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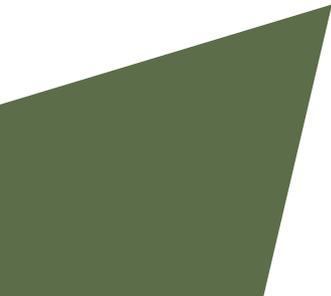
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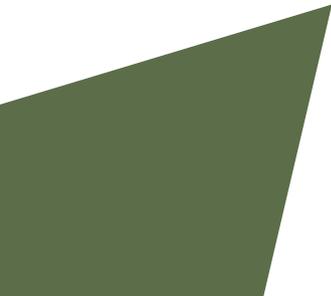
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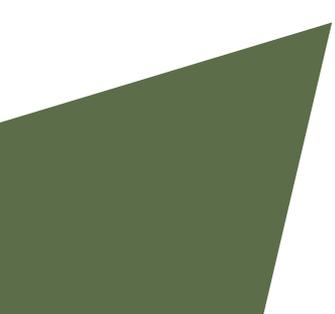
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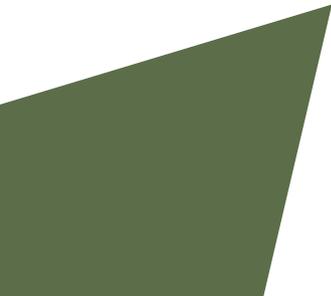
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THE CONCEPT OF INSIDER TRADING-INDIA AND USA

Karishma Singh

CHAPTER 1 - WHAT IS INSIDER TRADING?

Insider trading is a very famous topic which is not only famous in India but also is in many companies in all around the world. But, first we really need to understand what insider really is? So, Insider is a person who is holding more than 10 percent of the voting shares and has access to material non-public information. Even the person who is giving advice on the buying and selling of securities that person will also be called an insider. It is that person who is having the unpublished price-sensitive information. Insider Trading means a person who is an insider who has traded in the securities of a listed company.¹If I make it more comprehensible then in Insider Trading generally a person leaks some information outside the company which can lead to the change in market prices in future. It can be the buying of security also and can be the selling of security also. The person who is involved in it is basically a person who is related to management and knows what are the objectives that the company has in future, means what it is going to do in future.²They can be manager of a company also and can be a director of a company also. They are the ones to whom the non-public information is available which is relating to the security. Now, this concept is not applicable on private companies because in private companies there are no outsiders. So, in this research paper I am going to discuss the concept of insider trading in a more explanatory manner.³

CHAPTER 2 - WHY IS IT ILLEGAL?

Equality is a very important thing but if we explore this concept much deeper then the insiders are getting profit in any way, either the company is in loss or is in profit. The information should be reached towards the people of management at the same point of time. It should not be like that one is having this information from very earlier because in this way that person is surely going to earn profits through the information which has not been published in the public domain.⁴It is totally unfair because about such kinds of information most of the investors are unaware about it and in this way it also lowers their confidence and trust. There is no offence in being an insider but the offence is that if after being an insider you are leaking the unpublished price-sensitive information outside. If I explain it more then one of the best example for insider trading is the news of TATA

¹ <https://www.investopedia.com/terms/i/insidertrading.asp>

² <https://corporatefinanceinstitute.com/resources/knowledge/trading-investing/what-is-insider-trading/>

³ Book by Anita Raghavan - The Billionaire's Apprentice: The Rise of The Indian-American Elite and The Fall of The Galleon Hedge Fund

⁴ Book by Hasan Nejat Seyhun - Investment intelligence from insider trading

and Cyrus Mistry dispute in the year of 2017. This news was basically about Cyrus Mistry, who was removed from the post of chairman in TATA Sons. There were lots of reasons that were predicted but one of the most prominent reason that was apprehended was the dispute of arbitration between TATA and Docomo in which the case was won by Docomo and TATA has to pay 7000 crore rupees to Docomo. And, Cyrus Mistry had also contended that TATA Sons has done the violation of corporate governance. The decision of removing Cyrus Mistry from the post of chairman in TATA Sons was taken after calling an extra ordinary general meeting which has been discussed under section 100 of the Companies Act, 2013. But, the matter were sorted out among them and the matter did not come outside except in media or news because they were very well aware about the concept of insider trading, that it is illegal.⁵

CHAPTER 3 - LAWS ON SWING PROFITS IN U.S.A AND LAWS ON INSIDER TRADING IN INDIA

Well, If we talk about U.S.A then they have made laws on swing profits under section 16 of Securities Exchange Commission Act which talks about swing profits which means that the insiders buy the shares and sells it within 6 months or sell the shares and buys it within 6 months then it will be considered as that they have earned swing profits. Insider trading was first defined in the whole world under section 16 of the Securities Exchange Commission Act which has been passed by the US government or U.S.A. But, it was not defined as insider trading.⁶ It was defined as swing profits. It says that the insiders have earned swing profits through entering into opposite transactions within a period of 6 months. And, this is what in India is called insider trading. Now in India also, there was a committee that has been made in the year of 1940 under P.J Thomas to give details more on insider trading and to stop and put restrictions on insider trading and on the recommendation of the P.J Thomas committee section 307 and section 308 were introduced under Companies Act, 1956. But, in these provisions the insider trading was not prohibited, these provisions said to do the disclosures of the insider trading. According to my point of view, I don't think so it was a suitable provision because in this they are not stopping the insider trading after being well aware of the fact that it is illegal. Here, I can say that there was not a proper making of law because in this way they were actually promoting insider trading among the companies. I think the law was just improvised

⁵ <https://www.wallstreetmojo.com/insider-trading/>

⁶ <https://www.investopedia.com/ask/answers/what-exactly-is-insider-trading/>

without thinking of the repercussions that it will have on the country or the business of several companies.⁷

CHAPTER 4 - SEBI REGULATIONS ON INSIDER TRADING

So, SEBI(Security Exchange Board of India) sorted out a solution to prevent Insider Trading. SEBI has done this on the recommendation of Abid Hussain Committee, Patel Committee and Sachar Committee. Sachar Committee was made in the year of 1979 for the study relating to insider trading. Sachar Committee also given recommendations relating to insider trading to the central government. After the recommendations that were given by Sachar Committee there were lots of improvement happened in the Companies Act.⁸ But, the best recommendations were given by the Abid Hussain Committee which was formed in the year of 1989 and Patel Committee which was formed in the year of 1986 and this actually put a lot of restrictions on the insider trading that were happening even after the introduction of the sections 307 and 308 under Companies Act. Both of these Committees also put this point that there should other laws and regulations for the proper prohibition of insider trading. The Patel Committee also defined the insider trading.⁹ And, by the recommendations of these Committees new regulations were made by SEBI which was the Prohibition of Insider Trading Regulations, 1992 but because of several recent developments SEBI changed the regulations of the Prohibition of Insider Trading Regulations completely and new trading regulations came that was the Prohibition of Insider Trading Regulations, 2015 which was formed on the recommendation of Justice N.K. Sodhi. Patel committee has given the definition of insider in a very limited way. They have shown the scope very less. They says that if the people of management does trade with the shares of the company. So, they kept the definition of insider very limited. After that, Insider Trading Regulation of the year 1992, the scope of insider trading was a bit increased. But, I personally believe that the best definition that has been given for insider includes three things:-

1. The connected persons

⁷ <https://www.investopedia.com/terms/s/shortswingprofitrule.asp>

⁸ https://www.sebi.gov.in/legal/regulations/jul-2019/securities-and-exchange-board-of-india-prohibition-of-insider-trading-second-amendment-regulations-2019_43736.html

⁹ Bhuwadeshwar Mishra - Taxmann's Law Relating to SEBI (Prohibition of Insider Trading) Regulations, 2015 by CA.

2. Deemed to be connected persons.
3. Any person who is in possession of unpublished price sensitive information.

Regulation 3 & 3A mentions the various types of acts that an insider and company are not allowed doing. These regulations does not allow an insider and a company and an insider and to 'deal' in certain circumstances. The term 'deal' has been defined under regulation 2(d) which usually describes dealing in securities to signify an act of buying, selling, subscribing or agreeing to do so by any person either as agent or principle.¹⁰ Regulation 3 does not allow an insider to deal either on behalf of any other person or on his behalf in the company's securities which is listed on a stock exchange when they are having the unpublished price sensitive information. It also does not allow the counseling, communication, procurement of such information either in a directly or indirectly way of writing or is done verbally unless such communication has been made in the ordinary course of employment, business, profession, or under any law.¹¹ Regulation 3A puts an exact prohibition on companies that are dealing in securities of another company or another associate of that company when they are having the unpublished price sensitive information. Thus, Regulation 3B provides that if the company shows that the transaction was actually entered by an officer which was on its behalf, as he did not know about such information. In such kind of situation the company will not be held liable of insider trading.

CHAPTER 5 - HINDUSTAN LEVER LIMITED V. SEBI

This case is one of the most famous cases on Insider Trading in India. In this case, SEBI imposed fine on Hindustan Unilever Limited. Now, it is really very important that about what matter this case was. It is really important to know that what had been done by Hindustan Unilever Limited. Before I describe the facts of the case I would like to tell you that there was a merger happened between Brooke Bond Lipton India Limited and Hindustan Unilever Limited. In this case Hindustan lever Limited had purchased 8 lakh shares from Unit Trust of India (UTI) in the year of 1996, where the

¹⁰ Shailashri Bhaskar (Author) - Prohibition of Insider Trading

¹¹

<http://www.mondaq.com/india/x/830774/Securities/The+Amendments+To+The+SEBI+Prohibition+Of+Insider+Trading+Regulations+2015+Bane+Or+Boon>

target company was Brooke Bond.¹²So, here UTI became the seller. So, what happened was that, two Indian subsidiary companies of Hindustan Lever Limited were merged, means there were two companies from the same group and their merger was happened and one group company had purchased 8 lakh shares from UTI of the different company of the same group. Here the timing of the purchase was in question. The shares that had been purchased, they were purchased two weeks prior. So, two weeks prior the public announcement of the merger of Hindustan Unilever Limited and Brooke Bond Lipton India Limited, these shares were purchased. SEBI got to realize that something does not went well and there is some problem. If we will think it deeply, then the public can also be able to take the benefit of this information. But, SEBI was knowing that, not everyone is having this information. Only the insiders, the top directors, the top executives and along with that the Indian subsidiary companies of them were only having this information of proposed merger, and when there is a proposed merger happens then the assets of the company increases, the turnover of the company increases and with that there are full chances of increase in profits and then there is full possibility that the price of the shares of the company will also increase and here the insiders comes who take the advantage of these things, that before this information will reach to public these shares should be purchased by them so that in future when this information in the form of public announcement will reach to public then the insiders will sell these shares to the public and will earn the profit. And this is what we call as insider trading. Now, lets get back on the case, so after that SEBI had given the investigation order and in the year 1998, SEBI had confirmed that the HLL(Hindustan Lever Limited) has done Insider Trading. HLL is an insider under section 2(e) which is according to the regulation of insider trading. And, it was also said that HLL was having all the unpublished price sensitive information and SEBI also said that there were common directors in both the companies i.e., Hindustan Lever Limited(HLL) and Brooke Bond Lipton India Limited. It was also said that both the companies were under the same control of management.¹³

¹² <https://frontline.thehindu.com/static/html/fl1516/15161070.htm>

¹³ <https://corporate.cyrilamarchandblogs.com/2017/10/insider-trading-hindustan-lever-limited-v-sebi/>