

# Regulatory Hotline

January 23, 2015

## SEBI TIGHTENS ROPE: NEW INSIDER TRADING NORMS INTRODUCED

- SEBI notifies **SEBI (Prohibition of Insider Trading Regulations) 2015**, to be effective from May 15, 2015;
- Definitions of 'Insiders', 'Connected Persons' and 'Unpublished Price Sensitive Information' widened;
- Made applicable to all securities as defined under Securities Contracts (Regulation) Act, 1956 except units of mutual funds;
- Sharing of UPSI in PE/ M&A backed diligences allowed; certain valid defences for insiders introduced;
- Concept of Trading Plans introduced;
- Recommendations made by N.K. Sodhi Committee not taken in totality.

### INTRODUCTION

The Securities and Exchange Board of India ("SEBI") finally notified the SEBI (Prohibition of Insider Trading Regulations) 2015 ("Regulations") on January 15, 2015 replacing the two-decade old insider trading norms in India. The Regulations are based on the recommendations made by an 18 member committee ("Committee") constituted by SEBI under the chairmanship of Justice N.K. Sodhi, former Chief Justice of the High Courts of Kerala and Karnataka, which were approved by the SEBI Board in its meeting held on November 19, 2014 ("Board Meeting"). Please click on this [link](#) for our hotline on the Committee recommendations as well as a comparative study of the draft Regulations vis-a-vis the **SEBI (Prohibition of Insider Trading) Regulations of 1992 ("1992 Regulations")**. Our hotline on the Board Meeting is also available [here](#). Although the Committee recommendations have substantially been incorporated in the Regulations, certain provisions have been left out/amended in the Regulations.

In November, 2014, India's market capitalization crossed USD 1.6 trillion, making it world's ninth largest economy by market capitalization<sup>1</sup>. SEBI has been constantly focussed on developing and regulating the Indian capital market to boost the investors' confidence to maintain this momentum. The 1992 Regulations had considerable inadequacies in terms of their drafting, interpretation and outreach and over time, SEBI had introduced several amendments to certain provisions of the 1992 Regulations to fill in the lacunae. However, a need was felt to systematically review and provide a more robust and efficient mechanism in line with the global norms and standards to curb insider trading in India. Thus, the Regulations are formulated *in order to put in place a framework for prohibition of insider trading in securities and to strengthen the legal framework*.

### SNAPSHOT OF THE REGULATIONS

#### Applicability of the Regulations

The charge of insider trading has been extended to securities listed and proposed to be listed on stock exchanges. This is an expansion from the 1992 Regulations which only applied with respect to companies that were listed. Additionally, the Regulations also strengthen the definition of who an 'insider' is. The scope of 'connected persons' under the Regulations has been widened to include persons associated with the company in a contractual, fiduciary or employment relationship or having direct or indirect access to unpublished price-sensitive information. Further, under the Regulations, the criteria for what constitutes 'unpublished price sensitive information' would be whether the information is 'generally available' or not. The definition of 'unpublished price sensitive information' has been extended to both a company and securities.

#### Notes to interpretation

Every provision under the Regulations is accompanied with specific notes setting out the legislative intent for which that provision has been formulated. As India continues to move from a substance over form approach, these notes will aid in capturing the spirit of the legislation and how the regulatory is likely to look at its enforcement.

#### Prohibition on Insider Trading

Multiple restrictions have been placed i.e. (i) prohibition on communication of unpublished price sensitive information (ii) procurement of unpublished price sensitive information and (iii) trading in securities when in possession of unpublished price sensitive information. The 1992 Regulations prohibited 'dealing' in securities when in possession of unpublished price sensitive information, amongst others; the expression 'dealing' has been replaced with 'trading' in securities. Under the Regulations, the definition of 'trading' has been kept wide. It must be noted that the 1992 Regulations placed no restrictions on the 'procurement' of unpublished price sensitive information by other persons.

#### Exclusions

The Regulations provide for certain exclusions where the charge of insider trading will not get attracted, namely:-

- In the conduct of due diligences: Communication and procurement of information in connection with transactions

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- involving PIPE, mergers and acquisitions, subject to certain conditions;
- For off-market transactions between promoters who are in possession of the same information, and are making a conscious and informed decision;
- In case of non-individual insiders:--
- 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;
- when the trade was executed in the absence of any leakage of information, thereby recognising the concept of 'chinese walls' in large organisations;
- when trades executed in pursuance of trading plans.

### **Rebuttable Presumption**

It is clarified that the presumption against persons deemed to be 'connected' is rebuttable under the Regulations. This provision is akin to the presumption that exists against various persons having a common objective or purpose of acquisition i.e. persons acting in concert under the SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011.

### **Disclosure Obligations**

The disclosure obligations under the Regulations have been limited to 'insiders' and are as follows:

- Initial disclosures of trades to be made by only the promoters, key managerial personnel, directors internally;
- Continual disclosures to be made by every promoter, employee or director in case value of trade exceed monetary threshold of ten lakh rupees over a calendar quarter; company to accordingly notify stock exchanges within 2 trading days;
- Earlier disclosure requirement for persons holding more than 5% shares or voting rights or in case of any further change in their shareholding or voting rights has been done away with.

### **Trading Plans**

Quite a novel concept to India, provisions on 'trading plans' have been introduced whereby every insider is entitled to execute trades in pursuance of pre-determined trading plan in accordance with the Regulations.

### **Compliance Officer**

- Qualification criteria have been set for a compliance officer who shall report to the board of directors of the company or the head of the organization, as the case may be.
- The compliance officer's role in monitoring and approving a trading plan has been made important.
- Enhanced role for the compliance officer who would need to police, monitor and regulate trading by employees and connected persons.

### **Penalties**

No separate penalties have been prescribed under the Regulations. Reference is made however to the penalty provisions under the SEBI Act, 1992 which shall apply. As per the Act, insider trading is punishable with a penalty of INR 250,000,000 (Rupees Two Hundred Fifty Million Only) or 3 times the profit made out of insider trading, whichever is higher. SEBI is also empowered to prohibit an insider from investing in or dealing in securities, declare violative transactions as void, order return of securities so purchased or sold. Any person contravening or attempting to contravene or abetting the contravention of the Act may also be liable to imprisonment for a term which may extend to ten years or with fine which may extend to INR 250,000,000 (Rupees Two Hundred Fifty Million Only) or with both.

The Regulations, also, prescribe certain disciplinary sanctions that may be taken by companies or market intermediaries to require due compliance of the Regulations.

**Please click on this [link](#) for our detailed analysis of the Regulations and a comparison of the Regulations with international laws on the subject matter.**

– Tanya Pahwa, Simone Reis, Nishchal Joshipura & Pratibha Jain

You can direct your queries or comments to the authors

<sup>1</sup> As per article published in Economic Times on November 28, 2014 available [http://articles.economictimes.indiatimes.com/2014-11-28/news/56540612\\_1\\_lakh-crore-investor-wealth-market-cap](http://articles.economictimes.indiatimes.com/2014-11-28/news/56540612_1_lakh-crore-investor-wealth-market-cap)

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