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INSIDER TRADING MECHANISM -ENFORCEMENT ISSUES OF SEBI

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ABSTRACT

Corporations are expected to exhibit the highest standards of professionalism, transparency, and good practices of corporate governance that boost the confidence of the investors dealing in the capital markets. Any attempt to deviate from such standards will not only erode the confidence of the investors but also affect the integrity of the markets. Insider trading refers to the act of trading securities, such as stocks, stock options, and bonds, based on information that is not available to the public.One of the major problems in regulations governing insider trading is the element of proof. It is highly difficult to detect the usage of confidential information, which is the key perspective of this crime.This paper is a conceptual study and focuses on the impact of Insider Trading on stock markets, a case analysis of Insider Trading in National and International scenarios, critically evaluating the role and challenges faced by SEBI in regulating Insider trading and mitigating the issues by adopting PIT amendments. The researcher concludes that despite laws and regulations the insider trading is still prevailing. Implementing stringent laws and effective implementation of PIT regulations is the need of the hour.

Key Words - Insider Trading, UPSI, SEBI, PIT Amendments.

INTRODUCTION

India is one of the fastest-growing economies of Asia needs to have an effective check on its occurrence in financial markets to provide a fair and equal playfield for domestic and international investors if it wants to be in the ranks of major economies of the world.

According to Section 195 of the Companies Act of India 2013, Insider trading is defined as a malpractice wherein trade of a company's securities is undertaken by people who by their work have access to the otherwise non-public information which can be crucial for making investment decisions.

Insider trading is highly discouraged by the Securities and Exchange Board of India to promote fair trading in the market for the benefit of the common investor. It is an unfair practice, wherein the other stockholders are at a great disadvantage due to a lack of important insider non-public information. Any information about the Company is considered as nonpublic information until it is disseminated in a manner calculated to reach the securities marketplace through recognized channels of distribution and public investors. The information which has not been available to the investing public for at least two (2) full business days is considered to be nonpublic.

Review of Literature:

Roopanshi Sachar & Dr. M. Afzal Wani (2017)To ensure compelling execution of insider exchanging laws, at the grass-root level, collaboration from organizations is additionally required. The organizations should rehearse self-guideline and make a prophylactic move in light of the fact that corporate administration is one of the columns on which successful requirement against insider exchanging stands. Steady cautiousness and severe revealing and observing by organizations over their chiefs and officials are the need of the day. Each organization ought to embrace a watertight insider exchanging code its administration structure and guarantee its strictest adherence as their first line of protection to address insider exchanging and the compliance officer should screen the personal trading of employees by best practices and industry guidelines.

M. Anil Kumar (2018) World securities markets have become fundamentally more complex as far as how securities are traded and the diversity of securities traded. The respectability of securities markets is pivotal to the economy of a nation and regulators should uphold laws, denying market abuse to ensure market integrity.

Ako Doffou(2003) Inspite of the appearance of progressively extreme penalties the volume of total insider trading has not been altogether diminished. This leads us to scrutinize the viability of insider trading guidelines.

OBJECTIVES

1. To study and analyze the problem of insider trading and its long-time impact on the securities market of India.
2. To understand the impact of Insider trading through the past proven cases identified by SEBI.
3. To study the Challenges and issues of Insider Trading Regulation in India.

RESEARCH METHODOLOGY

This is a conceptual study based on secondary data. The data has been extracted from various sources like research papers, newspapers, articles, books, authenticated websites, The annual report of SEBI was referred to know and compare their cases. Data included in the working papers of standard universities were also considered for the study.

Impact of Illegal Insider Trading On The Retail Investors

Illegal insider trading not only affects a particular company that trades its stocks on the stock market but also the overall market. It brings negative effects to the conventional markets especially retail investors. Such trading activities destroy the fairness in the market and create artificial demand and supply of stocks which are the focal bottleneck to the well-being of a healthy stock market. Continuous illegal insider trading lessens investors' confidence in the investing mechanism and uncontrolled insider trading could make people withdraw their investment capital, which could eventually impair the economy as a whole.

A group of investors especially institutions accompanied by insiders could attempt to manipulate markets in their favor through disseminating fabricated information about a specific company. They artificially create demand for a specific company' s shares to synthetically fuel the stock price of that company. When the stock price is at its peak, they exit and make a huge profit.

Non-Public information is the key element in Insider trading. It has a huge impact on the investment decision of retail investors. Nonpublic Information include strategic plans;

significant capital investment plans; negotiations concerning acquisitions or dispositions; major new contracts (or the loss of a major contract); other favorable or unfavorable business or financial developments, projections, or prospects; a change in control or a significant change in management; impending securities splits, securities dividends or changes in dividends to be paid; a call of securities for redemption; and, most frequently, financial results.

All these information are not available to the investor through any published sources like annual reports, prospectuses, and other prominent financial publication. Once the actual information is released, the stock price will start to fall. The retail investors, who had no access to such information, hold the shares and become the ultimate loser which is very detrimental to the market.A security's price will rise or fall based on material information. The insider trades affect stock characteristics like price, return and volume and also buy and sell transactions both affect the stock characteristics.

Prominent Cases of Insider Trading in the International scenario:

Martha Stewart

Living Omni Media Inc., a firm having interests in publishing, television, merchandising, electronic commerce, and associated worldwide relationships, was founded and run by Martha Stewart. Martha Stewart was charged with insider trading after selling 4,000 ImClone shares just one day before the company's stock price fell. Ms. Stewart was found guilty of four counts of obstruction of justice and lying to investigators, despite the fact that the securities fraud charges were dropped. She received a five-month prison sentence, followed by five months of home arrest and two years of probation.

Raj Rajaratnam vs US SEC

Raj Rajaratnam, a New York hedge fund manager, was charged with fourteen charges of securities fraud and conspiracy in October 2009, after reportedly cultivating a network of executives at Intel, McKinsey, IBM, and Goldman Sachs. Raj Rajaratnam allegedly made

$60 million in illegal profits from inside information, according to the government's attorney. The conviction of Rajaratnam is part of a bigger post-recession crackdown on insider trading. More aggressive measures, such as wiretapping to prosecute insider trading charges that would otherwise be difficult to prove, have been used in this endeavour to prosecute insider trading.

Cases on Insider Trading regulated by SEBI

BIOCON VS SEBI

Regulator Sebihas restrained an official senior vice president of Biocon from accessing the securities market for three months and also levied a monetary penalty for contravening insider trading norms. The official at Biocon had traded the stocks during the period of unpublished price-sensitive information. The reason for this act was the insider information regarding the collaboration of Biocon with Sandoz which he was accessed to. This senior official violated the PIT norms also failed to make the timely requisite disclosures to Biocon about the sale of shares worth more than 10 lakhs during theperiod of UPSI from December 20, 2017, to January 18, 2018.In addition, it was found that at the time of applying for pre-clearance of trades from a compliance officer, he gave a declaration that he does not have UPSI.

Future Group vs SEBI

For alleged insider trading, SEBI barred Future Group founder Kishore Biyani, his brother Anil Biyani, and Future Corporate Resources Ltd (FCRL) from accessing the securities market. The regulator also restricted the Biyani brothers and FCRL from directly or indirectly purchasing, selling, or trading in FRL shares for two years, as well as imposing a penalty of Rs 1 crore on each of them. The three have also been ordered to "disgorge" Rs 17.78 crores by SEBI

The action was initiated after SEBI discovered that they were trading in Future Retail shares based on unpublished price sensitive information (UPSI) between March 10 and April 20, 2017, in violation of the Prohibition of Insider Trading Regulations, 2015. The case concerns an exchange statement made by FRL on April 20, 2017, which resulted in the demerger of some FRL businesses and had a favourable impact on the company's scrip.

Future Corporate Resources Private Limited (FCRPL), which was part of FRL's promoter group, traded in the company's scrip based on UPSI, according to SEBI. Biyani was the CMD of FRL and the director of FCRPL at the time, and he had access to UPSI.

Rakesh Jhunjhunwala vs SEBI

The Securities and Exchange Board of India (SEBI) has reached an agreement with ace investor Rakesh Jhunjhunwala, his wife Rekha Jhunjhunwala, and eight others accused of irregular trading in Aptech Computers shares. Jhunjhunwala and others were accused by SEBI of trading in Aptech while in possession of unpublished price-sensitive information (UPSI). Aptech announced their entry into the preschool market in September 2016. According to the SEBI order, this was a UPSI between March 14, 2016, and the formal announcement date of September 7, 2016.RakeshJhunjhunwalaAptech Ltd vs SEBI

" Utpal Seth and Rakesh Jhunjhunwala are accused of having the UPSI and communicating it to other applicants, as well as trading in Aptech stock during the UPSI period."

SEBI's Settlement Mechanism incorporates elements of the US SEC's settlement approach. Rakesh Jhunjhunwala has paid a total of $18.5 crore in charges, with roughly $6 crore in disgorgement.

Reliance Industries Ltd vs SEBI

Reliance Industries Ltd (RIL), its chairman and managing director Mukesh Ambani, and two other businesses were fined Rs 70 crore by the Securities and Exchange Board of India (SEBI) on Friday for allegedly manipulative trading in the shares of erstwhile Reliance Petroleum Ltd (RPL) in November 2007.

RIL and Ambani have been fined Rs 25 crore and Rs 15 crore, respectively, by the market regulator. In addition, Mumbai SEZ Ltd has been ordered to pay Rs 10 crore and Navi Mumbai SEZ Pvt Ltd has been ordered to pay Rs 20 crore.For the past 13 years, the RPL case has remained unsolved. RIL had sold 4.1% of its RPL stock. The equity was sold firstin the futures market and then in the spot market to avoid a drop in the RPL share price. The essence of the SEBI notice is that the corporation was informed that shares will be sold in the spot market, hence their sales in the futures market prior to that amounted to insider trading. In 2008, RPL and RIL combined to form RIL.

Furthermore, for one year following the date of the order, RIL was forbidden from dealing in equity derivatives in the F&O area of stock exchanges, directly or indirectly.

Satyam Computer Service Ltd. Vs SEBI

The Securities and Exchange Board of India (Sebi) has fined TAN Murti, the former head of investor relations at Satyam Computer Services Ltd (SCSL), Rs 10 lakh for engaging in insider trading in the company's shares. While the Satyam scandal was exposed in January 2009 after the company's founder B Ramalinga Raju admitted to falsifying the company's books, SCSL was acquired by Tech Mahindra in mid-2009 and integrated with it.

Murti, who was one of the key Satyam officials with advance knowledge of the announcement of the acquisition of Maytas Infra Ltd (MIL) and Maytas Properties Ltd (MPL), traded in SCSL shares in December 2008 while owning unpublished price sensitive information, according to SEBI's investigation into charges of insider trading against him before the scam broke (UPSI).

EVALUATING THE ROLE OF SEBI TO RESTRAIN INSIDER TRADING IN INDIA.

TABLE-1 INSIDER TRADING INVESTIGATIONS BY SEBI

	2010-11	11-12	12-13	13-14	14-15	15-16	16-17	17-18	18-19
Investigations taken up	28	24	11	13	10	12	34	15	70
Investigations Completed	15	21	14	13	15	20	15	06	19

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Sources: SEBI, Annual Reports

An analysis of the data in the above table shows that the number of investigations taken up by SEBI has increased four folds in 2019 compared to the previous year, which is arguably small given the size of India' s capital markets and their liquidity. Moreover, the data relating to ' investigations completedmay not truly reflect SEBI' s track record of success as several of the actions initiated by SEBI over the years including a few high-profile ones,were overturned on appeal. Since the charges of insider trading are mostly based on circumstantial evidence, it is difficult to be detected and proved. Even in cases where it is detected, the rate of successful prosecution has been very low. Despite the presence of a robust regulatory mechanism, SEBI lacks the required technological expertise, which is required to effectively carry out investigations. There has been an acute shortage of resources and manpower. As a result, the rate of successful prosecution is remarkably low. Further, under Indian law, there is no provision to impose a penalty or even ensure investigation on a foreign national who has committed the offense of insider trading. There is no mention of the extra-territorial applicability of the regulations. In this era of globalization of securities trade, this is a huge drawback.

Insider trading lays unnoticed because of the wrongdoers who are highly equipped in hiding it. Recently, the SEBI (Prohibition of Insider trading) (Third Amendment) Regulation 2019 has brought in provision for an informal mechanism to curb inside trading that can provide for effective prosecution. It provides whistle-blowers whose information leads to a disgorgement, a remarkable reward of 1 crore.

Concluding Remarks

With each of these amendments, while SEBI has chalked out additional responsibilities for intermediaries and fiduciaries, as well as streamlined its regulatory powers with stock exchanges, the overall impact on the market hygiene remains to be seen. While there seem to be concernsregarding the degree and extent of control that may be exercised by stock exchanges over unlisted entities, the same will depend on successful implementation of the PIT Amendment and issuance of further clarifications and circulars by SEBI.

As noted above, the requirement of maintaining an enhanced digital database is in line with SEBI' s investigation and surveillance procedure. However, the same may lead to certain operational challenges and issues for the listed company, intermediary or fiduciary, because in addition to maintaining more data for a longer period, the entity is no longer permitted to outsource the task of maintaining the database to a third party. The need of the hour is the continuous adaptation and modification of the present laws to make the practice of insider trading more deterrent so that insiders are prevented from indulging in such trades, thereby securing and augmenting investor confidence in the securities market.

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