PROJECT ON
INSIDER TRADING

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INTRODUCTION

Insider trading is defined as the buying, selling, or dealing in securities of a publicly traded company by a director, member of management, or corporate employees, or by another person such as an auditor, directors, consultants, or analytics who has access to "inside" information not available to the general public.

"Insider trading reduces the courage of investors in the securities market because they believe the market is rigged and that only those with insider information benefit and earn from their investment." "Insider trading tarnishes the playing field since it is more than a theft of information." "It's not always evident who the guilty insiders are and who the victims are, and insider trading has both rewards and drawbacks." "Insider trading has gotten a poor rap in the last few decades."

The mainstream press portrays it as a wicked behaviour involving people who are "completely bereft of ethical principles." However, not all insider trading is immoral, and some studies have found that certain types of insider trading are helpful to the financial community as a whole.

Insider trading is defined as "dealing in a company's securities on the basis of associated information about the company that isn't published or not known to the general public" (commonly referred to as unpublished price sensitive information), in order to make profits or avoid losses. It is merely a breach of fiduciary duties of officers of a corporation or connected persons as defined under the Securities Exchange Board of India (Prohibition of Insider trading) Act. It has enacted a number of insider trading restrictions.

Companies that are listed are required to maintain a compliance officer and to keep track of price sensitive data. Insiders now have access to a trading window, as well as prompt reporting of their securities transactions to the compliance officer and stock exchanges." "Any disclosures made by listed businesses or their directors/officers must be immediately posted on the relevant stock exchange's official websites." The organisation of stock exchanges is at a crossroads due to increased competition brought on by deregulation, technology advancements, and economic processes.

IMPORTANT DEFINATION

1. INSIDER TRADING

Insider trading is a breach of fiduciary duties of officers of a company or connected persons as defined under the Securities Exchange Board of India (Prohibition of Insider Trading) Regulations, 1992, toward making profits or avoiding loss by dealing in a company's securities on the basis of confidential information relating to the company that is not published or not known to the public (known and unpublished price sensitive information), used to make profits or avoid loss**.**

By virtue of his job or other relationship, an insider deals in shares of a firm to make unjustified gains, rendering the underlying ideal of fair and free transferability of shares unachievable in the capital market." "The primary aim for the creation of these regulations is to encourage free and fair stock transferability in the capital market, where investors can trade securities without fear of being harmed."

The rising size of the world's securities markets, where shares, derivatives, and bonds are traded on an international level, has increased authorities' concerns around the world." "Because they suspected anomalous profit/gain of businesspersons as well as shareholders, insider trading drew the attention of the public and the government." "In India, the Companies Act has shown a lack of skill in resolving business concerns and restricting unfair trading."

Insider trading has existed throughout the history of financial markets, but it was especially common during the early years of the Indian stock market." "Insider trading is prevalent in developing nations such as India, where it is performed by a diverse group of market participants, company officers, and regulatory authorities." Because of their position, employment, or obligation, primary insiders have access to information. "Controlling shareholders, corporate leaders and officers, as well as financial-market professionals who compile data on a firm's operations" are among them. This group also includes government personnel who have insider information.

Insider trading regulations enable the open exchange of securities-related information, resulting in more efficient stock pricing." "However, when insider trading restrictions prevent insiders from buying or selling on the basis of inside information, stock prices are only consistent with all available information."

"The goal of insider trading laws and regulations is to ensure that no one profits from trading on 'insider' or 'unpublished' information, which is not available to all market participants." The ultimate goal is to create a fair playing field for all market players by making information available to them all. Insider trading laws are enforced, which promotes market liquidity and lowers equity costs.

Evolution of insider trading regulation in India

Although India's stock exchanges have a nearly 134-year history, the regulatory framework governing insider trading is only 17 years old4. Insider trading went unchecked in India for the most of those 134 years." The first attempt to prevent insider trading in India took the form of a requirement for corporate directors to disclose their shareholdings." On the proposal of the Company Law Committee, provisions were added into sections 307 and 308 of the Companies Act 1956. Insider trading was only formally recognised as a bad conduct for the first time in the late 1970s." In 1992, a regulatory authority was established after a series of committee recommendations suggested strict regulation.

A. Sachar Committee (1979): "The High-Powered Expert Committee on Companies and Monopolies and Restrictive Trade Practices Act (MRTP) (Sachar Committee) was established in June 1977 with the purpose of evaluating the Companies Act, 1956 and the MRTP Act, 19696." The Sachar Committee submitted its report in 1979." The Committee offered two recommendations: one, complete disclosure of transactions by people who have made price sensitive information, and the other, restriction of transactions by such persons for a defined period unless extraordinary circumstances exist." "A company director, statutory auditor, accountant, tax and management consultant or advisor, and legal counsel, for example, could engage in such activities among insiders."

All public firms are required to keep a record of all dealings in the company's stock by the above individuals, including their spouses and dependent children, as well as those who are employed full-time by the company and earn a monthly income of three thousand rupees or more.

B. **Patel Committee (1987)**: In May 1984, the Indian government established the Patel Committee, a high-powered committee tasked with conducting a complete evaluation of the operation of stock exchanges and making suggestions. "The committee's final report expressed grave concern about India's lack of particular legislation to prevent the misuse of insider knowledge and suggested severe penalties for insider trading." Insider trading is common in the country's stock exchanges, according to the research, and it is one of the main causes of excessive speculative activity. "Even solicitors, auditors, financial consultants, and financial institutions in possession of concealed price sensitive information are said to be engaging in such activities," according to the paper.

C. Abid Hussein Committee (1989): In 1989, the Working Group on the 'Development of the Capital Market,' also known as the Abid Hussein Committee, was established." Insider trading should be deemed a severe offence punishable by civil fines as well as criminal proceedings, according to the organisation. Insider trading and secret takeover bids are issues that may be largely addressed by suitable regulatory measures." It was suggested that the SEBI be tasked with drafting the appropriate legislation and being given the ability to enforce it.

2.UNPUBLISHED PRICE SENSITIVE INFORMATION (UPSI)

Unpublished price sensitive information" refers to non-public information about a company or its securities that, when made public, is likely to materially affect the price of the securities, and includes but is not limited to:

(i) financial results;

(ii) "dividents;"

(iii) "change in capital structure;"

(iv) "mergers, de-mergers, acquisitions, delisting, dispositions, and business expansion, among other transactions;"

(v) "important management personnel changes; and"

(vi) "material occurrences as defined by the listing agreement"

IMPORTANT REGULATORY REQUIREMENT

RESTRICTION ON COMMUNICATION AND TRADING BY INSIDERS

- Communication or procurement of unpublished price sensitive information

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

 2) Except in advancement of legitimate goals, execution of duties, or satisfaction of legal obligations, no individual shall procure or cause the transmission by an insider of unpublished price sensitive information relating to a firm or securities listed or planned to be listed.

- Trading when in possession of unpublished price sensitive information

 When in possession of unpublished price sensitive information, no insider shall trade in securities that are listed or planned for listing on a stock exchange:
 If the insider can show that he is innocent by establishing the following circumstances

 1) The transaction is an off-market inter-se transfer two promoters who had access to the same unpublished price sensitive information without violating Regulation 3, and both parties had made a deliberate and informed trade decision.

 2) "In the case of non-personal insiders:"

 (a) "appropriate and adequate arrangements were in place to ensure that these regulations were not violated and no unpublished price sensitive information was communicated by those in possession of such unpublished price sensitive information," and (b) "appropriate and adequate arrangements were in place to ensure that these regulations were not violated and no unpublished price sensitive information was communicated by those in possession of such unpublished price sensitive information when they took the decision to trade,"

3) “the trades were pursuant to a trading plan set up in accordance with regulation 5

3.CONNECTED PERSON

"Connected Person" means

"any person who is or has been associated with a company, directly or indirectly, in any capacity during the six months preceding the concerned act, including by reason of frequent communication with its officers or by being in any contractual, fiduciary, or employment relationship, or by being a director, officers, or employee of the company, or holds any position including a professional or business relationship between himself and the company or holds any position including a professional or business relationship between himself and the company.

DEEMED TO BE CONNECTED PERSON

(i) Without the prejudice to the generality of the foregoing, the persons falling with the following categories shall be deemed to be connected persons unless the contrary is established

(a) “an immediate relative of connected persons specified in clause (i); or”

(b) “a holding company or associate company or subsidiary company; or”

(c) “an intermediary as specified in section 12 of the Act or an employee or director thereof; or”

(d) “an investment company, trustee company, asset management company or an employee ordirector thereof; or”

(e) “an official of a stock exchange or of clearing house or corporation; or”

(f) “a member of board of trustees of a mutual fund or a member of the board of directors of theasset management company of a mutual fund or is an employee thereof; or

(g) “a member of the board of directors or an employee of a public financial institution as definedin section 2 of the Companies Act ,2013; or”

(h) “an official or an employee of a self-regulatory organization recognised or authorized by theBoard; or”

(i) “a banker of the company; or”

“a concern, firm, trust, Hindu undivided family, company or association of persons wherein a director of a company or his immediate relative or banker of the company, has more than ten percent of the holding or interest

4. MARKET MANIPULATION

The act of intentionally inflating or deflating the price of a security or otherwise affecting the behaviour of the market for personal gain is known as market manipulation. Manipulation is unlawful in most situations, but in some cases, such as with omnibus accounts, it might be difficult for regulators and other authorities to discover. When someone manipulates the supply or demand of a security, such as by causing stock prices to rise or fall drastically, this is known as market manipulation. Market manipulation is the artificial modification of an asset's price so that it differs from the public's knowledge of the actual price. Instead of using existing possibilities, manipulators strive to fool other market participants and create a false sense of asset mispricing so that they can profit. Market manipulation may or may not include manufacturing and disseminating factually inaccurate comments, but it always entails attempting to affect prices in order to deceive other market participants.

Market manipulation: A result of insider trading

Market manipulation is the outcome of illicit insider trading, and this is not an exaggeration. Market manipulation happens when a person with knowledge of a company's material facts spreads misleading information or fails to disclose certain facts that they are required to disclose, so manipulating prices. Those who have been actively involved in corporate management, or so-called stock-market "gurus," are the ones to blame, as they frequently utilise inflated numbers to enhance the price of the stocks they have purchased.

Techniques of market manipulation

Market manipulators employ a variety of methods to influence stock prices and profit from it. The following are some examples of recognised manipulation techniques:

(a) Market Rumours: Spreading false rumours about a stock's price going up or down when the reverse is true is one of the most well-known techniques of market manipulation. Manipulators have discovered the internet to be a terrific instrument for spreading fake news in this age of technical growth. Companies and stock brokers commonly employ such strategies to disseminate false information about stock prices via chat rooms, message boards, e-mails, and other means.

(b) Pumping and Dumping: Pumping and dumping is a technique for artificially inflating the price of securities. Market manipulators employ the mass media, such as e-mails, to promote a stock, promising an incredible prospect of unknown firms, often a penny stock, in this strategy as well. Insiders and promoters are extremely important in getting ownership and control of a large block of shares.

(c) Churning: This is when traders issue buy-and-sell orders at the same price, with the goal of attracting additional investors while simultaneously increasing the price. Brokers use this to enhance trade activity on behalf of consumers in order to generate commissions for them. It is essentially a breach of the broker's fiduciary duty to the client.

(d) Insider knowledge or front running: This is another unethical method in which a company's insider is involved. In this case, a person who is aware of a significant market transaction makes a profitable deal prior to the transaction. Because an asset is acquired and sold ahead of a public announcement that could materially alter the value of a securities, it is known as front running.

(e) Spoofing: Its goal is to create the illusion that there are many buyers and sellers in the market, and that manipulators often place large orders with no intention of being filled, and that the spoofer profits from this. The short-term traders are the ones that are most affected.

(f) Wash Trading: The manipulators use this strategy to purchase and sell stocks very instantly and repeatedly. This provides investors the misleading impression that the stock has a lot of activity and that buying it would be lucrative for them, resulting in a fake price increase. The schemer then shorts the stock, causing the market to plummet, leaving the investors with nothing.

(g) Bear raiding: In the stock market, there are two sorts of lobbies: the "bull" and the "bear." The bull feels that a stock should be longed, whereas the bear predicts that prices will fall. The bears will sell stocks in large quantities to artificially decrease the price, and when the price falls, other investors will panic and sell the stocks.

Market manipulation: A highly unethical means:

Market manipulation is defined as methods that distort security prices and confuse investors who rely on publicly available information. It puts all investors' interests on hold and disturbs the smooth operation of the market, lowering investor confidence.

Manipulation of the market has the potential to create harm.

(a) Lack of faith in the market's fairness.

(a) Reduce the number of investors.

c) Affect a country's growth and economic health.

d) Distort the financial market's price-setting mechanism. Thus, market manipulation can affect and become a challenge for the market to grow positively, which, when combined with unethical means to manipulate the prices of tradable securities, can cause a hindrance in the country's economic growth due to investors' lack of confidence in the market, can cause a hindrance in the country's economic growth.

INSIDER TRADING REGULATION IN INDIA

An overview of SEBI (Prohibition of insider trading) Regulations (1992)

The SEBI (Prohibition of Insider Trading) Regulations (1992), which came into effect in 1992, established insider trading regulations. Insider trading has been subjected to a number of limitations. A compliance officer is required for listed companies, as well as the preservation of price-sensitive information.

Insiders can now trade and report their securities transactions to the compliance officer and stock exchanges through a new trading window. The disclosures made by listed businesses or their directors/officers must be immediately displayed on the relevant stock exchange's official websites or via a trading terminal alert.

In February 2002, SEBI revised its regulations to include a policy on disclosures and internal procedures for insider trading prevention. Any individual who owns more than 5% of a firm's stock or voting rights must notify the corporation within four working days of their ownership.

It also made continuous disclosures by directors/officers mandatory whenever their holdings increased in value by more than INR 5 lakh, 5,000 shares, or 2% of the total shareholding or voting rights, whichever is lower. Within five days of such disclosures, all publicly traded corporations must report to the stock exchanges where they are listed.

For other entities, SEBI has developed a model code of conduct to prohibit insider trading, as well as sanctions for violating the code.

SEBI introduced disclosure forms 'A', 'B', 'C', and 'D' for directors/officers in July 2003. Form A contains information regarding the purchase of shares in a publicly traded firm by people who own more than 5% of the company. The director or officer's shares in a publicly traded firm are detailed on Form B. Individuals who own more than 5% of a publicly traded firm must fill out Form C, which contains information about changes in their holdings. Details of a director's or officer's holdings in a publicly traded firm are included on Form D.

In April 2007, SEBI added regulation 11A, which governs the procedure of serving summons and notices issued by the board in cases of insider trading.

SEBI modified its regulations in November 2008, including e-filing of stock exchange disclosures and regulation 14 governing actions in the event of default. It made it mandatory for a director/officer and his dependents to report their derivative contract holdings in a publicly traded company to the company in Form B within two working days of becoming a director. They are also prohibited from trading in the company's derivative contracts.

Directors/officers/designated staff of publicly traded firms who buy or sell any number of shares will not sell or buy any number of shares in the six months following the previous transaction. They must hold the share(s) if granted for a minimum of 30 days in the case of an Initial JFC Public Offering. It also made continuous disclosures by directors/officers mandatory whenever their holdings change in value above INR 5 lakh or 25,000 shares or 1% of the total shareholding or voting rights, whichever is lower. Within two working days of such disclosures, all listed businesses must report to the respective stock exchanges where they are listed.

Insider trading was prohibited, and disclosure 52 requirements for insiders were strengthened. To ensure consistency in disclosure requirements across several SEBI regulations, the Act was amended in August 2011 to include a requirement for continuous disclosures by directors/officers whenever their holdings change in value beyond INR 5 lakh or 25,000 shares or 1% of the total shareholding or voting rights, whichever is lower.

SEBI (Prohibition of Insider Trading) Restrictions have been updated to align with takeover regulations (1992). In relation to the promoter and his/her dependent interests in derivative contracts of the listed businesses, Form B and Form D were also revised correspondingly.

In March 2013, SEBI formed a high-level group to evaluate insider trading restrictions, which included Mr N.K. Sodhi, a retired Chief Justice of the Karnataka High Court and a former presiding officer of the Securities Appellate Tribunal (SAT). In December 2013, a high-level committee chaired by N.K. Sodhi delivered a report to SEBI Chairman Shri U.K. Sinha on the SEBI (Prohibition of Insider Trading) Regulations (1992).

The Committee suggested that the legal and enforcement framework be strengthened, that insider trading norms be aligned with worldwide standards, and that terminology and ideas of insider trading be clarified. As a result, the new SEBI (Prohibition of Insider Trading) Regulations (2015), which were published in the gazette on January 15, 2015 and went into effect on May 15, 2015, came into effect.

An overview of SEBI (Prohibition of insider trading) Regulations (2015)

SEBI's (Prohibition of Insider Trading) Regulations (2015) appear to be more upbeat and in line with the global outlook on insider trading. They appear to be well-equipped to improve superior compliance and prosecution."With clarity in the terminology and principles of insider trading, it has improved the insider trading regulations." It has broadened the definition of who is a linked person and has provided more information about the UPSI. It has set limits on insider trading and communication.

Insiders with price-sensitive information can trade using a pre-scheduled trading strategy that must be made public six months ahead of time. Insiders are prohibited from trading 20 days before and two trading days after interim financial results are announced, according to Regulation 5(2)(ii) (even under trading plan). The promoter/director must make their initial disclosures of ownership to the stock market within seven days of their employment with the firm.

Regulation 7(2)(a) made it essential for every listed company's promoter/employee and director to disclose the number of shares/ derivatives purchased or sold during a three-month period valued at INR 10 lakh or more and report within two trading days under the continuous disclosures provisions. It has established minimal requirements for a code of conduct to govern, monitor, and report insider trading.

SEBI has the authority to investigate any complaint received from investors, intermediaries, or other individuals on any topic relating to insider trading suspicions. When an insider owns UPSI, the SEBI (Prohibition of Insider Trading) Regulations (2015) prohibit him or her from dealing in the securities of a firm listed on any stock market on his or her own behalf or on behalf of any other individual. It also bans any insider from discussing, suggesting, or offering (directly or indirectly) any UPSI to any individual who should not trade securities while owning such UPSI.

Price-sensitive information is any information that is directly or indirectly related to a business concern that, if disclosed, is expected to have a significant impact on the price of a company's stocks. Financial results, dividends, changes in capital structure, mergers, de-mergers, acquisitions, delisting, significant management staff changes, and disposals and business expansion are all included.

CONVICTION & PENALITIES

Insider trading investigations by SEBI

In India, the first insider trading case was reported in 1996-1997. Since 1996, there have been a total of 203 insider trading cases recorded, with 185 investigations completed until the end of March 2014. In 2007-2008, 28 investigations were conducted, and in 2010-2011, 28 more insider trading cases were filed. During the years 2008-2009, 2009-2010, and 2013-2014, SEBI's investigations revealed that no cases were resolved.

The Justice Department and the SEC will handle insider trading charges and convictions in the United States. To protect the integrity of the financial markets, they had set criminal and civil charges for insider trading. In a civil insider trading case in 2012, the SEC levied a $13.9 million penalty on Rajat Gupta, an Indian-born former Goldman Sachs director. He was barred from serving on the board of any public firm for the rest of his life. Two years in prison and a $5 million fine were also issued as part of the criminal charges. Cases of insider trading have been investigated by India's capital market regulator, SEBI.

In the futures market segment, SEBI initiated insider trading allegations against Reliance Industries Limited (RILformer)'s arm Reliance Petroleum in 2007. In the insider trading issue, RIL has taken SEBI to the SAT. Individuals and companies in India can settle disputes by paying a penalty without admitting or disputing the alleged wrongdoing, thanks to the SAT's consent settlement provision. SEBI tightened the permission procedure framework in May 2012.

If any person contravenes, attempts to contravene, or abets the contravention of the provisions of this Act or of any rule or regulation made thereunder, he shall be punished with imprisonment for a term not exceeding ten years, or with a fine not exceeding twenty-five crore rupees, or with both, according to the provisions of this Act.

If a person fails to pay the penalty imposed by the adjudicating officer or to follow any of his directions or commands, he must be punished by imprisonment for a period not less than one month but not more than ten years, or by a fine of up to twenty-five crore rupees, or by both.

CONCLUSION & SUGGESTIONS

Insider trading's impact, scope, and impacts vary per country, but any degree of insider trading has a significant impact on a country's reputation. Every shareholder places his money in the market with the expectation of market openness and efficiency."

There are numerous rules and regulations in place to prevent such practises, but they persist. It should be noted that insider trading can be both legal and unlawful, because if insiders are not allowed to invest in the market because they are insiders, their interests will be jeopardised. It should not, however, be made illegal at any moment.

Insider trading jeopardises the capital market's integrity, lowering investor interest and trust because trading on UPSI gives insiders an unfair advantage over other investors. And if they continue to engage in insider trading, they will lose interest in the market, hence insider trading must be dealt with harshly.

Even though SEBI has been dealing with this horrible crime in a professional manner, there are still several gaps in the existing legal structure that allow this threat to flourish. Existing laws must be improved and evolved to better suit the current scenario.

Suggestion:

- The first step in problem solving is to identify the issues at hand. There are a number of initiatives that can be made to address the gaps in the existing legal framework. The first is the dissemination of insider trading training, education, and awareness. The general public cannot be protected if they are unaware of the wrongs that are being perpetrated against them.

- There is a need to extend the application of insider trading laws beyond national borders to protect domestic markets and investors from insider trading committed by foreign nationals.
- SEBI can engage in publishing manuals or booklets and ensuring that it reaches the people who are affected by the offence of insider trading.
- The SEBI Act stipulates a fine of Rs. 25 crore, or three times the profit made, as well as a 10-year prison sentence. However, SEBI's willingness to take on the cases and prosecute them is highly questionable. Some of this is understandable, given how difficult it is to prove insider trading accusations. Even when charges are brought, the cases are frequently resolved through consent orders or the payment of minor fines.