



AN INSIGHT ON CHANGES IN INSIDER TRADING REGULATIONS 2014

The year 2014 is going into the history of the Indian Corporate laws as the year of changes. The beginning of the year saw the advent of the Companies Act, 2013 (CA 2013) coming into effect and the midst of it there were changes in the Listing Agreement to align the latter with the CA 2013. In the latter part of the ensuing financial year there were changes in the regulatory frame work for the Non-Banking Financial Banking Companies (NBFC) and ESOP and this has been followed with yesterday's Securities Exchange Board of India (SEBI) board meeting wherein see saw changes have been brought into place.

Through this information document we are analyzing the insider trading, and the key changes brought in such regulations are discussed herein below on the basis of SEBI Press release dated November 19, 2014 and once the entire set of new regulations are out we shall be analyzing and accordingly updating the same in detail in coming days.

Significant changes to Insider Trading Regulations

SEBI had formed a high level committee to review the Insider Trading Regulations, 1992 (IT 92 or the Old Regulations) under the chairmanship of Justice N.K. Sodhi and on the basis of recommendations of Sodhi Committee Insider Trading Regulations, 2014 (IT 14 or the New Regulations) have come into place. The key changes which are contained in the new regulations are as following-

1. Connected Person

Connected person has been defined to mean any person who is or has during the six months prior to the concerned trade been associated with a company in any capacity including by reason of frequent communication with its officers or being in any contractual, fiduciary or employment relationship and includes any person who is a public servant or occupies a statutory position that allows such person access to unpublished price sensitive information relating to the company or is reasonably expected to allow such access. Also now the immediate relatives of connected persons shall be deemed to be connected persons unless such immediate relative can establish absence of access or reasonable expectation of access to unpublished price sensitive information.

This definition now brings into its ambit persons who may not seemingly occupy any position in a company but are in regular touch with the company and its officers and are involved in how the company operates. Thus the intention is to bring within its ambit those who would have access to unpublished price sensitive information about any company or class of companies by virtue of being government servants and occupying official positions that would put them in possession of unpublished price sensitive Information.



Following two examples reflects how wide the definition of Insider Trading is now –

- i. An officer in the government who would know ahead of the market about a proposed policy change that would impact market price say, a proposed change in foreign ownership limit in specific sectors would be a connected person and thereby an insider.
- ii. A judge whose decision in a litigation could have a material bearing on the price of the securities in the market when the judgement is made public, say, a decision on a dispute over whether the offer price for an open offer under the takeover regulations should be higher or lower. All such persons are intended to be “connected persons” and thereby insiders who would be prohibited from trading in securities of the company when in possession of unpublished price sensitive information.

2. Insider

The terms Insider very much crucial in the whole scheme of Insider Trading and under the new regulations the definition is clear. In short the definition within its reach covers any person if they are connected person or are in possession of unpublished price sensitive information (UPSI).

Now the definition has become much wider in its scope and it includes persons connected on the basis of being in any contractual, fiduciary or employment relationship that allows such person access to UPSI. Also the directors, employees and all other persons in the deeming category covered under 1992 regulations would continue to be covered and the term insider shall include also include a person who is in possession or has access to UPSI. Now, immediate relatives will be presumed to be connected persons, with a right to rebut the presumption. In 1992 regulations, definition of connected person was largely position based.

The onus of showing that a certain person was in possession of unpublished price sensitive information at the time of trading would, therefore, be on the person leveling the charge after which the person who has traded when in possession of unpublished price sensitive information may demonstrate that he was not in such possession or that he has not traded or that his trading when in possession of such information was squarely covered by the available defenses.

3. Unpublished Price Sensitive Information (UPSI)

The new definition is very stringent but the same is still linked to information available on a stock exchange platform the committee in its recommendation had suggested to widen the scope of UPSI to other than stock exchange disclosures. Thus, now the UPSI has been defined as information not generally available and which may impact the price. The definition of UPSI has been strengthened by providing a test to identify price sensitive information, aligning it with listing agreement and providing platform of disclosure. Earlier, the definition of price sensitive information had reference to company only; now it has reference to both a company and securities. In others words, the generally available Information will be the information that is accessible to the public on a non-discriminatory platform which would ordinarily be stock exchange platform.

Now specifically the UPSI means any information that is not generally available which upon becoming generally available, is likely to materially affect the price of the securities to which it relates and will ordinarily include information relating to the following: –

- (i) financial results;
- (ii) dividends;
- (iii) change in capital structure;
- (iv) mergers, de-mergers, acquisitions, delistings, disposals and expansion of business and such other



transactions; and
(v) changes in key management personnel

The underlying intention is that the information that is not generally available would be unpublished price sensitive information if it is likely to materially affect the price upon coming into the public domain. Since this will always be a mixed question of fact and law, a bright line indicating the types of matters that would ordinarily give rise to unpublished price sensitive information should be listed to give illustrative guidance about the nature of unpublished price sensitive information when a court has to determine whether any piece of information is unpublished price sensitive information. These listed illustrations are ordinarily in the nature of information that could affect the price upon becoming public and are not exhaustive. Merely because a particular type of event is listed above it should not lead to inexorably being regarded as unpublished price sensitive information regardless of its potential price impact. For example, where a very large company makes a non-material and inconsequential acquisition of a tiny business, or where a company declares the same rate of dividend that it has declared for several years as per publicly stated dividend policy.

4. Third parties and effect on new regulations

Now even the third parties who are connected to a Company have to disclose their trading/holding in the company's securities. Such provision did not exist in the old regulations and was proposed by the Committee as a discretion left to the company, but the SEBI has made it mandatory. Thus it is essential by law that the Companies are required to ask the third party connected persons to disclose their trading and holdings in securities of the company.

This is now an enabling provision which has been enacted wherein the companies are mandatorily required to seek information from those to whom it has to provide unpublished price sensitive information. For example, a listed company may ask that a management consultant who would advise it on corporate strategy and would need to review unpublished price sensitive information, should make disclosures of his trades to the company. It is interesting to keep a watch on the notified regulations as to whether such disclosure will be public or private.

5. Acquisition of UPSI via Due Diligence .

Any law has to be progressive and the new regulations now intends to permit investor access to unpublished price sensitive information via due diligence. The old regulations prohibited communication of UPSI and prohibited trading when in possession of UPSI, it was construed that an investor such as a Private Equity investor or a strategic acquirer could not access any non-public information regarding a company when doing due diligence. However on the recommendations of the committee the SEBI has now allowed access to UPSI for legitimate business transactions ie: when a takeover offer is involved. This provision will make life easier for strategic acquirers. Considering every investor's interest in securities market, advance disclosure of UPSI at least 2 days prior to trading has been made mandatory in case of permitted communication of UPSI.

6. Insider Dealing via Trading Plan

The experience suggest that dealing in shares of the Company has always been an issue which has caused confusion and hazard for the management like CEO,CFO,COO,CS,MD etc. The Committee recommendation has accepted by SEBI and features in the new regulations and are as per international accepted practices. A provision of Trading Plans on the lines of U.S. has been introduced for insiders with necessary safeguards. Such a plan has to be for bona fide transactions and has to be disclosed on stock exchange platform in advance.



The new provision provides an option to such persons who are perpetually in possession of unpublished price sensitive information and enabling them to trade in securities in a compliant manner. Such provision would enable the formulation of a trading plan by an insider to enable him to plan for trades to be executed in future. By doing so, the possession of unpublished price sensitive information when a trade under a trading plan is actually executed would not prohibit the execution of such trades that he had pre-decided even before the unpublished price sensitive information came into being. Trading on the basis of such a trading plan would not grant absolute immunity from bringing proceedings for market abuse. For instance, in the event of manipulative timing of the release of unpublished price sensitive information to ensure that trading under a trading plan becomes lucrative in circumvention of regulation 4 being detected, it would be open to initiate proceedings for alleged breach of SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to the Securities Market) Regulations, 2003.

7. Code of Fair Disclosure and Code of Conduct

The Code of Fair Disclosure mandates every company whose shares are listed on stock exchanges to formulate a stated framework and policy for fair disclosure of events and occurrences that could impact price discovery in the market for its securities. Principles such as equality of access to information, publication of policies such as those on dividend, inorganic growth pursuits, calls and meetings with analysts, publication of transcripts of such calls and meetings, and the like are set out in the schedule. Further the Code of Fair Disclosure and every amendment thereto is required to be promptly reported to the Stock Exchange.

The Code of Conduct on the other hand intends that every company whose securities are listed on stock exchanges and every market intermediary registered with SEBI is mandatorily required to formulate a code of conduct governing trading by its employees. The standards set out in the schedule are required to be addressed by such code of conduct. Also persons other than listed companies and market intermediaries that are required to handle unpublished price sensitive information to formulate a code of conduct governing trading in securities by their employees. Some of these persons may also be regulated by other agencies while some others may themselves be playing the role of regulatory agencies. Even entities that normally operate outside the capital market may handle unpublished price sensitive information. This provision would enable all of them to formulate a code of conduct. The existence of such a code would point to the seriousness with which the organizations treat compliance requirements under these regulations.

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