading in India and has focused on making this area of regulation more predictable, precise and clear by suggesting a combination of principles-based regulations and rules that are backed by principles. The Committee has also suggested that each regulatory provision may be backed by a note on legislative intent.

Some of the salient features of the proposed regulations are set out below:-

1- While enlarging the definition of "insider", the term "connected person" has been defined more clearly and immediate relatives are presumed to be connected persons, with a right to rebut the presumption. The term "immediate relative" would cover close relatives who are either financially dependent or consult an insider in connection with trading in securities.

2- Insiders would be prohibited from communicating, providing or allowing access to UPSI unless required for discharge of duties or for compliance with law.

3- The regulations would bring greater clarity on what constitutes "unpublished price sensitive information" ("UPSI") by defining what constitutes "generally available information" (essentially, information to which non-discriminatory public access would be available). A list of types of information that may ordinarily be regarded as price sensitive information has also been provided.

4- Trading in listed securities when in possession of UPSI would be prohibited except in certain situations provided in the regulations.

5- Insiders who are liable to possess UPSI all round the year would have the option to formulate pre-scheduled trading plans. In such cases, the new UPSI that may come into their possession without having been with them when formulating the plan would not impede their ability to trade. Trading plans would, however, be required to be disclosed to the stock exchanges and have to be strictly adhered to.

6- Conducting due diligence on listed companies would be permissible for purposes of transactions entailing an obligation to make an open offer under the Takeover Regulations. In all other cases, due diligence would be permissible subject to making the diligence findings that constitute UPSI generally available prior to the proposed trading. In all cases, the board of directors would need to opine that permitting the conduct of due diligence is in the best interests of the company, and would also have to ensure execution of non-disclosure and non-dealing agreements.

7- Trades by promoters, employees, directors and their immediate relatives would need to be disclosed internally to

the company. Trades within a calendar quarter of a value beyond Rs. 10 lakhs or such other amount as SEBI may specify, would be required to be disclosed to the stock exchanges.

8- Every entity that has issued securities which are listed on a stock exchange or which are intended to be so listed would be required to formulate and publish a Code of Fair Disclosure governing disclosure of events and circumstances that would impact price discovery of its securities.

9- Every listed company and market intermediary is required to formulate a Code of Conduct to regulate, monitor and report trading in securities by its employees and other connected persons. All other persons such as auditors, law firms, accountancy firms, analysts, consultants etc. who handle UPSI in the course of business operations may formulate a code of conduct and the existence of such a code would evidence the seriousness with which the organization treats compliance requirements.

10- Companies would be entitled to require third-party connected persons who are not employees to disclose their trading and holdings in securities of the company.

The Committee had its first sitting on April 12, 2013, and finalized the report at its last sitting on December 7, 2013. The [report of the Committee](#) is available on SEBI's website (www.sebi.gov.in). SEBI invites public comments on the above report, which may be sent to comments_pit@sebi.gov.in so as to reach on or before December 31, 2013. Public comments may also be sent at the following address:-

Legal Affairs Department

Division of Policy

Securities and Exchange Board of India

C-4A, G Block, Bandra Kurla Complex, Mumbai – 51

Comments are required to be sent in the following format:-

Sr. No.	Details of the Organization/ Individual	Draft Provision Recommended by the Committee	Comment	Rationale
1.	<i>Provide the name and other details of the organization / individual here</i>	<i>Insert reference to paragraph number/ regulation number of the Committee's Report</i>	<i>Provide your comment here</i>	<i>Specify your reasons / rationale for the comment</i>

Mumbai

December 11, 2013



REPORT OF
THE HIGH LEVEL COMMITTEE TO REVIEW THE
SEBI (PROHIBITION OF INSIDER TRADING)
REGULATIONS, 1992

UNDER THE CHAIRMANSHIP OF

N. K. SODHI,

Former Chief Justice

DECEMBER 7, 2013

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GLOSSARY OF TERMS USED IN THE REPORT

Sr. No	Terms Used	Meaning
1.	ICDR Regulations	Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009
2.	IOSCO	International Organisation of Securities Commissions
3.	IPO	initial public offering
4.	PIT Regulations, 1992	Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 1992
5.	Proposed Regulations	The proposed regulations i.e. the Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2013
6.	SCRA	Securities Contracts (Regulation) Act, 1956
7.	SEBI	Securities and Exchange Board of India
8.	SEBI Act	The Securities and Exchange Board of India Act, 1992
9.	Takeover Regulations	Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011
10.	The Committee	The High Level Committee to Review the SEBI (Prohibition of Insider Trading) Regulations, 1992
11.	UPSI	unpublished price sensitive information

PREFACE AND NOTE FROM THE CHAIRMAN

1. Insider trading – essentially the wrong of trading in securities with the advantage of having asymmetrical access to unpublished information which when published would impact the price of securities in the market – has been attracting regulatory attention worldwide. While jurisdictions across the world are unambiguously unanimous in the resolve to fight insider trading by ensuring a level-playing field for trading in the securities market primarily on the ground that it erodes investor confidence in the market and the integrity of price discovery, legal treatment of what precisely should be the measure to determine whether an act of trading by an insider is illegal varies across jurisdictions.
2. In any good legal system, in dealing with any form of wrong or misconduct, it is critical that the law draws a clear line making it evident as to what the treatment of persons falling on either side of the line will be. Unless the law and its implications are set out in a clear, specific and predictable manner, it would not be possible to provide a just and transparent regulatory system that is respected and adhered to.
3. In India, insider trading is not only a tort i.e. a civil wrong but also a crime¹. The SEBI Act does not define the term by itself although it refers to the term “insider trading” in many provisions². However, using the powers to make regulations and in discharge of its functions, SEBI has made regulations prohibiting insider trading in the form of the PIT Regulations, 1992, which have defined various terms such as “connected person”, “dealing in securities”, “insider”, “price sensitive information”, “unpublished”, to name a few, to build up a framework of the prohibition on insider trading.

¹ Section 24 of the SEBI Act criminalizes insider trading, punishable with imprisonment of up to ten years, or with fine of up to Rs. 25 crores, or both.

² Sections 11(2)(g), 11(2A) and 11(4) (power to take measures and issue directions in the interests of the market); Section 11D (power to issue cease and desist directions); Section 12A(d) (prohibition on directly or indirectly engaging in insider trading); Section 15G (power to impose civil monetary penalty for trading on the basis of unpublished price sensitive information)

4. Who is an “insider”, when and what form of dealings should get prohibited, what restrictions the regulations should impose in its attempt to prevent violative insider trading, the safeguards within which insiders may trade in securities in a compliant manner and the administrative aspects of how to review, monitor and achieve compliance are all critical to a workable and deterrent insider trading regulatory regime.
5. The Committee feels that by its very nature, insider trading is difficult to prove and the initial burden to bring home a charge could be heavy. However, where the charge is indeed established, the delinquent should be dealt with severely and in an exemplary manner in accordance with the rule of law. Such an approach would send a proper signal to the market about the seriousness of the issue, and about the approach of the regulator within the parameters of what can be justified in law.
6. The PIT Regulations, 1992 have had their challenges in their drafting, interpretation and reach. Besides, the felt need to ensure a clear regulatory policy that is not only easily comprehensible but is also comprehensive led to this Committee being set up under the chairmanship of Justice N. K. Sodhi, Former Chief Justice of the High Courts of Kerala and Karnataka and a Former Presiding Officer of the Securities Appellate Tribunal. The members of the Committee are:-

1. Darius Khambata, Advocate General of Maharashtra
2. Somasekhar Sundaresan, Partner, J. Sagar Associates, Advocates & Solicitors
3. Rajeev Luthra, Managing Partner, Luthra & Luthra Law Offices
4. Subodh Kumar Agrawal, President, Institute of Chartered Accountants of India
5. K. Venkataramanan, CEO & MD, Larsen & Toubro
6. Suresh Senapaty, Chief Financial Officer, Wipro Ltd.
7. Nirmal Jain, Chairman and MD, India Infoline Ltd.
8. Motilal Oswal, Chairman & MD, Motilal Oswal Financial Services
9. Rashesh Shah, Chairman & CEO, Edelweiss Group
10. Milind Barve, Chairman, AMFI & MD, HDFC AMC Ltd.
11. Arundhati Bhattacharya, MD& CEO, SBI Capital Markets Ltd
12. Deepak Kumar Chatterjee, MD & CEO, SBI Mutual Fund

13. Mobis Philipose, Columnist, Mint, HT Media Limited
 14. Menaka Doshi, Journalist, CNBC TV 18
 15. A. P. Bakliwal, The Bombay Shareholders' Association
 16. S. Ramann, Executive Director (Surveillance), SEBI
 17. R. K. Padmanabhan, Executive Director (Investigations), SEBI
 18. J. Ranganayakulu, Executive Director (Law), SEBI - Member Secretary
7. Mr. S. Ramann left the Committee on July 8, 2013 upon repatriation to his parent cadre and was replaced by Mr. S. Ravindran, Executive Director (Surveillance), SEBI.

Methodology and Approach:

8. The Committee had its first sitting on April 12, 2013, and finalized this report at its last sitting on December 7, 2013. At the outset, the Committee decided to invite public comments on any and every aspect of the regulations dealing with insider trading which enabled a review of all aspects of the PIT Regulations, 1992 including those where it was felt the provisions are inadequate and those where Indian regulations are superior to regimes elsewhere in the world. The Committee received comments and contributions from various persons whose inputs were compiled and collated for review by it. A list of the persons who provided their inputs to the Committee is contained in the Annexure.
9. The Committee is grateful for such participation and contribution by members of the public. Without their inputs, the burden of the Committee would have been much heavier and the Committee would not have had the benefit of public participation, articulation and the feedback of society on various aspects of the regulations. Thereafter, the Committee met on several occasions to deliberate upon various issues and aspects of insider trading and what good law to deal with insider trading should be along with the appropriate regulatory response as a matter of policy.
10. The Committee has drafted the Proposed Regulations dealing with insider trading so that its recommendations are spelt out in complete detail including the language of the

regulatory formulation. The Committee recommends that these regulations be notified, repealing and replacing the PIT Regulations, 1992.

11. The Committee formed a core drafting sub-group to prepare working drafts of the Proposed Regulations to enable the Committee to specifically focus on issues to be dealt with in ideal regulations, and this enabled reviewing the adequacy or lack thereof in the PIT Regulations, 1992 in achieving the regulatory objectives. Various members of the Committee provided both written inputs and contributions during deliberations, challenging one another in the inputs given, reconciling differences, and working towards addressing the regulatory and societal concerns connected with insider trading. The members of this sub-group were:-

1. Justice N.K. Sodhi
2. Darius Khambata
3. Somasekhar Sundaresan
4. R. K. Padmanabhan
5. J. Ranganayakulu
6. S. Ramann (replaced by S. Ravindran)

12. The following officers were invited to assist the sub-group in its work:-

1. Amit Pradhan, Legal Advisor, SEBI
2. Sumit Agrawal, Assistant Legal Advisor, SEBI
3. Vaneesa Abhishek, Legal Officer, SEBI

The Committee would like to place on record its deep appreciation of the valuable inputs that these young officers who have been associated with the Committee from the very beginning, have provided from time to time. Without their able support and assistance and the timely provision of data and co-ordination across all Committee members, it would not have been possible to achieve completion of the Committee's task.

13. Insider trading is an evocative subject. Drafting regulations in precise, unambiguous and predictable terms necessarily entails balancing multiple, and at times, conflicting perceptions of various stakeholders in the market system. For example, the easiest but most simplistic approach would be to prohibit any trading by an insider. However, such an approach would not only be as ineffective as any blanket prohibition policy but would also be unrealistic and out of sync with economic and regulatory realities. For example, rewarding and incentivizing employees with stock options on securities of a listed issuer is well recognized in the securities regulatory policy – SEBI has even made guidelines on the subject. A simplistic prohibition on all forms of trading by all insiders would mean that stock options would be rendered impossible to implement.
14. In drafting these regulations, the Committee has done its best to take into account every contribution received in response to the invitation of public inputs. In writing any legislation, it is not possible to accept and adopt every single suggestion and contribution. Therefore, the omission of any input received from the public is a conscious and deliberate one. An ideal approach to legislation would be to address every regulatory concern raised, taking into account the effectiveness of the regulatory measure adopted, the cost and burden imposed by the regulation on the market place and whether the corresponding benefit outweighs the burdens imposed. The Committee has had to walk a very nuanced and tight rope – as indeed would be the case with any legislation – in balancing and calibrating various conflicting inputs. Nevertheless, the non-acceptance of any contribution received from the public can never dilute the value of the suggestion received and the Committee is grateful for every suggestion received.
15. In so balancing the multiple objectives, the Committee wishes to emphasize and underline that trading by insiders to extract undue benefit out of their possession of UPI, stealing a march over the rest of the market owing to asymmetrical access to such information ought to be strictly prohibited. Such trading affects the integrity of the market and results in investors who do not have such access being deprived of an informed investment or divestment decision. In drafting the Proposed Regulations, the Committee has factored in the regulatory regime obtaining in various other jurisdictions

across the world. It is immensely grateful to the literature from IOSCO and also that published by in various jurisdictions such as Australia, Canada, Israel, Malaysia, New Zealand, Singapore, United Kingdom and United States of America.

16. With the benefit of having examined the literature available on the subject from across the globe, the Committee applied its mind to ground realities in India to develop the most appropriate regulatory policy that should be made applicable in India to address specific conditions prevalent in India. The review of how other markets have dealt with similar issues enabled a reference point to analyze the rich experience available in India. Such an approach enabled formulating the Proposed Regulations balancing the needs of the Indian market and investors in India with international standards and best practices.

Structure of the Report:

17. This Report is divided in to the following parts:-
 - a. Part I, containing the salient features and key highlights of the Proposed Regulations;
 - b. Part II, discussing the key recommendations of the Committee, articulating the Committee's deliberations on these issues and what weighed with the Committee in arriving at its final recommendations; and
 - c. Part III, containing the draft of the Proposed Regulations.

Legislative Notes:

18. The Committee wishes to highlight a very important recommendation that it has made and hopes that not only SEBI but every regulator adopts this recommendation in their law-making role. The Proposed Regulations contain specific notes on each provision setting out the legislative intent for which that provision has been formulated. These

notes are meant to be an integral and operative part of the regulations and are aimed at telling society what role the regulatory system expects the provision of the regulation to perform and help in their interpretation.

19. The Committee believes that in formulating regulatory policy, the authors of legislation should take courage not to stop short of articulating what the legislation was meant to achieve and intended to mean. The Supreme Court of India has observed³ that authors of subordinate legislation ought to articulate what they intended to legislate when writing regulations. The Committee believes that this is even more necessary in the case of any complex specialized legislation which has quasi-criminal implications such as the Proposed Regulations.
20. Penal provisions should be precise and should not impose an unfair burden on Courts by expecting that ambiguities would be ironed out during legal proceedings. In fact, the Committee believes that articulating the legislative intent behind each provision would be a powerful tool in nudging society towards a greater understanding of the law and a superior degree of compliance thereby minimizing the scope for litigation for controversies to be adjudicated by courts of law.

Acknowledgements:

21. Finally, the Committee wishes to acknowledge and thank every officer of SEBI involved in assisting the Committee in its work. In addition to those already named above, the co-ordination and support from Mr. D.V. Sekhar, Deputy Legal Advisor, SEBI and Mr. Rajeev Rastogi, Assistant Legal Advisor, SEBI too deserves mention. Without the tireless contribution and support of the SEBI officers ranging from organizing logistics to help collate information and data, it would not have been possible to complete this work within the relatively short timeframe in which this report is delivered.

³ AIR 2010 SC 3089 / (2010) 7 SCC 449

22. Before parting, my heartfelt gratitude for the vital inputs and most cherished cooperation by each and every member of the Committee, thus enabling us to complete the task of formulating new insider trading regulations in just a few months. Special efforts have been put in by the core group including the learned Advocate General of Maharashtra Mr. Darius Khambata and Mr. Somasekhar Sundaresan, Advocate and Partner, J. Sagar Associates, and I will be ever grateful for their walking that extra mile. But for their efforts, the completion of this challenging task would not have been possible. Their immaculate drafting of the regulations and the involved deliberations by the full Committee helped us evolve this work product as reflected in the final draft of the Proposed Regulations.

Sd/-
N.K. Sodhi
Chairman

PART I

SALIENT FEATURES OF THE PROPOSED REGULATIONS

The salient features of the Proposed Regulations are set out below:-

General Aspects:

1. The regulations will cover securities listed or proposed to be listed on stock exchanges⁴.
2. The term “connected person” is defined to explicitly include public servants who handle UPSI relating to listed companies⁵.
3. The term “generally available information” is defined to identify what is not UPSI and formulate a test based on whether the information in question is accessible to the public on a non-discriminatory basis⁶.
4. The term “immediate relative” is defined to cover close relatives who are either financially dependent or consult the insider in connection with their trading in securities⁷.
5. The term “unpublished price sensitive information” is defined to mean information that is not generally available but which upon becoming so available could materially affect the price of securities specifying types of information that will ordinarily be regarded as UPSI being listed out⁸.
6. Every provision of any importance (except for provisions such as definitions of other regulations cross-referenced) has been annotated with legislative notes with a view to set out the legislative intent and scope of the provision and more importantly, the principles on

⁴ Regulation 2(1)(c)

⁵ Regulation 2(1)(e)

⁶ Regulation 2(1)(f)

⁷ Regulation 2(1)(g)

⁸ Regulation 2(1)(p)

which the regulation is based. The legislative notes are an integral part of the Proposed Regulations⁹.

Charging Prohibitions:

Communication of information

7. Insiders are prohibited from communicating, providing or allowing access to UPSI unless required for discharge of duties¹⁰.
8. A general prohibition is imposed on all persons from procuring and causing communication of UPSI unless required for discharge of duties¹¹.

*Due diligence*¹²

9. Conducting due diligence on listed companies is permissible for purposes of transactions entailing an obligation to make an open offer under the Takeover Regulations.
10. Due diligence is permissible in other cases subject to making diligence findings constituting UPSI “generally available” at least two trading days prior to the proposed trading.
11. The board of directors of the listed company will have to opine that permitting the conduct of due diligence is in the best interests of the company and will also have to ensure execution of non-disclosure and non-dealing agreements.

Trading with possession of information

⁹ Regulation 1(3)

¹⁰ Regulation 3(1)

¹¹ Regulation 3(2)

¹² Regulations 3(3) & 3(4)

12. Trading in listed securities when in possession of UPSI is prohibited¹³.
13. Various specific defences¹⁴ are provided since the prohibition is wide-ranging and expansive. By clearly enumerating the defences, the prohibition has been made more effective. The defences include:-
- the trades being contrary to the nature of UPSI¹⁵;
 - the insider being an innocent recipient of UPSI or placed reliance on information not believed to be UPSI¹⁶;
 - the trade was between counterparties having parity in possession of the UPSI¹⁷;
 - the exercise of stock options entailing a pre-determined price¹⁸;
 - the trades were decided upon and executed by authorized persons / agents of a “blind trust” without access to the UPSI that the insider had¹⁹; and
 - the trades were pursuant to a trading plan compliant with the requirements of the regulations²⁰.

Trading plans

14. Insiders who are liable to possess UPSI round the year are permitted to formulate trading plans with appropriate safeguards²¹.

¹³ Regulation 4(1)

¹⁴ Regulation 4(3)

¹⁵ Regulation 4(3)(i)

¹⁶ Regulations 4(3)(ii)

¹⁷ Regulation 4(3)(iii)

¹⁸ Regulation 4(3)(iv)

¹⁹ Regulations 4(3)(v) & (vi)

²⁰ Regulation 4(3)(vii)

²¹ Regulation 5(1)

15. The compliance officer's role in monitoring and approving a trading plan has been made important²².

Disclosure Obligations:

16. Trades by promoters, employees, directors and their immediate relatives are required to be disclosed to the company²³.
17. Trades of a value beyond certain materiality thresholds are required to be disclosed in the public domain²⁴.
18. Company to keep record of all holdings by all employees²⁵.
19. Companies are entitled to require third-party connected persons who are not employees to disclose their trading and holdings in securities of the company²⁶.

Codes of Disclosure and Conduct:

20. Every company whose securities are listed or proposed to be listed is required to formulate and publish a code of fair disclosure governing disclosure of events and circumstances that would impact price discovery of its securities²⁷.
21. Every listed company and market intermediary is required to formulate a code of conduct to regulate, monitor and report trading in securities by employees and other connected persons²⁸.

²² Regulation 5

²³ Regulation 7(1) & 7(2)

²⁴ Regulation 7(3)

²⁵ Regulation 6(3)

²⁶ Regulation 7(5)

²⁷ Regulation 8(1)

²⁸ Regulation 9(1)

22. All other persons who handle UPSI in their ordinary course of work may formulate a code of conduct to enable compliance, monitoring and administration²⁹.

²⁹ Regulation 9(2)

PART II

KEY RECOMMENDATIONS: DELIBERATIONS AND RATIONALE

1. Part III of this Report contains the recommended draft of the Proposed Regulations. The Committee hopes that a plain reading of the regulatory provisions along with the legislative notes annotated with every material provision would set out the scope, reach and meaning in precise terms of the prohibitory provisions on insider trading. In this part of the Report, the Committee has articulated the key issues and concepts that were debated in connection with the Proposed Regulations set out in Part III.
2. Simply put, the Proposed Regulations entail a prohibition on trading by insiders in securities when in possession of UPSI, thus obtaining an unfair advantage. They also entail outlawing communication of UPSI by any insider except where such communication is legitimately necessary for performance of duties or discharge of legal obligations. Towards this end, it is necessary to define who an “insider” is; how a “connected person” has to shoulder a higher burden than those who receive UPSI and thereby attract the prohibition on trading; when information takes the character of “unpublished price sensitive information”; when information can be regarded as “generally available information”; what type of securities are covered by the prohibition against insider trading; how insiders may arrange their affairs in a compliant manner to have the capacity to trade in securities; recording and disclosing trades by connected persons; and most importantly, what defences may be available validly pressed considering the nature of the prohibition on trading by insiders when in possession of UPSI.
3. Against this backdrop, some of the key issues debated have been articulated to give the reader a glimpse of the nature of the deliberations and issues that weighed with the Committee. More important than this Part II are the legislative notes appended to the actual provisions drafted and set out in Part III. The Committee was unanimously of the view that there would be little point in writing a conceptual report that has later to be translated into regulations leaving scope for loss of meaning in translation. Therefore, the Committee has

drafted the Proposed Regulations with legislative notes that would explain the legislative intent and the regulatory policy behind each provision.

Reach of the Regulations:

4. The prohibitions contained in the Proposed Regulations would apply to trading in securities issued by a company which are listed on a stock exchange. The term “company” is defined notionally inasmuch as it would bring within its scope entities that are technically not companies incorporated under the Indian company law but entities that issue securities listed on stock exchanges in India. For example, a mutual fund set up as a trust, that can issue units of close-ended schemes which are traded in the market would also be a “company” for purposes of the Proposed Regulations.
5. The Committee was mindful of the need for a price-discovery platform for a security for the wrong of insider trading to be prosecuted as a crime or punished as a civil wrong. If securities are not listed, they would not be amenable to price discovery. Consequently, price discovery for the security would not be exposed to the prospect of an insider benefitting from trading when in possession of UPSI. In the absence of the ability to discover price in a market through an inter-play of demand and supply, it would not be possible to envisage an insider benefitting from his possession of UPSI and the lack of such information in possession of the others in the market.
6. The Companies Act, 2013 was passed by Parliament during the term of the Committee. Section 195 of this legislation covers insider trading and the Committee notes that there is no conceptual inconsistency between the generic provisions in that legislation and what the Proposed Regulations provide for. Section 458 of the Companies Act, 2013 delegates powers to SEBI to prosecute insider trading in securities of listed companies and companies which intend to get their securities listed. Therefore, the definition of “company” has been extended to cover entities that intend to get their securities listed. Since the ICDR Regulations mandate disclosure of all material information necessary for making an informed decision about applying for securities in an IPO, insider trading could

occur in relation to the price discovery process in the book-building under the ICDR Regulations, and would therefore be punishable by SEBI. These provisions may particularly get attracted in the case of an offer for sale as part of the IPO, where an insider could take advantage of his access to UPSI and trade with the investors in the IPO without making such UPSI generally available in the prospectus of the company.

7. The Committee was also mindful that it is possible that without a market for price-discovery being in place there could be abuse of asymmetry of information leading to fraud or cheating in connection with dealing in securities – such market abuse would be squarely covered by the SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to the Securities Market) Regulations, 2003 and other legal provisions on fraud, cheating, breach of trust etc. but it is not intended that every form of cheating and fraud would be regarded as “insider trading”.
8. With this approach, the Committee deliberated upon what the term “securities” would mean. Various suggestions were dealt with including whether one should look at over-the-counter derivatives based on listed securities, which could be the conduit for committing insider trading without seemingly trading in listed securities. The Committee concluded that the term “securities” is well defined in the SCRA and that therefore, it would not be necessary to re-invent the wheel. For example, an interest in a security is also a security under that definition. Moreover, the Committee was cognizant of the scope and reach of Section 12A of the SEBI Act which outlaws insider trading committed directly or indirectly.
9. This definition of “securities” is time tested and is used across all securities regulations and it would not be appropriate to re-define the term solely for purposes of these regulations. Such an approach would also enable bringing insider trading in listed derivatives that are not issued by any company but is an interest in securities issued by a listed company within the scope and reach of the Proposed Regulations.

10. In future, other price-discovery platforms that are not “stock exchanges” may emerge under extant securities laws. It would not be possible for envisaging future hypotheses and legislating today for those scenarios. Therefore, having adopted a principle-based approach to regulation, the Committee is of the view that any security listed on any public platform for price discovery would come within the scope and reach of the provisions of the Proposed Regulations.
11. To conclude, any security that fits the definition of the term under the SCRA and is amenable to price discovery on a market platform would be amenable to insider trading. Such a security may be issued by any entity – ranging from a company that issues shares, debentures or other securities, to a trust, for example, a mutual fund or an alternative investment fund that issues units that are listed on a stock exchange. The provisions in the Proposed Regulations that define the terms “company” and “securities” have been drafted in the light of the aforesaid discussion.

Who is an Insider?

12. Various suggestions were received on what the scope of the term “insider” ought to be. The Committee reviewed the legislative policy in various jurisdictions. Some suggestions were to the effect that whether a person is an insider should be determined on the basis of whether he is connected with an insider to the issuer of the securities while others were of the view that any person who gets connected to the UPSI would become an insider so long as the information has the character of UPSI.
13. The Committee had substantive deliberations on this aspect. The Committee took note of jurisdictions such as the United States where a breach of a duty owed to keep the UPSI confidential or not to trade when in possession of the UPSI was necessary for the trading to become illegal. Other jurisdictions, such as New Zealand have adopted a different approach i.e. of not having to prove that there was a breach of duty involved in the course of the information coming into possession of the person who has traded. Therefore, the

Committee felt that it was important to keep the scope of the prohibition as being applicable to “insiders” with a clear definition of who an “insider” would be.

14. The Committee built consensus around the view that anyone who is in possession of UPSI should be an insider provided the terms “UPSI” and “generally available information” are well defined. For further discussion of this issue please see the discussion under the head “*Information: Generally Available / Unpublished Price Sensitive*” in this Report.
15. The Committee therefore concluded that the term “insider” should be defined to mean all “connected person” and those in possession of UPSI leaving it to the definitions of “generally available information” to safeguard against an over-reach of the prohibition being read as a ban on “informed trading” as opposed to “insider trading”. The Committee has also provided robust defences against bringing a charge without satisfying the essential ingredient and rationale behind the prohibition on insider trading.

Connected Person:

16. The definition of “connected person” is crucial for purposes of defining an “insider”. It was felt that although the approach of rendering any person in receipt of UPSI has been adopted, it is important to have a framework that has an enhanced set of responsibilities for a “connected person”. The Committee was cognizant of the difficulties arising from unintended punctuation and syntax errors in the current regulations in this regard.
17. Any person associated with a company in any capacity that would allow such person access to UPSI relating to the company or whose association is reasonably expected to allow such access would be a “connected person”. Such association with the company and access to UPSI may arise owing to the connected person holding any position of employment with the company or being in any contractual or fiduciary relationship with the company.
18. The Committee was conscious that merely because a person does not hold any official position with a listed company but is otherwise completely involved with its operations and

is an insider to decision-making should not escape the scope and reach of the definition. Consequently, it was felt that even those persons who are in frequent communication with the officers of the company would also be connected persons. This would necessarily be a question of fact and when evidence is brought to bear to demonstrate such close contact, it should not be required to shut one's eyes to his being an insider, and have to look for a smoking gun i.e. demonstrate an actual communication of UPSI.

19. Whether or not a person is a connected person will always and necessarily be a mixed question of fact and law to be answered from the facts and circumstances of the case. Whether the association of a person with a company would put him in a position of accessing UPSI would also be a mixed question of fact and law. The Committee was conscious that if it were not possible to have direct evidence of actual access to UPSI, the test to be applied would be to consider whether the person in question is reasonably expected to have such access as a reasonable inference that a reasonable man would draw from the facts and circumstances of the case.
20. The Committee was also conscious of the fact that once a person is a "connected person", he should ideally not be regarded forever as being a connected person. After much deliberation it was felt that any person who has been a connected person during the six-month period prior to an act of trading should still be regarded as a connected person. This is only a bright line for attracting the deeming and notional implications in the eyes of the regulations. Indeed, if it can be shown that despite the passage of six months there had been contact that would lead to a reasonable prospect of UPSI having been accessed, and the consequence of trading when in possession of UPSI would follow.
21. Immediate relatives of connected persons have also been included in the category of connected persons provided they are either financially dependent or if their trading decisions involve consultation with a connected person. Frequent communication with a connected person who is in possession of UPSI and trading during such possession would point to consultation with the connected person for purposes of trading decisions. However, the Committee was of the view that such immediate relatives should indeed have

an opportunity to demonstrate that despite being an immediate relative in such a position, the immediate relative could not reasonably be expected to have had access to the UPSI.

22. A new feature of the Proposed Regulations is that of treating public servants and persons holding statutory positions that are reasonably expected to have access to UPSI as “connected persons” and thereby prohibit them from trading when in possession of UPSI. For example, a judge who has heard arguments in a complex tax proceedings the outcome of which would be materially adverse or materially positive to the price of securities of a company would be a “connected person” until he pronounces the order. Another example will make it clear. A public servant who is actively involved in formulating policy on any matter that could result in a material impact on the price discovery for securities of listed companies – say, pricing policy for a natural resource, or the cap on foreign investment in a specific sector, would be a connected person in the eyes of the regulations. Therefore, the restrictions on trading that would apply to connected persons would apply to such persons as well.
23. Accordingly, the Committee has drafted the definition of the term “connected person” in **Regulation 2(1)(e) of the Proposed Regulations** by factoring in the analysis set out above.

Generally Available Information and Unpublished Price Sensitive Information:

24. At the core of any regulations that regulate and prohibit insider trading lies the concept of “unpublished price sensitive information”. Jurisdictions worldwide use varying nomenclatures – mostly, “material non public information”. The SEBI Act specifically uses the term “UPSI” in Section 15G to impose monetary penalties connected with insider trading. Therefore, the Committee decided to adopt the same phraseology, so long as the concept is well understood and well aligned with the regulatory objectives *viz.* of outlawing the abuse of UPSI to the detriment of the general investors in the market. The Committee believes that notwithstanding the nomenclature the terms “unpublished price sensitive

information” or “material non public information” connote the same meaning and would not make a difference so long as the concept is well defined and understood.

25. UPSI is essentially information that is not generally available which on becoming generally available, would materially affect the price of securities to which it relates. The Committee decided to define the concept of “generally available information” and lay down the principle of how general availability should be ascertained. Essentially, information that is accessible to the public on a non-discriminatory basis would be considered generally available information. Analysis and research based on generally available information would also be generally available information.
26. The Committee deliberated upon how one should understand “non-discriminatory access” and it was felt that one should not over-stipulate how this should be understood since that could risk narrowing the scope of that term. For example, a research report that is priced for purchase and is made available to all clients of a stock broker would be considered non-discriminatory inasmuch as any client of the broker or any class of clients of a broker having a certain risk profile may acquire that research report. Merely because the report is priced and needs to be purchased would by itself mean that access to it is non-discriminatory. However, if one were to find extraordinary and peculiar structures such as pricing a research report at a level not in line with market practice such that only some identified persons may be able to acquire it and hope to rely on it by way of ostensible non-discriminatory access, it would not be non-discriminatory. Therefore, whether some information is available on a non-discriminatory basis would be a question of fact to be answered adopting the standard of a reasonable man.
27. Information that is capable of being accessed by any person without breach of any law would be considered generally available. Various examples were discussed by the Committee. One interesting example was this: If one were to see the chief executive officer of a listed company who is also the company’s alter ego collapse with a heart seizure at the reception of a doctor’s clinic and were to call up the broker to sell shares, would the information be UPSI or generally available information? The Committee

concluded that such information would indeed be considered “generally available” since the reception at the doctor’s clinic would be a public place and anyone who happens to be there could have seen it and could have reacted. On the other hand, if the same chief executive officer were to have collapsed with a heart seizure in the midst of a small meeting and his colleagues were to sell the shares before the news could reach the market, they would have been in possession of the information owing to their presence at a private meeting in the line of duty and the news of the ill-health would not be generally available information and would therefore be UPSI.

28. Another example is of a person standing outside the gates of the most material factories of a listed company and determining the movement and quantum of goods by counting the trucks entering and exiting the factory gates to analyze and assess the company’s performance beyond the stated numbers. Since such an activity would not involve any breach of any obligation under the Proposed Regulations it would be legitimate activity since the information being collected and processed is generally available and anyone with enterprise could have done the same. However, if one were to bribe the officials of the factory to provide such data, or if one were to hack into the computer systems of the factory to procure the information, such access would not be accessing of generally available information.
29. While these principles are also backed by the provisions containing the prohibition on communication of UPSI and the inducement of communication of UPSI in Regulation 3, it is important to also articulate how the concepts of “generally available information” and “unpublished price sensitive information” are intended to be understood.
30. A piece of research work that is available on a discriminatory basis but is based entirely on generally available information would not change the character of the research work from being “generally available” to being “UPSI”. The Committee is conscious that generally available information well analyzed by an insightful mind would not be transformed into UPSI. Therefore, the regulation explicitly provides that conclusions, deductions and

analyses of generally available information too would be regarded as generally available information.

31. The Committee also felt that some illustrative examples of what would ordinarily constitute UPSI should be set out to clearly understand the concept. It would be important to ensure that regardless of whether the information in question is price-sensitive, no piece of information should mandatorily be regarded as “UPSI”. Towards this end, examples of events and developments information about which would ordinarily be regarded as UPSI, are listed – such as financial results, dividends, mergers and acquisitions, changes in capital structure etc.

32. Some members of the Committee felt that the Proposed Regulations ought to prescribe specific forums in which publication would be mandatory for information to be regarded as being generally available. Specifically, the suggestion was that unless information is published on the website of the stock exchange, it would not be regarded as generally available and therefore, if price sensitive in nature, it would be regarded as UPSI. The problem with this approach would be that even if large newspapers and television channels were to have published a piece of news and market participants were already factoring in the news in price discovery, an insider who trades when in possession of such news would be regarded as violating the law merely because the stock exchange website does not carry the news. The Committee believes that it would be inappropriate to regard information that is widely available in the public domain as UPSI. On the other hand, some members felt that one could register a newspaper in a remote region in the country, publish news there, and then trade despite the news not truly being publicly accessible. It was felt that such extreme and convoluted structures would be regarded as contrivances and devices to circumvent the Proposed Regulations in terms of Section 12A of the SEBI Act. Moreover, it is settled law that such regulations ought to be purposively construed and if two views were possible, the view that furthers the legislative objective would need to be adopted over a view that makes a mockery of the legal provisions.

33. To conclude, whether or not a piece of information is generally available or is unpublished would necessarily be a mixed question of fact and law. A bright line indicating the types of matters that would ordinarily give rise to UPSI are listed to give illustrative guidance. It could well also be possible that information from such events could be routine in nature and consistent with a long history. Information about the repetition of the same event on predictable lines would not render it to be UPSI unless deviated from. For example, the declaration of dividend at the same rate at which a company has declared dividend for the several years as per publicly stated dividend policy. Therefore, the Committee has drafted the definition of “generally available information” in **Regulation 2(1)(f) of the Proposed Regulations** and that of “unpublished price sensitive information” in **Regulation 2(1)(p) of the Proposed Regulations** bearing in mind the analysis articulated above.

Trading versus Dealing:

34. There was considerable debate in the Committee about whether the term “dealing” or the term “trading” should be adopted for purposes of prohibiting insider trading. It was felt that the term “dealing” is extremely wide and would then warrant a definitional delineation which in turn would end up with defining “dealing” as “trading”. Each and every act of doing something with securities would constitute “dealing” – for example, getting securities dematerialized, creating an encumbrance, agreeing not to dispose of the securities without another person’s consent such as a lender, would all be acts of “dealing” in securities. The Committee believes that the mandate of the Parliament is to prohibit “insider trading” and the regulations ought to focus on such a prohibition and not inflict unintended and untold prohibitions on any and every activity connected with securities.
35. “Trading” in the ordinary English meaning of the term would entail an act of getting something in return for something else i.e. entailing an element of consideration changing hands. Even an act of subscription to securities would be an act of “trading” inasmuch as the subscriber would trade his funds towards subscription money for the securities allotted to him. When one trades in securities by acquiring or disposing of an interest in securities

when in possession of UPSI there would be an abuse of the UPSI, necessitating the prohibition.

36. On the other hand, using a vague and open-ended phrase like “dealing” could result in outlawing routine *bona fide* transactions that have no nexus with the objective of the Regulations. For example, a prohibition in “dealing” when in possession of UPSI would result in a prohibition on pledging of shares by any person in possession of UPSI. In the ordinary course of lending activity, substantial shareholders in listed companies are routinely required to provide third party security for borrowings by them or by the companies whose shares they hold. Such encumbrances are but provision of security for loans advanced and as such cannot be justified as being the mischief sought to be suppressed by these regulations. If “dealing in securities” were to be prohibited when in possession of UPSI, all such acts of providing security would become illegal. Such a prohibition would bring the activity of taking a pledge or encumbrance on listed securities to a standstill for the banking and finance industry with no real corresponding benefit to the market.
37. The Committee deliberated as to whether pledges and encumbrances could be created as a device for circumventing the prohibition and concluded that such a mischief is unrealistic and impractical and would in any case not go scot-free owing to Section 12A of the SEBI Act. The Committee is mindful that this provision categorically outlaws any contrivance or a device that would enable a direct or indirect circumvention of any provision of the Act or regulations made thereunder or even the direct or indirect commission of insider trading. Therefore, if one were to construct a pledge or an encumbrance as a device to get around the prohibition on insider trading, the provisions of Section 12A of the SEBI Act would adequately empower enforcement.
38. By adopting the term “trading”, the Proposed Regulations would in fact ensure that the provisions are made precise rather than be left to wide and potentially ambiguous interpretation. When one trades securities or interest in securities for something else, one

would be trading in the security for consideration. The Committee concluded that the more appropriate term to be used particularly for imposing the prohibition under the regulations would be that of “trading” and not “dealing”. The Committee built consensus around using the term “trading” instead of the term “dealing”.

39. The Committee has therefore dealt with the drafting of the Proposed Regulations in line with the aforesaid discussion i.e. by adopting the term “trading” instead of the term “dealing”.

Charging Provisions:

40. The Committee felt that an effective barrier to trading when in possession of UPSI should be maintained as a charging principle. This should be the general rule backed by the principle that no insider should gain undue benefit by trading with the benefit of possessing UPSI which the rest of the market does not have and therefore, gain an advantage over the market. The exceptions to the rule are set out in the form of defences that are available. The principle behind these defences can be summarized as situations and circumstances in which this general charging principle would not be applicable – for example where both parties to a trade in fact have the same UPSI with them although the market may not have it.
41. One core principle that the Committee would seek to highlight is that the purpose of the Proposed Regulations is to prohibit violative insider trading whereby insiders who are in possession of UPSI take undue advantage of such possession in their trades with the rest of the market that does not have a level-playing field in terms of access to material information. Therefore, the identity of the owner of the mind that trades in securities is what the Proposed Regulations would look to rather than the identity of the owner of the title to the securities that are traded. The title to the securities would point to the person who traded, but if the person who traded and the person whose securities were traded are different persons, whether the person who traded had UPSI would be the key issue to be determined.

42. The provisions of **Regulation 4 of the Proposed Regulations**, which imposes the prohibition on trading by insiders when in possession of UPSI, and provide specific defences, are drafted taking the aforesaid principles into account.
43. Likewise, to maintain hygiene in the market place it is necessary to ensure that UPSI is not handled lightly and is handled only on a need to know basis and is not communicated except where necessary. Therefore, the Committee decided to retain the general prohibition on communication or counseling UPSI and has also introduced conditions on which due diligence may indeed be conducted so that there can be communication of UPSI in well-regulated circumstances. The provisions of **Regulation 3 of the Proposed Regulations**, which imposes the prohibition on communication of UPSI and the obligation to treat UPSI on a need-to-know basis are drafted accordingly.

Due Diligence:

44. Whether any exercise of due diligence inquiring into the affairs of a listed company should at all be permitted was keenly considered particularly since this is a question that keeps coming up under the current regulations in the context of transactions involving mergers and acquisitions. There are doubts about this issue under the current regime and yet, there is case law and precedent of a substantial acquirer being told that he ought to have conducted an exercise of due diligence before taking a decision to acquire a substantial stake in a listed company particularly when he seeks to withdraw from the transaction.
45. In an ideal world, the information that is generally available about any listed company in the public domain ought to be adequate for any and every investment in its securities. However, that is neither a true position nor a correct expectation is evidenced by even listed companies having to write detailed offer documents and prospectuses for securities offerings such as rights issues and follow-on public offerings. Banks that lend for acquisitions would need to conduct due diligence on a company's operations. Substantial

investors who invest in a company to enable it to fund its businesses may need to understand more than just what is publicly available to appraise the investment proposition.

46. Therefore, the Committee decided to squarely deal with the problem by clearly articulating the principles underlying the prohibition on communication of UPSI and stating the principles based on which due diligence may be conducted on listed companies. The Committee was conscious of how market price was but one of the criteria for computing the minimum offer price under the Takeover Regulations but there were other criteria as well – more so in the case of infrequently traded stocks. The Takeover Regulations Advisory Committee commented on this phenomenon whilst discussing the relevance of market price for computing the minimum offer price for an open offer transaction. In the circumstances the Committee reached a consensus around permitting due diligence in relation to material transactions but as a special exception to the general rule with a number of strings attached.
47. First, the board of directors will need to come to a clear view that permitting exercise of due diligence is in the best interests of the company. It is the company that is the owner of the UPSI relating to the company and it should be the responsibility of its board of directors to justify permitting the conduct of a due diligence exercise. The dispensation for permitting such an exception has been differentiated between transactions that entail an open offer under the Takeover Regulations and other transactions. The Committee recommends that in transactions not involving an open offer under the Takeover Regulations (where the UPSI would get published in the letter of offer sent to all shareholders) the findings of the diligence that constitute UPSI would need to be made generally available before the trade for which due diligence is permitted.
48. Mr. Mobis Philipose believes that making the UPSI public after conducting due diligence would pose challenges – particularly one of reluctance to have competitive information disclosed to a person conducting diligence to be brought into the public domain and get accessed by competitors although it may be necessary to share such information to large financial investors or strategic partners who are prospective traders in the company's

securities. Consequently, due diligence exercise conducted by a prospective strategic partner or large financial investors should be excluded from public disclosure of findings with a minimum threshold of 10% of the equity being acquired by such investors. On the other hand, Ms. Menaka Doshi has a diametrically opposite view i.e. that no due diligence exercise should at all be allowed if an open offer is not triggered under the takeover regulations. Even where an open offer is triggered, in her view, permission to conduct due diligence is unfair to the other investors. According to her, such due diligence exercise would disturb the level playing field and making the information generally available two days before the trade is unrealistic and inadequate.

49. The recommendation of the Committee is based on the premises articulated above. As stated earlier, there can be multiple views ranging from one extreme to another on any aspect of law and policy. However, there is clearly no case to be made to oppose any conduct of any due diligence since it is indeed true that due diligence before public transactions is necessary since information in the public domain about listed companies is not considered fully adequate. It would only stand to reason that one should provide a predictable, clear and conditional framework to enable a due and proper acknowledgement of market and regulatory reality and to have an orderly environment in the securities market to address these issues. Mandating that the Board of Directors, which is the owner and custodian of the UPSI should have to sign off that there is a need for conduct of due diligence to serve the interests of the company, and the obligation to make the findings public before the trade takes place are counterbalancing measures towards reaching such an objective.
50. The Committee therefore recommends that the exercise of due diligence and the consequent enquiries into the affairs of listed companies be permitted subject to the safeguards and conditions articulated above. The provisions of **Regulations 3(3) and 3(4) of the Proposed Regulations** have been appropriately drafted to factor in the requirements articulated above.

Valid Defences:

51. As regards the blanket prohibition on trading in securities when in possession of UPSI, the Committee decided to articulate specific defences that would be available in line with the principle for which the blanket prohibition has been recommended. Each of the defences articulated is based on a specific principle that would demonstrably counteract against a reasonable charge of insider trading having taken place. Therefore, whether the relevant principle is evident from the facts and circumstances of the case would need to be seen when any of these defences is adopted. All actions relating to enforcement against insider trading would necessarily depend on the facts and circumstances of each case. Both the charge and the defence would be a mixed question of fact and law.

52. The fundamental premise on which trading when in possession of UPSI is prohibited is that when an insider is in such possession, he would be assumed to be influenced by the nature of the UPSI in his possession, which others in the market would not have. Such a position would place him at an unfair advantage over the others in the market. However, it is noteworthy that insider trading is not only a tort (a civil wrong) but is also a punishable crime that could lead to an insider being imprisoned for a period of upto 10 years. Therefore, a charge of insider trading should be clear, precise and reasonable.

Contrary to nature of UPSI

53. Against this backdrop, it should be emphasized that insider trading is a wrong arising out of an insider taking advantage of UPSI in his possession to the exclusion of the others. Therefore, if the insider's trades were in fact contrary to the nature of the UPSI in his possession, such trading ought not to be treated as a wrongful act. Therefore, where an insider has traded in a manner contrary to how a reasonable man who is seeking to benefit from the UPSI would act, it should follow that he has not committed a tort or a crime. For example, if the information in possession of an insider were to be adverse in nature say, the denial of an important license by a regulatory agency and the insider had actually purchased shares before the UPSI became generally available, it would but follow that the

UPSI in his possession did not motivate his trade. Conversely, where the UPSI in possession of an insider is positive information say, the award of a material contract to the company which could impact the price positively and if the insider sold the shares before the good news came into the public domain, it would follow that he was not committing a tort or a crime.

54. It would be quite difficult to establish but important to provide that where the insider was an innocent recipient of the UPSI and despite exercise of diligence expected of a reasonable man, he had no reason to believe that the information was UPSI. In such an event, the insider who has traded should have a chance to demonstrate that he did no wrong. Needless to say, the insider would need to prove that he did everything reasonably in his power to assess whether the information in his possession was UPSI (i.e. exercise of diligence expected of a reasonable man) and that he traded *bona fide*. If the insider can indeed demonstrate that he did not *bona fide* understand the nature of the UPSI or that the UPSI was price sensitive to attract the prohibition (in doing so, adopting the standard of a reasonable man), he should not be held to have violated the prohibition.

Unaware of Tipper's violation

55. It is possible that an insider may have received information from someone who is not a connected person and he did not have reason to believe that the person providing the information violated any law or confidentiality obligation owed by that person. Any person who receives UPSI would be immediately placed in the shoes of an "insider" in view of the definition of the term. Therefore, if a person were to receive information about a company from someone who is not a connected person, but such person had procured the information illegally, the recipient would be innocent if unaware of the tipper's violation. Therefore where a person trades on the basis of contents of a research report which later turns out to have contained UPSI illegally procured by the research analyst, the fact that a *bona fide* recipient of that report traded when in possession of that report should not be visited with the charge of insider trading.

Parity of information

56. The Committee believes that in situations where both the buyer and the seller of securities are in possession of identical information, the trade by itself should not be rendered violative. Such a transaction between two identifiable persons who have identical access to UPSI ought not to be outlawed. Had the information in question been generally available and the trade had been in the open market, there would have been no room for alleging insider trading. Likewise, where the counterparty to the trade is clearly identifiable and in a bilateral trade the counterparty was indeed privy to the very same UPSI, the trade should be held to have wronged no one. If such a principle were not to be followed, every *inter se* transfer of shares among promoters could get regarded as insider trading since promoters would be in possession of UPSI and although no third party has traded with the promoters. Therefore, it is important to provide the parity of information among the trading parties as a valid defence.
57. Ms. Doshi believes that such a defence should only be available to transfers of securities between persons whose ultimate beneficial owners are the same, and that not doing so would result in those who are not party to such a trade not enjoying a level-playing field. The Committee has refrained from such an approach not only because parity of information is not violative insider trading in many jurisdictions across the world, but also because even without common beneficial ownership, two or more persons could have parity of information – say, joint venture partners.

Stock Options

58. Stock options are a means of rewarding and incentivizing performance by employees of listed companies. The exercise price for a stock option is pre-determined and after a certain vesting period, the option that is granted would vest and may be exercised to acquire the underlying shares. SEBI administers specific guidelines to deal with employee stock options. Therefore, where an insider exercises a stock option when he is in possession

of UPSI but the price for the stock option was fixed long ago and he had no role in negotiating any such price, it would be unfair to taint such an insider-employee with the charge of insider trading. Insider trading is fundamentally based on prohibiting the insider from getting a price advantage over the others in the market. Where the price is pre-determined as in the case of a stock option and the option is exercised at such price despite there being UPSI in possession of the insider, he should be able to defend himself in the ordinary course.

Non-insider decision-maker for trades

59. While trading to take advantage of the possession of UPSI should be outlawed, it is equally important to make provision for the ability to disconnect the two aspects of the matter i.e. the possession of UPSI and the decision to trade at a certain price. In any business group comprising multiple entities discharging multiple roles, if it is possible to ring-fence the persons who are in possession of UPSI from those who are responsible for the decision-making necessary for the trades, the rationale underlying the prohibition of insider trading would not be attracted. In situations where the person in possession of the UPSI is different from the person who takes the trading decisions and the two are segregated by effective arrangements, the purpose of the prohibition would not be attracted. Consequently, if it can be established that adequate arrangements were in place to ensure that the persons taking decisions on the trade are different from the persons having possession of the UPSI and there is no evidence of such arrangements breaking down, a valid defence ought to be available. Likewise, if the trades are made by a duly authorised person other than the insider without any reference to or prior knowledge of the insider although the trades may have been made on behalf of the insider, the defence ought to be available. This is the principle on which the concept of “blind trust” is adopted worldwide i.e. where a person is given complete authority to trade – say, a discretionary portfolio manager who is himself not in possession of UPSI. In such a fact situation, the Committee believes that a valid defence should be provided.

60. In the light of the foregoing discussion, the imposition of the prohibition in Regulation 4(1) and the provision of specific and narrow valid defences in Regulation 4(3) have been stipulated, factoring in the aforesaid analyses.

Trading Plan:

61. Since the prohibition on trading when in possession of UPSI is a stringent one, it is quite possible that certain persons particularly those in senior management and those who are promoters may perpetually be in possession of some UPSI or the other rendering such persons incapable of trading in securities throughout the year. This would be so because at any point of time such persons may be involved in some decision-making or the other and be privy to confidential information that could affect the discovery of price if such information were to become generally available. It is important to reconcile the need to maintain the prohibition on trading in securities when in possession of UPSI with the need to provide a regime in which compliance-conscious insiders are able to put in place a compliant mechanism to trade in securities where they are insiders. Towards this end, the Committee upon a review of provisions made in some other jurisdictions felt that it would be in the fitness of things for India to test the concept of a “trading plan” that would enable compliant trading by insiders without compromising the prohibitions imposed in the Proposed Regulations.
62. There are jurisdictions that have not warmed up to the concept of a trading plan and there are jurisdictions where the concept has been available for a reasonably long time and further improvements have been made on the basis of empirical evidence of how they have worked. The Committee believes that there is merit in the idea and with appropriate safeguards it is time to test the concept in India to enable the framework of compliant trading. Such an experiment could well be utilised for compliant trading towards creeping acquisitions by promoters (envisaged under the Takeover Regulations) or monetizing of securities holdings by entrepreneurs who have listed their companies.

63. The very concept of a trading plan is meant for those who are perpetually in possession of UPSI. Therefore, it would not be possible to formulate a plan when the insider is not in possession of any UPSI. Instead, the regulatory framework for the trading plan would entail permitting an insider to formulate the plan in advance to effect trades at a subsequent date, by which time they be in possession of new UPSI but the UPSI that would have been in his possession when formulating the plan would have become generally available. The possession of new UPSI that was not even in existence when the trading plan is formulated should not act as a barrier to the trades being executed provided the safeguards stipulated are met. The Committee took note of literature in the United States about the alleged abuse of the trading plan whereby trades may be pre-determined but the making of UPSI generally available may be timed to profit the insider. Therefore, the Committee decided that the trading plan would not provide absolute immunity from investigation into whether such manipulation of timing had been used to circumvent the prohibition on violative insider trading.
64. Some of the salient features of the safeguards are that the execution of the trading plan may commence only at least six months after the trading plan is publicly disclosed. No trading plan should entail trading for the period between the twentieth trading day prior to the last date of a financial period for which results are to be announced and until the third day after the disclosure of the results. Trading plans are required to be in place for at least twelve months, no two trading plans should overlap and a trading plan should be reviewed and approved by the compliance officer of the company and then publicly disclosed after which it must be implemented. Some members have expressed reservations about the onerous nature of such requirements and feel that the concept of a trading plan may not find many takers. Specifically, the suggestion is to bring down the cooling off period to commence the trading plan to 90 days. The Committee is however conscious that this is a novel experiment being tested in India. Even in jurisdictions where the concept was introduced long ago, empirical evidence points to abuse with timing of the UPSI being made generally available to suit the trading plan of those who manage the company. It is felt that the concept should be introduced with sufficient safeguards and adequate care should be taken to ensure that rampant abuse does not lead to this significant reform measure being

removed in the near future as a reaction to abuse. In fact, upon review of empirical evidence and feedback after the concept is introduced, it would always be open to SEBI to dilute or enhance the regulatory conditions attached to trading plans under the Proposed Regulations.

65. A trading plan may set out either the value of the trades to be effected or the number of securities to be traded. It should also set out the nature of the trade and the intervals at which or the dates on which the planned trades may be executed. If it can be reasonably inferred that the UPSI that was in possession of the insider when formulating the plan is not yet generally available, the compliance officer would be empowered to defer the commencement of the trading plan. However, the trading plan once commenced cannot be revoked and would have to mandatorily be implemented. This is critical to ensure that the prospect of abuse by timing the publication of unpublished information is dis-incentivised.

66. A public disclosure of every trading plan is envisaged to make it clear to the market at large that such a planned set of trades would be effected and the public would be able to take an informed decision about trades in the same securities. One member of the Committee is of the view that the trading plan should not be disclosed to the stock exchange at all while another is of the view that it may be disclosed provided the value of the trades envisaged in a plan is beyond a material threshold. First, the Committee feels that an insider would adopt a trading plan only for material trades and if he does not truly need a material pre-programmed compliant trading plan, he would follow the pre-clearance route envisaged under the regulations, as is the case under the PIT Regulations, 1992. Second, the Committee felt that disclosure to the stock exchange is an important measure of transparency which would be welcome under Indian conditions. The Committee is of the view that it would only be appropriate to entail a public disclosure and the market would be mature enough to absorb the news about the intended trades pursuant to a trading plan and draw appropriate conclusions.

67. Mr. Philipose believes that the policy preference should be towards trading plans rather than towards encouraging blind trusts, and that restrictions on the trading plans such as the

bar on transactions being contemplated when trading windows are closed on a pre-scheduled basis should be considered for blind trusts as well. However, it is noteworthy that the two concepts are different – the usage of a SEBI-registered discretionary portfolio manager on a blind trust basis involves shutting out the decision-maker from the owner of the title to the securities being traded. On the other hand, the trading plan involves formulation of a pre-scheduled plan by persons perpetually in possession of UPSI to trade, which may not be commenced until the UPSI in their possession while formulating the plan becomes published and which may be implemented despite their being in possession of new UPSI which was not in their possession when deciding on the trading plan. Therefore, there is no specific policy preference on either route. In any case, the onus of establishing a defence adopted would be on the person relying on it.

68. The provisions of Regulation 5 which comprehensively deal with the various requirements to be met for formulation of a trading plan have been drafted accordingly, factoring in the reasoning and analyses articulated in the foregoing paragraphs.

Disclosure of Trades:

69. The Committee believes that it is necessary to make provision for disclosure of trades by employees of listed companies and their immediate relatives on two grounds. Such disclosures would not only enable the administration and policing of the Proposed Regulations but it would also enable the market at large to take an informed investment decision on the basis of dealings by the company's insiders. The Committee has carefully differentiated between internal disclosures and external disclosures and has sought to minimize external disclosures unless such disclosures serve any specific regulatory purpose.
70. The Committee debated whether even in the internal disclosures there would be a need to restrict disclosures with any materiality threshold being involved. Some members of the Committee felt that it may be onerous to keep records of all employees' holdings and trades in securities. However, it was felt that given the advancement in information technology,

keeping a repository of information of trades internally should not be very onerous for listed companies. It was also felt that providing for a routine maintenance of records would be a laudable legislative measure and should not be diluted. However, if the value of trades were to cross a materiality threshold it would then become necessary to require public disclosure of such trades.

71. The idea behind the provisions relating to disclosures to enable a smooth administration of the Proposed Regulations. The provisions entailing disclosure by all employees impose an internal requirement. Introducing a provision to stipulate such requirement only for designated employees would lead to a difficulty in administration inasmuch as even the reach and jurisdiction of these provisions would become dependent on questions of fact. There would be higher prospect of regulatory litigation through that approach, leading to questions of whether a certain employee ought to have been designated or whether he was outside the scope of coverage. Instead, since this requirement is nothing but an internal exercise, it would be eminently feasible for companies to have an electronic means of providing such information and retaining the same in the records.
72. The Committee has also consciously stipulated value thresholds for external disclosures. While there can always be a debate about what the value of such thresholds should be, it was felt necessary to leave flexibility to SEBI to specify any value other than what is being stipulated in the Proposed Regulations.
73. The Committee believes that reference to voting rights as a threshold for disclosures as is the case with the PIT Regulations, 1992 is not really relevant. The regulatory objective of the Proposed Regulations, unlike the Takeover Regulations, is not aligned with making the voting power relevant. What is of greater relevance is the scale and size of the trading by insiders particularly those who are expected to have access to UPSI. Even the size of the company is not relevant in this regard. The disclosure obligations in **Chapter III of the Proposed Regulations** have been drafted accordingly.
74. Mr. Suresh Senapaty and Mr. Subodh Kumar Agarwal have expressed their dissent to the requirement for coverage of disclosures of securities held and traded by all employees, and

to public disclosure of material trades by all employees. Their dissenting view is also supported by Ms. Arundhati Bhattacharya, Mr. Nirmal Jain and Mr. K. Venkataramanan.

75. According to them, the correct approach would be to restrict the coverage of the disclosures only to those covered by the Code of Conduct i.e. to “designated persons” (see the section on Code of Conduct), since only such persons are “insiders” and not each and every employee. Their grounds of dissent on this issue are summarized below:-

- a. a company would need to educate all employees and their relatives about these disclosure requirements;
- b. obtain accurate declaration from them;
- c. put in place mechanism to capture and track data on a real time basis;
- d. do a due diligence on the data integrity and compile such data accurately;
- e. retain audit trail of the same for reference in future; and
- f. timely report the same to the Stock Exchange.

76. They also believe that many companies have in their employee base as much as about 40% based outside India and about another 40% having nationalities outside India. Many companies have dual listing in India and overseas. Having to ensure that the employees have a mechanism to track such data accurately for themselves and their immediate relatives and report in time would invite penalty on the company too. They acknowledge that the number of transactions in excess of Rs. 10 lakhs may be infrequent, but having to accurately report this would necessitate tracking and monitoring of all transactions which makes the activity very onerous considering it would need to cover all employees and their immediate relatives. They are also opposed to public disclosure of all such trades that are above the thresholds on the premise that this would result in competition getting to know information about Indian listed companies. Consequently, in their view, the recommendation ought to be that only directors and those in the senior management of listed companies should be covered by the disclosure obligations. The companies should be required to keep records only for such persons. Such records should be available to SEBI but should not be disclosed in the public domain. They also believe that mandating disclosures of trades and holdings in securities of all employees and not just “designated

persons” would go beyond the mandate of this Committee since it should only make recommendations for insiders and not for those who are not insiders.

77. The majority view set out in **Regulation 7 of the Proposed Regulations**, and in particular, those governing disclosures by employees, essentially entail imposing obligations on employees of listed companies. The failure on their part to report to their employers would be a violation of law by them and not by their employers. Indeed, increasing awareness and educating employees to enable them to comply would only be a welcome measure and would further the regulatory objective of improving hygiene in the securities market in connection with insider trading and quite consistent with the mandate of this Committee. The threshold beyond which public disclosure is mandated has been materially enhanced. Currently, any trade of above a value of above Rs. 5,00,000 would in any case fall within public disclosure. Public disclosure is also mandatory regardless of value if the securities traded are more than 2,500 in number, or if the share represent more than 1% of the total share capital. The Committee has consciously reviewed such thresholds from the standpoint of materiality and relevance and is recommending reform to rationalize the trades disclosure threshold at a value of Rs. 10,00,000 or more in a calendar quarter.
78. On the other hand, it is critical to ensure that employees, regardless of their designation should report to their employer the trades they execute in securities of the employer. Considering there is no scope for penalty on a company on the ground of a violation by the employees, the Committee believes that this fundamental reform measure should indeed be recommended, taking note with respect, the dissenting voice of those representing industry.

Code of Conduct:

79. The Committee believes that every listed company and every market intermediary registered with SEBI should have a code of conduct to regulate, monitor and report trading by its employees and other connected persons with a view to monitor the administration of the regulations, and their enforcement. The Committee has set out mandatory minimum standards that such codes of conduct would need to have, leaving it to the entities in

question to formulate the actual code of conduct that they would adopt. The Code of Conduct pursuant to the Proposed Regulations are not meant to enhance or dilute the charging provisions of the Proposed Regulations. The Committee strongly believes that replicating the provisions of the Proposed Regulations in another draft code of conduct can have unintended consequences such as the creation of conflicting requirements, provisions getting out-dated after amendment of the provisions and the risk of being too narrowly prescriptive rather than achieve a bigger regulatory mandate of nudging such entities to think through what is best suited for them.

80. The minimum standards stipulated in **Schedule B to the Proposed Regulations** entail a serious role for the compliance officer who would need to police, monitor and regulate trading by employees and connected persons. A system of pre-clearance of trades, post-transaction reporting and recording of reasons for decisions has to be devised by each such entity. In addition, one of the standards statutorily prescribed is that UPSI should be handled on a need to know basis.
81. The Committee felt that all other entities and agencies that would routinely be required to handle UPSI in the course of their business operations, and over which SEBI may not have jurisdiction should, in any case, be given the discretion and a clear policy nudge towards adopting such a code of conduct for their own internal organisation. The same principles as applicable to listed companies and market intermediaries would apply to such codes of conduct as well. Some of such entities may be subject to their own regulatory oversight by different agencies such as the Bar Council of India, Institute of Chartered Accountants of India, Institute of Company Secretaries of India etc.. Therefore, enabling them to formulate such a code of conduct would put at rest the doubt about jurisdictional issues but the existence of a code of conduct would point to the seriousness with which the entity treats compliance with matters relating to insider trading. Such an approach would nudge society into a higher level of compliance and nudging of a social framework that is more conducive to eradicating insider trading.

82. The Committee's attention was also drawn to a circular bearing Ref. No. MFD/CIR No. 4/216/2001 dated May 8, 2001 issued by SEBI's Mutual Fund Division governing, among others, insider trading-related requirements issued to mutual funds. It was felt that the SEBI Circular was issued even before the requirement to have a code of conduct for market intermediaries was introduced in the PIT Regulations, 1992. There is no longer a special need for a special or separate circular for a specific class of market intermediaries on the subject of insider trading. It is therefore recommended that the aforesaid SEBI Circular insofar as it relates to insider trading be withdrawn by SEBI to ensure that there is no inconsistency and the regulatory requirements are kept precise and clear.
83. The Committee has therefore spelt out provisions of **Regulation 9 read with Schedule B of the Proposed Regulations**, relating to the Code of Conduct in line with the foregoing discussions.

Principles of Fair Disclosure:

84. The Committee feels that the market looks primarily to the listing agreement in determining the obligations on disclosures. However, the PIT Regulations, 1992 indeed has a schedule on disclosures to be followed. It was felt that it is important to strengthen it and provide clear-cut principles on how a listed company should follow best practices relating to fair disclosures about emergence of any UPSI that warrants public dissemination.
85. The Committee believes that it is necessary to statutorily lay down the principles that every such code should conform to such as the need for prompt disclosure of material information that could impact price discovery no sooner than credible and concrete information comes into existence. Speculative disclosures or selective disclosures that could in fact have an adverse impact on the market and the price discovery process should be avoided. Even if UPSI were to get disclosed selectively, inadvertently or otherwise, the Committee believes that without prejudice to punitive consequences for violating the

requirement not to communicate UPSI, the company should remedy the mistake by making the information available to the public.

86. It is important to mention that any remedial action such as dissemination of UPSI that is wrongly disclosed selectively in violation of the prohibition on communication and counseling of UPSI other than for discharge of legitimate duties and purposes would not detract from the regulatory consequences of breaching the prohibition. Such dissemination is meant to set right the mistake or the wrong but that would not be the ground for excusing a violator from the consequences of the violation. Indeed, whether to punish and how to measure the penalty should be independently assessed in accordance with known and settled principles of imposition of penalty with the considerations mandated in law being followed.
87. In view of the foregoing, the provisions of **Regulation 8 read with Schedule A of the Proposed Regulations** have been drafted.

Onus of Proof:

88. Finally, it would be remiss if the Committee does not articulate a view on how the onus of proof would play out under the Proposed Regulations. The onus of showing that a certain person is an insider and that he was in possession of UPSI at the time of trading would naturally be on the person leveling the charge. To bring such a charge, the ingredients would be to show that the person is an insider, that trading indeed took place and that a reasonable inference of being in possession of UPSI is possible. Thereafter, the alleged insider who has traded may demonstrate that he was not in possession of UPSI, or that he has not traded himself and that someone else took the decision to trade without reference to him, or indeed, that any of the available defences articulated above are attracted. The onus of proving the defence would be on the person accused of violating the prohibition.
89. It was felt that in the case of a “connected person” where the connection is stronger and, therefore, the access to information would be even more direct (as compared to any other person who becomes an insider by reason of receipt of the UPSI) the onus of demonstrating

that the connected person in fact did not have access to the UPSI would be on the connected person. In other cases, it would be important for SEBI to demonstrate a *prima facie* case that there had been possession of UPSI when the insider who is not a connected person has traded.

90. No law or regulation can envisage all future factual situations. Therefore, it would not be possible to make provisions for every scenario. It is important to lay down clear and focused definitions and identify concepts and principles which would make it possible for society to ascertain the status of compliance or non-compliance accordingly. Consequently, the Proposed Regulations provide for various concepts and principles to enable the regulator and the courts to arrive at a view on whether a transaction in question is compliant or violative in character. The legislative notes attached to the provisions are intended to throw light on the principles set out in the provisions. The Committee is cognizant of the fact that India is a common law country where interpretation of statutes is not always literal in nature but is founded on the principles of justice, equity and good conscience. The Committee sincerely hopes that its effort in making the Proposed Regulations will lead to a clearer understanding of the issues involved in insider trading in India and how best it can be tackled – both by way of regulations that nudge society to become more compliant and also by way of clarity and predictability of the regulations that will enable swift and clear enforcement.

PART III

DRAFT OF THE PROPOSED REGULATIONS

CHAPTER – I

PRELIMINARY

Short title and commencement.

1. (1) These regulations may be called the SEBI (Prohibition of Insider Trading) Regulations, 2013.

(2) These regulations shall come into force on such date as may be specified by the Board.

***NOTE:** Since the scope of what is prohibited, what defences are available to an alleged breach of a prohibition and a new regime for enabling compliant trading by insiders is envisaged, it is intended that the Board be empowered to fix an appropriate prospective date to bring these regulations into effect giving the market and officials of the Board appropriate time to arrange their affairs to operate under the new regulations.*

(3) The notes set out along with the provisions of these regulations are an integral part thereof setting out the legislative intent to guide the interpretation of these regulations.

***NOTE:** It is intended that the note in relation to any provision contained herein shall guide the authorities administering the regulations and courts interpreting these regulations about the intent, scope and legislative reasoning in connection with the provision to which it relates.*

Definitions.

2. (1) In these regulations, unless the context otherwise requires, the following words, expressions and derivations therefrom shall have the meanings assigned to them as under:–

***NOTE:** These are the meanings that are intended to ordinarily apply to these defined terms for their usage in these regulations. If the context requires a different meaning to be given to any of these words to further the purpose of these regulations, such different meaning could be adopted.*

- (a) “Act” means the Securities and Exchange Board of India Act, 1992 (15 of 1992);
- (b) “Board” means the Securities and Exchange Board of India;
- (c) "company" means any entity that has issued securities which are listed on a stock exchange or which are intended to be so listed;

***NOTE:** It is intended that securities should be capable of being traded for them to be amenable to price discovery and consequently be exposed to the prospect of an insider benefitting from trading when in possession of unpublished price sensitive information. In the absence of the ability to discover price in a market through an inter-play of demand and supply, it would not be possible to bring a charge of insider trading i.e. of an insider benefitting from possession of unpublished-price sensitive information to the detriment of others in the market. It is possible that without a market for price-discovery being in place there could be abuse of asymmetry of information leading to fraud in connection with dealing in securities – such market abuse would be squarely covered by the SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to the Securities Market) Regulations, 2003, and is not intended to be covered by these regulations.*

- (d) “compliance officer” means any senior officer who is financially literate and is capable of appreciating requirements for legal and regulatory compliance under these regulations;

***NOTE:** Under these regulations, every issuer and market intermediary would need to appoint a compliance officer. It is intended that such compliance officer should be one who is capable of appreciating regulatory and legal requirements and has the ability to read and understand basic financial statements so as to understand the impact of unpublished price sensitive information on price discovery for securities so that he is able to administer the regulations in an informed manner.*

- (e) "connected person" means any person who is or has during the six months prior to the concerned trade been associated with a company in any capacity including by reason of frequent communication with its officers or being in any contractual, fiduciary or employment relationship and includes any person who is a public servant or occupies a

statutory position that allows such person access to unpublished price sensitive information relating to the company or is reasonably expected to allow such access;

Provided that immediate relatives of connected persons shall be deemed to be connected persons unless such immediate relative can establish absence of access or reasonable expectation of access to unpublished price sensitive information;

NOTE: *It is intended that a connected person is one who has a connection with the company that is expected to put him in possession of unpublished price sensitive information. Immediate relatives of such persons are also presumed to be connected persons but such a presumption is a deeming legal fiction and is rebuttable.*

This definition is also intended to bring into its ambit persons who may not seemingly occupy any position in a company but are in regular touch with the company and its officers and are involved in how the company operates. It is intended to bring within its ambit those who would have access to unpublished price sensitive information about any company or class of companies by virtue of being government servants and occupying official positions that would put them in possession of unpublished price sensitive information – for example, an officer in the government who would know ahead of the market about a proposed policy change that would impact market price say, a proposed change in foreign ownership limit in specific sectors would be a connected person and thereby an insider.

So also, it is intended to cover, for example, a judge whose decision in a litigation could have a material bearing on the price of the securities in the market when the judgement is made public, say, a decision on a dispute over whether the offer price for an open offer under the takeover regulations should be higher or lower. All such persons are intended to be “connected persons” and thereby insiders who would be prohibited from trading in securities of the company when in possession of unpublished price sensitive information.

(f) "generally available information" means information that is accessible to the public on a non-discriminatory basis and shall include research and analysis based thereon;

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 that is accessible to the public on a non-discriminatory basis say, information published on the website of a stock exchange,*

would normally be considered generally available. Research, deductions and conclusions based on generally available information will also constitute “generally available information”. For example, organisations that provide research reports may add value to the information because of their research and analysis but so long as the research is based on generally available information, the findings of such research would not become unpublished price sensitive information. Such research reports may be available for a price (to compensate for their enterprise of conducting research) and so long as such research is available for purchase by clients without discrimination, the fact that it has to be paid for would not make the access discriminatory. So long as it can be shown that the research is based on information in the public domain, the findings would also be “generally available information”.

So also, it is intended that information that is capable of being accessed by any one without breach of any law would be considered generally available. For example, a person legitimately watching and counting the movement of goods from factories of a company and making his own analysis and assessment without involving a breach of the obligations under these regulations would be accessing information that is generally available. Such research would not render him to be in possession of unpublished price sensitive information. However, a person who procures such information by breaking into the company’s systems or by reason of an insider passing on such information in breach of the obligation to keep information confidential, would be regarded as having availed of publicly accessible information.

(g) “immediate relative” means a spouse of a person, and includes parent, sibling, and child of such person or of the spouse, any of whom is either dependent financially on such person, or consults such person in taking decisions relating to trading in securities;

NOTE: *It is intended that to presume in the eyes of law that immediate relatives, who are closely connected to connected persons, are deemed to have access to the mind of the person whose immediate relatives they are. Immediate relatives of any person are those who are financially dependent and also those who consult the person concerned in taking decisions on securities trading. It is intended that the immediate relatives of a “connected person” too become connected persons for purposes of these regulations. Indeed, this too is rebuttable akin to the takeover regulations where such an approach has been adopted for a deeming and rebuttable fiction of various persons having a common objective or purpose of acquisition.*

(h) "insider" means any person who is:

i) a connected person; or

- ii) in possession of unpublished price sensitive information;

NOTE: Since “generally available information” is defined, it is intended that anyone in possession of unpublished price sensitive information should be considered an “insider” regardless of how one came in possession of such information. Various defences are provided for such a person to demonstrate that he has not indulged in insider trading. Therefore, this definition is intended to bring within its reach any person who is in receipt of unpublished price sensitive information and the charging provisions would deal with whether or not the prohibition has been violated. The onus of showing that a certain person was in possession of unpublished price sensitive information at the time of trading would, therefore, be on the person leveling the charge after which the person who has traded when in possession of unpublished price sensitive information may demonstrate that he was not in such possession or that he has not traded or that his trading when in possession of such information was squarely covered by the available defences.

(i) "promoter" shall have the meaning assigned to it under the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009;

(j) "public servant" shall have the meaning assigned to it under the Prevention of Corruption Act, 1988 (49 of 1988);

(k) "securities" shall have the meaning assigned to it under the Securities Contracts (Regulation) Act, 1956 (42 of 1956);

NOTE: It is intended to adopt the well-settled and well-interpreted definition of “securities”. Since the possession of “unpublished price sensitive information” about a “company” results in a prohibition on trading in securities, this definition should be read in conjunction with these definitions. For purposes of what “securities” are, the time-tested definition of the term adopted across all securities laws is intended to be adopted. It is intended that read with other definitions and charging provisions of these regulations, any instrument that fits within the definition of “securities” would be covered by these regulations if they are listed and are amenable to price discovery on a market platform. Therefore, a security such as a derivative instrument which is not issued by the company but which is based on an interest in a security issued by the company and is traded on stock exchanges too would be covered within the scope of these regulations. Securities covered would be those that are listed on stock exchanges including listed securities that are issued by market intermediaries such as mutual funds and collective investment schemes.

(l) "specified" means specified by the Board in writing;

NOTE: It is intended that the Board be given flexibility to specify norms and guidance acting through the Chairman or Wholetime Members by way of circulars on specific areas where the Board may require to calibrate the regulatory measure provided for in these regulations. Such specification should be in writing and disseminated publicly.

(m) "takeover regulations" means the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011;

(n) "trading" means transacting in securities whether by way of acquisition or disposal;

NOTE: Since the regulations deal with insider trading, it is intended to use the term "trading" uniformly instead of the term "dealing" which is a very wide term. The change of nomenclature from "dealing" does not mean that market abuse in the form of any dealing other than trading i.e. transacting in securities for consideration would not be covered by securities laws. Other provisions such as the SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to the Securities Market) Regulations, 2003 would cover the scope of such other forms of market abuse. So also it should be noted that in any case, any contrivance or device that is aimed at executing an indirect act of insider trading without involving "trading" would fall foul of Section 12A of the Securities and Exchange Board of India Act, 1992.

(o) "trading day" means a day on which the recognized stock exchanges are open for trading;

(p) "unpublished price sensitive information" means 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 and will ordinarily include information relating to the following: –

(i) financial results;

- (ii) dividends;
- (iii) change in capital structure;
- (iv) mergers, de-mergers, acquisitions, delistings, disposals and expansion of business and such other transactions; and
- (v) changes in key management personnel;

NOTE: *It is intended that information that is not generally available would be unpublished price sensitive information if it is likely to materially affect the price upon coming into the public domain. Since this will always be a mixed question of fact and law, a bright line indicating the types of matters that would ordinarily give rise to unpublished price sensitive information should be listed to give illustrative guidance about the nature of unpublished price sensitive information when a court has to determine whether any piece of information is unpublished price sensitive information. These listed illustrations are ordinarily in the nature of information that could affect the price upon becoming public and are not exhaustive. Merely because a particular type of event is listed above it should not lead to inexorably being regarded as unpublished price sensitive information regardless of its potential price impact. For example, where a very large company makes a non-material and inconsequential acquisition of a tiny business, or where a company declares the same rate of dividend that it has declared for several years as per publicly stated dividend policy.*

(2) Words and expressions used and not defined in these regulations but defined in the Securities and Exchange Board of India Act, 1992 (15 of 1992), the Securities Contracts (Regulation) Act, 1956 (42 of 1956) or the Depositories Act, 1996 (22 of 1996) and rules and regulations made thereunder shall have the meanings respectively assigned to them in those legislation.

CHAPTER – II

RESTRICTIONS ON COMMUNICATION AND TRADING BY INSIDERS

Communication or procurement of unpublished price sensitive information.

3. (1) No insider shall communicate, provide, or allow access to any unpublished price sensitive information to any person including other insiders except where such communication is in furtherance of legitimate purposes, performance of duties or discharge of legal obligations.

***NOTE:** This provision is intended to cast an obligation on all insiders who are essentially persons in possession of unpublished price sensitive information to handle such information with care and to deal with the information with them when transacting their business strictly on a need-to-know basis. This provision is also intended to impose an obligation not to make selective disclosures of such information except within the framework for fair disclosure set out in these regulations. This standard is intended to lead to organisations developing practices based on need-to-know principles for treatment of information in their possession.*

(2) No person shall procure from or cause the communication by any insider of unpublished price sensitive information except in furtherance of legitimate purposes, performance of duties or discharge of legal obligations.

***NOTE:** This provision is intended to impose a statutory prohibition on unlawfully procuring possession of unpublished price sensitive information. Inducement and procurement of unpublished price sensitive information not in furtherance of one's legitimate duties and discharge of obligations would be illegal under this provision.*

(3) Notwithstanding anything contained in this regulation, it shall be legitimate to conduct due diligence on a company in connection with the assessment of any 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 and conduct of due diligence therefor are in the best interests of the company;

***NOTE:** It is intended to acknowledge the necessity for substantial transactions such as takeovers, mergers and acquisitions involving trading in securities and change of control to entail due diligence to assess a*

potential investment. In an open offer under the takeover regulations, not only would the same price be made available to all shareholders of the company but also all information necessary to enable an informed divestment or retention decision by the public shareholders is required to be made available to all shareholders in the letter of offer under those regulations.

(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 and conduct of due diligence therefor are in the best interests of the company and the diligence findings that constitute unpublished price sensitive information are 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.

NOTE: *It is intended to permit conduct of due diligence for transactions that do not entail an open offer obligation under the takeover regulations if the board of directors of the company are able to justify the view that it is necessary to further the best interests of the company. The board of directors would also need to cause public disclosures of the diligence findings constituting unpublished price sensitive information so that there is no asymmetry of access to information in the market.*

(4) For purposes of sub-regulation (3), the board of directors shall require the parties conducting due diligence to execute agreements to contract confidentiality and non-disclosure obligations on the part of such parties and such parties shall keep information so received confidential, save and except for conduct of due diligence, and shall not otherwise trade in securities of the company when in possession of unpublished price sensitive information.

Trading when in possession of unpublished price sensitive information.

4. (1) No insider shall trade in securities that are listed on a stock exchange when in possession of unpublished price sensitive information relating to such securities.

NOTE: *This is the primary charging prohibition on insider trading. It is intended that when a person who has traded in securities has been in possession of unpublished price sensitive information, his trades would be assumed to have been motivated by the knowledge and awareness of such information in his possession. The reasons for which he trades or the purposes to which he applies the proceeds of the transactions are not intended to be relevant for determining whether a person has breached the prohibition. Whether he traded when in possession is what*

would need to be demonstrated at the outset to bring a charge. Once this is established, it would be open to the insider to rely on the defences made available to him, failing which he would have violated the prohibition.

(2) Where an insider who has traded in securities is a connected person, the onus of establishing that he was not in breach of the prohibition in sub-regulation (1) shall be on such connected person.

NOTE: *It is intended that when a connected person has traded, it is for him to demonstrate that he did not violate the prohibition under sub-regulation (1) – for example, by demonstrating that the information in his possession was not unpublished price sensitive information, or that the trades were not decided upon or executed by him, or that the trades were pursuant to a trading plan, or that any of the other defences available to him under sub-regulation (3) are indeed available to him. This standard is only for those insiders who are “connected persons” and not for others who are alleged to have committed insider trading. In those cases, the onus would be on the Board to show a reasonable prospect of access to the information or to a connected person.*

(3) Notwithstanding anything contained in sub-regulation (1), it shall be open to the insider who has traded when in possession of unpublished price sensitive information to demonstrate as a valid defence that: –

NOTE: *The onus of proving these defences would be on the person adopting the defence.*

(i) the nature of his trades was contrary to the manner in which any person acting reasonably would have traded when seeking to take advantage of the nature of the unpublished price sensitive information in his possession;

NOTE: *This provision is intended to enable a person who has traded contrary to the nature of the information in his possession to establish his innocence. For example, a person in possession of positive information may demonstrate that he has actually sold securities whereas a reasonable man seeking to profit from the unpublished nature of such information would have actually acquired securities. Likewise, a person who has acquired securities could show that the unpublished price sensitive information with him was actually adverse.*

(ii) he was an innocent recipient of unpublished price sensitive information and had no reason to believe, exercising diligence expected of a reasonable man, that the

information in his possession was unpublished price sensitive information or the person who communicated it to him violated any law or confidentiality obligation owed by such person;

NOTE: This provision is intended to enable a person who has traded bona fide when in possession of unpublished price sensitive information that he had no cause to believe that the information with him was unpublished price sensitive information. For example, if a research report is in possession of a person who is accused of insider trading and it turns out that the research report was a product of access to unpublished price sensitive information, the person who has traded bona fide should demonstrate that he had no reason to believe that what he read in the research report was a product of violation of law and that he had no role in the violation that occurred in the authorship of the research report. The person adopting the defence may also show that he did not have reason to believe that the person putting him in possession of information was in breach of a duty or was violating these regulations in giving him the information. The nature of the information and whether any reasonable man would believe it not to be unpublished price sensitive information would be material in assessing this defence.

(iii) the counterparty to the transaction is identifiable and such counterparty was 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;

NOTE: This provision is intended to protect trades between two identically placed persons from violating sub-regulation (1). Two insiders who are identically placed in terms of possession of unpublished price sensitive information – for example, transactions involved in inter-promoter or inter-institutional re-arrangements of existing shareholding. Such transactions would not be prohibited on the ground that both the buyer and seller are in possession of unpublished price sensitive information since both would be possession of the very same unpublished price sensitive information and one could not have been victimized by the other with disparity in access to information.

(iv) the trade was an exercise of stock options for which the exercise price was pre-determined in compliance with applicable regulations;

NOTE: This provision is intended to protect exercise of employee stock options that are granted with an exercise price upfront since stock options can be exercised only when the options have vested – typically, one year after the grant. The price for exercise of the stock option is fixed earlier and therefore, the

exercise ought not to become violative because new unpublished price sensitive information comes into the possession of the employee who has been granted stock options at a pre-determined price formula.

(v) 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 that 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;

NOTE: *This provision is intended to enable business organisations or groups of entities that trade in securities to put in place arrangements to comply with these regulations such as Chinese Walls and segregation of roles to ensure that unpublished price sensitive information is cordoned off and other arms of the same organisation do not get access to the same. Therefore, if the organisation or group adheres to these safeguards, they would not violate the prohibition in sub-regulation (1).*

(vi) the trades of the insider were made by another person authorised to so trade on the insider's behalf without reference to and without prior knowledge of the insider and that other person who traded was not in possession of the unpublished price sensitive information and appropriate and adequate arrangements were in place to ensure that these regulations are not violated;

NOTE: *This provision is intended to enable insiders to create a blind trust or appoint discretionary portfolio managers or investment advisors who act on their behalf and are fully authorised to take trading decisions of their own accord without any involvement of the insider. This provision is also intended to protect an insider from a violation of sub-regulation (1) when a lender or trustee to whom the insider has pledged or encumbered securities, transacts in exercise of his enforcement rights. The creation of any*

pledge as a circumventing contrivance or device would indeed result in this defence not being available since that would be a violation of Section 12A of the Act.

(vii) the trades were pursuant to a trading plan set up in accordance with regulation 5.

NOTE: *This provision is intended to enable insiders to formulate a trading plan under regulation 5 pursuant to which trades may be effected in future by when the unpublished price sensitive information that may have been in their possession when formulating the trading plan would become generally available and new unpublished price sensitive information may come into their possession. Since the decision to trade would be taken without being in possession of unpublished price sensitive information, this shall be a valid defence.*

(4) The Board may specify such standards and requirements as may be necessary for arrangements referred to in these regulations to be regarded as being appropriate and adequate in respect of: –

(i) standards for treatment of information on a need-to-know basis among insiders;

(ii) execution of non-disclosure agreements between communicators and recipients of unpublished price sensitive information;

(iii) procedures for binding any person who necessarily has to be put in possession of information to an obligation not to disclose further except on a need-to-know basis and in furtherance of legitimate purposes, performance of duties and discharge of legal obligations; and

(iv) model codes of conduct laying down minimum standards to be adopted by companies and their insiders.

Trading Plans.

5. (1) 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.

NOTE: *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 possession of unpublished price sensitive information when a trade under a trading plan is actually executed would not prohibit the execution of such trades that he had pre-decided even before the unpublished price sensitive information came into being. Trading on the basis of such a trading plan would not grant absolute immunity from bringing proceedings for market abuse. For instance, in the event of manipulative timing of the release of unpublished price sensitive information to ensure that trading under a trading plan becomes lucrative in circumvention of regulation 4 being detected, it would be open to initiate proceedings for alleged breach of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to the Securities Market) Regulations, 2003.*

(2) Such trading plan shall:—

(i) not entail commencement of trading on behalf of the insider earlier than six months from the public disclosure of the plan;

NOTE: *It is intended that to get the benefit of a trading plan, a cool-off period of six months is necessary. Such a period is considered reasonably long for unpublished price sensitive information that is in possession of the insider when formulating the trading plan, to become generally available. It is also considered to be a reasonable period for a time lag in which new unpublished price sensitive information may come into being without adversely affecting the trading plan formulated earlier. In any case, it should be remembered that this is only a statutory cool-off period and would not grant immunity from action if the insider were to be in possession of the same unpublished price sensitive information both at the time of formulation of the plan and implementation of the same.*

(ii) not entail trading for the period between the twentieth trading day prior to the last day of any financial period for which results are required to be announced by the issuer of the securities and the second trading day after the disclosure of such financial results;

NOTE: *Since the trading plan is envisaged to be an exception to the general rule prohibiting trading by insiders when in possession of unpublished price sensitive information, it is important that the trading plan does not entail trading for a reasonable period around the declaration of financial results as that would generate unpublished price sensitive information.*

(iii) entail trading for a period of not less than twelve months;

NOTE: *It is intended that it would be undesirable to have frequent announcements of trading plans for short periods of time rendering meaningless the defence of a reasonable time gap between the decision to trade and the actual trade. Hence it is felt that a reasonable time would be twelve months.*

(iv) not entail overlap of any period for which another trading plan is already in existence; and

NOTE: *It is intended that it would be undesirable to have multiple trading plans operating during the same time period. Since it would be possible for an insider to time the publication of the unpublished price sensitive information to make it generally available instead of timing the trades, it is important not to have the ability to initiate more than one plan covering the same time period.*

(v) 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.

NOTE: *It is intended that while regulations should not be too prescriptive and rigid about what a trading plan should entail, they should stipulate certain basic parameters that a trading plan should conform to and within which, the plan may be formulated with full flexibility. The nature of the trades entailed in the trading plan i.e. acquisition or disposal should be set out. The trading plan may set out the value of securities or the number of securities to be invested or divested. Specific dates or specific time intervals may be set out in the plan.*

(3) The compliance officer shall review the trading plan to assess whether the plan would have any potential for violation of these regulations and shall be entitled to seek such express

undertakings as may be necessary to enable such assessment and to approve and monitor the implementation of the plan.

NOTE: *It is intended that the compliance officer would have to review and approve the plan. For doing so, he may need the insider to declare that he is not in possession of unpublished price sensitive information or that he would ensure that any unpublished price sensitive information in his possession becomes generally available before he commences executing his trades. Once satisfied, he may approve the trading plan, which would then have to be implemented in accordance with these regulations.*

(4) 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.

Provided that the implementation of the trading plan shall not be commenced if any unpublished price sensitive information in possession of the insider at the time of formulation of the plan has not become generally available at the time of the commencement of implementation and in such event the compliance officer shall confirm that the commencement ought to be deferred until such unpublished price sensitive information becomes generally available information so as to avoid a violation of sub-regulation (1) of regulation 4.

NOTE: *It is intended that since the trading plan is an exception to the general rule that an insider should not trade when in possession of unpublished price sensitive information, changing the plan or trading outside the same would negate the intent behind the exception. Other investors in the market, too, would factor the impact of the trading plan on their own trading decisions and in price discovery. Therefore, it is not fair or desirable to permit the insider to deviate from the trading plan based on which others in the market have assessed their views on the securities.*

The proviso is intended to address the prospect that despite the six-month gap between the formulation of the trading plan and its commencement, the unpublished price sensitive information in possession of the insider is still not generally available. In such a situation, commencement of the plan would conflict with the over-riding principle that trades should not be executed when in possession of such information. If the very same unpublished price sensitive information is still in the insider's possession, the commencement of execution of the trading plan ought to be deferred.

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

NOTE: *It is intended that given the material exception to the prohibitory rule in regulation 4, a trading plan is required to be publicly disseminated. Investors in the market at large would also factor the potential pointers in the trading plan in their own assessment of the securities and price discovery for them on the premise of how the insiders perceive the prospects or approach the securities in their trading plan.*

CHAPTER – III

DISCLOSURES OF TRADING BY INSIDERS

General provisions.

6. (1) Every public disclosure under this Chapter shall be made in such form as may be specified.

(2) The disclosures to be made by any individual under this Chapter shall include those relating to trading by such person's immediate relatives, and by any other person for whom such person takes trading decisions.

***NOTE:** It is intended that disclosure of trades would need to be of not only those executed by the person concerned but also by the immediate relatives and of other persons for whom the person concerned takes trading decisions. These regulations are primarily aimed at preventing abuse by trading when in possession of unpublished price sensitive information and therefore, what matters is whether the person who takes trading decisions is in possession of such information rather than whether the person who has title to the trades is in such possession.*

(3) The disclosures made under this Chapter shall be maintained by the company in such form as may be specified.

(4) 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 for purposes of this Chapter.

Disclosures by certain persons.

7. (1) Every promoter, employee and director of every company whose securities are listed on any recognised stock exchange shall disclose to the company within thirty days of these regulations taking effect, his holding of securities of the company.

***NOTE:** It is intended that these specific insiders being closely connected with the company should disclose their holdings in securities of the company including derivatives positions to the company. This is a one-time disclosure at the commencement of these regulations and this is internal to the company to help the compliance officer monitor*

and administer compliance. A duty is cast by this provision on the employees and directors to make accurate disclosures of their holdings to the company. This is not a public disclosure requirement.

(2) Every person on appointment as an employee or a director of the company or upon becoming a promoter shall disclose to the company, within seven days of such appointment, his holding of securities of the company.

NOTE: *This sub-regulation is intended to cover anyone who newly occupies such a position to make a disclosure within seven days. This disclosure is internal to the company to help the compliance officer monitor and administer compliance. A duty is cast by this provision on the employees and directors to make accurate disclosures of their holdings to the company. This is not a public disclosure requirement.*

(3) Every such person 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 Rs. 10,00,000 or such other value as may be specified.

NOTE: *Since such persons are closely connected to the company, material trades by them are required to be disclosed to the company. This is an internal disclosure within the company and not a public disclosure, and will help the compliance officer to monitor and administer the regulations. A duty is cast by this provision on the employees and directors to make accurate disclosures to the company if the thresholds for disclosures are triggered. Whether such thresholds are triggered is for the employees to track and report accurately to the employer. This is an internal requirement of disclosure from the employees and directors to the company.*

(4) Every company shall notify the particulars of such trading to the stock exchange on which the securities are listed within two working days of receipt of the disclosure or from becoming aware of such information.

Explanation. — It is clarified for the avoidance of doubts that the disclosure of the incremental transactions after any disclosure under this sub-regulation, shall be made when the transactions effected after the prior disclosure cross the threshold specified in sub-regulation (3).

NOTE: *This provision is intended as a continual disclosure requirement. As and when the trading by these insiders crosses the material thresholds specified, a public disclosure would have to be made within the time specified. A duty is cast by this provision on the company to make public disclosures of whatever has been disclosed to it under sub-regulation (3) by the employees and directors i.e. disclosures above a materiality threshold. The company is not required to audit the accuracy of the disclosures, particularly since it may not have the capacity to check trading particulars of immediate relatives of the employees and directors. However, if the company becomes otherwise aware of such trading, it would be required to make the disclosures under this sub-regulation.*

(5) 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 holdings 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.

NOTE: *This is an enabling provision for listed companies to seek information from those to whom it has to provide unpublished price sensitive information. This provision confers discretion on any company to seek such information. It is not mandatory to do so. For example, a listed company may ask that a management consultant who would advise it on corporate strategy and would need to review unpublished price sensitive information, should make disclosures of his trades to the company. This is an internal matter and will not result in a public disclosure. However, this would enable the listed company to internally review and keep a check on whether there has been any trading by persons who become connected persons by virtue of their association with the company.*

CHAPTER – IV

CODES OF FAIR DISCLOSURE AND CONDUCT

Code of Fair Disclosure.

8. (1) The board of directors of every company shall formulate and publish on its official website, a code of practices and procedures for fair disclosure of material information that it would follow in order to adhere to each of the principles set out in Schedule A to these regulations.

***NOTE:** This provision intends to require every company whose shares are listed on stock exchanges 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. Principles such as, equality of access to information, publication of policies such as those on dividend, inorganic growth pursuits, calls and meetings with analysts, publication of transcripts of such calls and meetings, and the like are set out in the schedule.*

(2) Every such policy and every amendment thereto shall be promptly intimated to the stock exchanges where the securities are listed.

***NOTE:** This provision is aimed at requiring transparent disclosure of the policy formulated in sub-regulation (1).*

Code of Conduct.

9. (1) The board of directors of every company and market intermediary 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, adopting the minimum standards set out in Schedule B to these regulations.

***NOTE:** It is intended that every company whose securities are listed on stock exchanges and every market intermediary registered with SEBI is mandatorily required to formulate a code of conduct governing trading by its employees. The standards set out in the schedule are required to be addressed by such code of conduct.*

(2) Every other person who is required to handle unpublished price sensitive information in the course of business operations may formulate a code of conduct to regulate, monitor and

report trading by employees and other connected persons towards achieving compliance with these regulations, adopting the minimum standards set out in Schedule B to these regulations.

NOTE: *This provision is intended to enable persons other than listed companies and market intermediaries that are required to handle unpublished price sensitive information to formulate a code of conduct governing trading in securities by their employees. Some of these persons may also be regulated by other agencies while some others may themselves be playing the role of regulatory agencies. Even entities that normally operate outside the capital market may handle unpublished price sensitive information. This provision would enable all of them to formulate a code of conduct. The existence of such a code would point to the seriousness with which the organisations treat compliance requirements under these regulations. However, the existence or the absence of a code of conduct would not in any way alter the full force of applicability of these regulations including the prohibitions set out in regulations 3 and 4.*

(3) Every company, market intermediary and other persons formulating a code of conduct under sub-regulation (2) shall identify and designate a compliance officer to administer the code of conduct and other requirements under these regulations.

NOTE: *This provision is intended to designate a senior officer as the compliance officer with the responsibility to administer the code of conduct and monitor compliance with these regulations.*

CHAPTER – V
MISCELLANEOUS

Sanction for violations.

10. Any contravention of these regulations shall be dealt with by the Board following principles of natural justice and the Board may take remedial or punitive measures in exercise of its powers under the Act.

***NOTE:** The Act sets out various powers to issue remedial directions, impose punitive sanctions and to initiate prosecution for the violation of these regulations.*

Repeal and Savings.

11. (1) The Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 1992 are hereby repealed.

***NOTE:** These regulations are intended to replace the earlier regulations on the subject.*

(2) Notwithstanding such repeal,—

(a) the previous operation of the repealed regulations or anything duly done or suffered thereunder, any right, privilege, obligation or liability acquired, accrued or incurred under the repealed regulations, any penalty, forfeiture or punishment incurred in respect of any offence committed against the repealed regulations, or any investigation, legal proceeding or remedy in respect of any such right, privilege, obligation, liability, penalty, forfeiture or punishment as aforesaid, shall remain unaffected as if the repealed regulations had never been repealed; and

(b) anything done or any action taken or purported to have been done or taken including any adjudication, enquiry or investigation commenced or show-cause notice issued under the repealed regulations prior to such repeal, shall be deemed to have been done or taken under the corresponding provisions of these regulations;

NOTE: *This provision is intended to save actions, decisions, rights and liabilities that have already arisen under the repealed regulations so that they do not lapse.*

(3) After the repeal of Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 1992, any reference thereto in any other regulations made, guidelines or circulars issued thereunder by the Board shall be deemed to be a reference to the corresponding provisions of these regulations.

NOTE: *It is intended that any reference to the repealed regulations in other regulations, guidelines or circulars does not need to be replaced with reference to these regulations and the references shall automatically be assumed to be references to the corresponding provisions of these regulations.*

SCHEDULE A

(See sub-regulation (1) of regulation 8)

Principles of Fair Disclosure for purposes of Code of Practices and Procedures for Fair Disclosure of Material Information

1. Prompt public disclosure of material information that would impact price discovery no sooner than credible and concrete information comes into being in order to make such information generally available.
2. Uniform and universal dissemination of material information to avoid selective disclosure.
3. Designation of a senior officer as a chief investor relations officer to deal with dissemination of information and disclosure of material information.
4. Prompt dissemination of material information that gets disclosed selectively, inadvertently or otherwise to make such information generally available.
5. Appropriate and fair response to queries on news reports and requests for verification of market rumours by regulatory authorities.
6. Ensuring that information shared with analysts and research personnel is not unpublished price sensitive information.
7. Developing best practices to make transcripts or records of proceedings of meetings with analysts and other investor relations conferences on the official website to ensure official confirmation and documentation of disclosures made.
8. Handling of all unpublished price sensitive information on a need-to-know basis.

SCHEDULE B

(See sub-regulation (1) and sub-regulation (2) of regulation 9)

Minimum Standards for Code of Conduct to Regulate, Monitor and Report Trading by Insiders

1. The compliance officer shall report to the board of directors and in particular, shall provide reports to the Chairman of the Audit Committee, if any, or to the Chairman of the board of directors at such frequency as may be stipulated by the board of directors.
2. All information shall be handled within the organisation on a need-to-know basis and no unpublished price sensitive information shall be communicated to any person except in furtherance of the insider's legitimate purposes, performance of duties or discharge of his legal obligations. The code of conduct may contain norms for appropriate Chinese Walls procedures, and processes for permitting any designated person to "cross the wall".
3. Employees and connected persons designated on the basis of their functional role ("**designated persons**") in the organisation shall be governed by an internal code of conduct governing dealing in securities. The board of directors shall in consultation with the compliance officer specify the designated persons to be covered by such code on the basis of their role and function in the organisation. Due regard shall be had to the access that such role and function would provide to unpublished price sensitive information in addition to seniority and professional designation.
4. Designated persons may execute trades subject to compliance with these regulations. Towards this end, a notional trading window shall be used as an instrument of monitoring trading by the designated persons. The trading window shall be closed when the compliance officer determines that a designated person or class of designated persons can reasonably be expected to have possession of unpublished price sensitive information. Such closure may be imposed in relation to such securities to which such unpublished price sensitive information relates. Designated persons and their immediate relatives may trade in securities when the trading window is not closed.

5. The timing for re-opening of the trading window shall be determined by the compliance officer taking into account various factors including the unpublished price sensitive information in question becoming generally available and being capable of assimilation by the market, which in any event shall be earlier than twenty-four hours after the information becomes generally available.

6. When the trading window is open, trading by designated persons shall be subject to pre-clearance by the compliance officer, if the value of the proposed trades is above such thresholds as the board of directors may stipulate. No designated person shall apply for pre-clearance of any proposed trade if such designated person is in possession of unpublished price sensitive information even if the trading window is not closed.

7. The compliance officer shall confidentially maintain a list of such securities as a “restricted list” which shall be used as the basis for approving or rejecting applications for pre-clearance of trades.

8. Prior to approving any trades, the compliance officer shall be entitled to seek declarations to the effect that the applicant for pre-clearance is not in possession of any unpublished price sensitive information. He shall also have regard to whether any such declaration is reasonably capable of being rendered inaccurate.

9. The code of conduct may specify any reasonable timeframe within which trades that have been pre-cleared have to be executed by the designated person, failing which fresh pre-clearance would be needed for the trades to be executed.

10. The code of conduct may specify the period within which a designated person who is permitted to trade may not execute a contra trade. The compliance officer may be empowered to grant relaxation from strict application of such restriction for reasons to be recorded in writing provided that such relaxation does not violate these regulations. Should a contra trade be executed, inadvertently or otherwise, in violation of such a restriction, the profits from such trade

shall be liable to be disgorged for remittance to the Board for credit to the Investor Education and Protection Fund administered by the Board under the Act.

11. The code of conduct may stipulate such formats as the board of directors deems necessary for making applications for pre-clearance, reporting of trades executed, reporting of decisions not to trade after securing pre-clearance, recording of reasons for such decisions and for reporting level of holdings in securities at such intervals as may be determined as being necessary to monitor compliance with these regulations.

ANNEXURE

LIST OF PERSONS WHO PROVIDED THEIR INPUTS TO THE COMMITTEE

(in alphabetical order)

1. Aimi Ramlee, Deputy Director, **Asia Trader Forum**
2. Amol Kulkarni, Policy Analyst, Centre for Investment, Competition and Economic Regulation; **CUTS International**
3. Ashok Singh, Manager, Listing Compliance, **Bombay Stock Exchange**
4. Anjali Aggarwal, Vice President, **Corporate Professionals Capital Pvt. Ltd.**
5. Ankit Shah, Chartered Accountant
6. Bharat Vasani, Chief, Legal & Group General Counsel, **Tata Sons Ltd**
7. Compliance Legal
8. Cyril Shroff, Partner, **Amarchand & Mangaldas & Suresh A Shroff & Co**
9. Devang Joshi, Assistant Manager, Compliance-India, Franklin Templeton Asset Management (India) Pvt. Ltd.
10. Dinesh Bhakade
11. **Federation of Indian Chambers of Commerce & Industry**
12. Girish V. Koliyote, Company Secretary, **HDFC Ltd**
13. **HSBC Securities and Capital Markets (India) Pvt. Ltd.**
14. Krishnan Sitaraman, Senior Director-Compliance, **CRISIL Ltd.**
15. Kritika Daga, AGM, **ICICI Bank Ltd.**
16. Nidhi Sharma Wig, Company Secretary
17. Padmaja Shirke, **Union KBC Asset Management Company Private Limited**
18. Pankaj Mishra, AVP Compliance, **Kotak Securities Ltd.**

19. Parmeshwaran N Swamy, Compliance, Equity and F&O, **J.P. Morgan**
20. Pinky Talreja, Company Secretary and Lawyer
21. Pritesh Majumdar, Compliance Officer & Company Secretary, **DSP Blackrock Investment Managers Pvt. Ltd.**
22. S.C. Jain, Company Secretary, **Xpro India Limited**
23. S.K Dixit, Director, **Institute of Company Secretaries of India**
24. Sandeep Parekh, Partner, **FINSEC Law Advisors**
25. Sandip Bhagat, Partner, **S&R Associates**
26. Sanjay Dalmiya
27. Umakanth Varotttil, Assistant Professor, Faculty of Law, **National University of Singapore**
28. Yogesh Chande, Advocate, **Economic Laws Practice**