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International Information for International Business

VOLUME 21, NUMBER 2 >>> FEBRUARY 2015

India's New Regulations on Insider Trading

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The Securities and Exchange Board of India ("SEBI") notified the SEBI (Prohibition of Insider Trading Regulations) 2015 ("Regulations") on January 15, 2015, replacing India's two decades old insider trading norms, the SEBI (Prohibition of Insider Trading) Regulations, 1992 ("1992 Regulations"). The Regulations will be effective from May 15, 2015.

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 on November 19, 2014 (*see analysis by Tanya Pahwa, Arun Scaria, Simone Reis and Pratibha Jain, of Nishith Desai Associates, at WSLR, December 2014, page 4*). Although the Committee's recommendations have substantially been incorporated in the Regulations, certain provisions have been left out or amended in the Regulations.

In November 2014, India's market capitalisation exceeded U.S.$1.6 trillion, making it the world's ninth largest economy by market capitalisation, according to an article published in The Economic Times on November 28, 2014 (available at http://articles.economictimes.indiatimes.com/2014-11-28/news/56540612_1_lakh-crore-investor-wealth-market-cap). SEBI has been constantly focussed on developing and regulating the Indian capital market to boost 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 the old regime and provide a more robust and efficient mechanism in line with global norms and standards to curb insider trading in India.

Thus, the Regulations are formulated to put in place a framework for the prohibition of insider trading in securities and to strengthen the legal framework.

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 applied only 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 criterion for what constitutes "unpublished price sensitive information" will be whether the information is "generally available"

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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 by specific notes setting out the legislative intent for which that provision has been formulated. As India continues to move from a form approach to a substance approach, these notes will aid in capturing the spirit of the legislation and how the regulator is likely to view its enforcement.

Prohibition on Insider Trading

Multiple restrictions have been placed, that is, on:

- communication of unpublished price sensitive information;
- procurement of unpublished price sensitive information; and
- 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 broad.

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 be applicable, namely:

- in the conduct of due diligence: communication and procurement of information in connection with transactions involving private investment in public equity ("PIPE") and 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; and
- in the 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; and
  - when trades were 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 only by the promoters, key managerial personnel and directors internally;
- continual disclosures to be made by every promoter, employee or director in case the value of a trade exceeds the monetary threshold of 10 lakh rupees (U.S.$16,667) over a calendar quarter; the company accordingly is to notify stock exchanges within two trading days; and
- the earlier disclosure requirement for persons holding more than 5 percent of the 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 for India, provisions on "trading plans" have been introduced whereby every insider is entitled to execute trades in pursuance of predetermined trading plans 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 organisation, as the case may be.
- The compliance officer's role in monitoring and approving a trading plan has been made important.
- There is an enhanced role for the compliance officer, who will need to police, monitor and regulate trading by employees and connected persons.

Penalties

No separate penalties have been prescribed under the Regulations. However, reference is made to the penalty provisions under the SEBI Act, 1992 ("Act"), which shall apply.

As per the Act, insider trading is publishable with a penalty of INR 250,000,000 (U.S.$4,166,667) or three times the profit made from insider trading, whichever is higher.

   ISSN 1357-0889

SEBI is also empowered to prohibit an insider from investing in or dealing in securities, declare violative transactions to be void, and order the 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 10 years or a fine which may extend to INR 250,000,000 (U.S.$4,166,667) or both.

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

The text of the Regulations is available, in English, at http://www.sebi.gov.in/cms/sebi_data/attachdocs/1421319519608.pdf.

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