

# Amendment to Insider Trading Regulations: An Incentive for Insiders?

By Guest / February 8, 2019 / 5 Min read / Add comment

*[Bhavin Gada, Soumya Shanker and Mehak Gupta are with M/s Economic Laws Practice, Advocates and Solicitors. The views of the authors are personal]*

On 31 December 2018, the Securities and Exchange Board of India (“SEBI”) issued an [amendment](#) to the SEBI (Prohibition of Insider Trading) Regulations, 2015 (“PIT Regulations”). The amendment was pursuant to the recommendations made in the [Committee Report](#) on Fair Market Conduct under the Chairmanship of Dr. T. K. Viswanathan (“Committee”). In this post, we deal with certain issues in the amended PIT Regulations pertaining to communication of information by insiders and off-market transactions between insiders.

## ***Communication of UPSI by an ‘Insider’ and its Implications***

An ‘insider’ is a person who in possession of, or has access to, unpublished price sensitive information (“UPSI”) or is a connected person (as defined under the PIT Regulations). An insider is prohibited from communicating the UPSI to any person except for a legitimate purpose, performance of duties or discharge of obligations.



in the ordinary course of business with partners, collaborators, lenders, customers, suppliers, merchant bankers, legal advisors, auditors, insolvency professionals or other advisors or consultants, provided that such information has not been shared to circumvent the provisions of the PIT Regulations.

The amended PIT Regulations clarify, albeit unnecessarily, that any person in receipt of UPSI pursuant to a legitimate purpose would be considered to be an insider. However, the amended PIT Regulations include a new requirement that such persons must be provided with a notice to keep the UPSI confidential. As this new notice requirement has been ambiguously drafted, it is likely to lead to confusion. For instance, the amendment does not specify the person whose obligation it is to provide such a notice. Depending on one's interpretation of the new provision, the requirement to provide notice appears to have been cast on several people such as: the insider disclosing the UPSI, the listed company to whom the UPSI pertains, or its board of directors or compliance officer.

This lack of clarity may result in such persons taking a defence regarding his or her responsibility to give notice. Since the obligation to issue notice is not clearly cast on any specific person or entity, it may transpire that a recipient of UPSI never receives such a notice. In such a scenario, the recipient would be classified as an insider under the PIT Regulations, but may not be aware of this, or of their obligations in respect of confidentiality and trading as an insider. Under the SEBI Act, 1992, the penalty prescribed for insider trading or communication of UPSI in breach of the PIT Regulations is a fine upto Rs. 25 crore or three times the amount of profits made out of insider trading, whichever is higher. Further, the effect of the burden of proof under the PIT Regulations has always been on the insider to establish his innocence. Therefore, in our view, this inequitable and ambiguous situation created by



Further, the board of directors is required to maintain a digital database with names of persons with whom UPSI has been shared. In order to maintain such a database, the notice of communication of UPSI should be shared with the board of directors by either the disclosing party or receiving party. The amended PIT Regulations do not mandate the requirement for such a notice to be provided to the listed entity. In case of failure to provide notice to the board of directors, they would not be able to comply with this obligation.

Without further clarity from the regulator or the legislature with respect to the notice and the digital database, there are no signposts to help in interpretation of these obligations. Insiders and listed entities may therefore be exposed to enquiries by the regulator with respect to compliance with their obligations under the PIT Regulations.

### ***Off-market Transactions between Insiders***

The spirit of the PIT Regulations is to regulate market abuse, but not to impose a ban on transactions between insiders. Keeping this in mind, the amendment liberalised transactions between insiders with certain checks and balances to avoid market abuse.

Prior to the amendment, off-market transactions between ‘promoters’ in possession of the same UPSI were permitted. Now, such off-market transactions are permitted between ‘insiders’ who would be in possession of the same UPSI. However, such transactions are not permitted when the UPSI is disclosed pursuant to a decision of the board of directors of the listed company in connection with a proposed transaction.

In light of such relaxation under the amendment, let us reflect on an interesting example. An existing insider (such as the promoter or employee of a listed entity) may share UPSI with another person (such as a potential



market price for the benefit of such insiders. It is also pertinent to note that the terms of such 'off-market' transactions are not regulated under SEBI laws and they can be undertaken on such terms and conditions as mutually agreed between the parties.

Such 'off-market' transactions are required to be reported by the insiders to the listed entity within two working days, which would then have to be notified to the stock exchanges by the listed entity. However, the reporting obligation does not specify which particulars of the transaction would have to be disclosed to the stock exchanges. Therefore, the trading insiders may choose to just disclose certain particulars of the transaction, and not all the terms (including the price) thereof.

It appears that the recent amendment to the PIT Regulations may incentivise insiders to undertake transactions resulting in unforeseen consequences.

– *Bhavin Gada, Soumya Shanker & Mehak Gupta*

Insider Trading

SEBI

Securities Regulation



### About the author



Guest