The Study of Insider Trading in India

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ABSTRACT

In financial markets, "insider trading" refers to trading in securities such as stocks and bonds by corporate insiders who have exclusive information about the issuer of a particular instrument before it is published to the broader public. Insiders can take advantage of this. Profit by buying or selling stocks before they go up or down in price. Insider trading is more than just stealing confidential knowledge. Insider trading involves both rewards and drawbacks, and it is not always evident who are the guilty insiders and who are the sufferers. In recent decades, insider trading has gotten a poor rap. The mainstream media portrays it as a crisis.It is an evil behaviour in which those who indulge in it have no moral principles. However, not all Insider trading is immoral, and some studies have found that only certain types of insider trading are more harmful than others. Trading is actually advantageous to the investment industry as a whole. Some philosophers, lawyers, and economists disagree about whether insider trading should be punished at all, while others believe it should be prohibited in all cases. Both government regulators and academics are paying more attention to financial ethics. This study examines the subject of insider trading, its evolution in India, and the actions taken by the SEBI to combat it.

KEYWORDS:-insider trading, shareholders, price sensitive information, shares, stock market, investors, security, security market, stock exchange, securities exchange board of india act 1992, market players

INTRODUCTION

The institution of stock exchanges is at a crisis due to increased competition brought on by deregulation, technology advancements, and economic processes. Stock exchanges were traditionally run as non-profit organisations, with brokers founding and owning them .Dealers who ran "their" stock exchange as though it were a private club, with rigorous entry requirements newcomers and a regional or even national monopoly, similar to a mediaeval gild. The globalisation of capital markets has resulted in an increase in stock exchange trading volume around the world. and the struggle for trading profits has resulted in a disintermediation similar to that which occurred during the financial crisis. commission prices to be unfixed[1]

Although formal stock exchange activities in India began in 1875, the securities sector was mainly uncontrolled prior to independence. As a result, the focus of securities market reform

[1] History of Stock Exchange in India, available at http://www.yourarticlelibrary.com/stock-exchange/history-of-stockexchange-in-india/23488 last seen on 26/02/2022

has been on improving the markets' operations and efficiency. The Securities and Exchange Board of India was founded under the SEBI Act, 1992, after it was realised that a healthy capital market would be difficult to grow without the presence of strong regulators. The goal was to protect the interests of securities investors, promote the development of, and regulate the securities market, as well as other topics related to or incidental to it.

The first established securities market in India opened in Mumbai in 1875, and it is said to be Asia's oldest. The Ahmedabad Stock Exchange was established in 1894 to promote the stock trading in textile factories in the city. In the1908, the Kolkata Stock Exchange was established to provide a market for plantation and jute mill shares. Two more stock market have set up shop in the area. The National Stock Exchange (NSE) and the Over-the-Counter Exchange of India (OTCEI) were established during the reform era.(OICEI) has been given the task of implementing nation-wide mercantilism.

WHAT IS INSIDER TRADING?

Insider trading is a breach of good faith obligations of officers of a company or related persons as defined under the Securities Exchange Board of India (Prohibition of Insider Trading) Regulations, 1992, to regulate the company's securities on the basis of confidential information concerning the company that is not released or the public is not aware about it (known and unpublished price sensitive information), used to earn profit or avoid loss. It is fairly a breach of fiduciary duties of officers of a company or connected persons[2] By virtue of his employment or other relationship, an insider deals in shares of a corporation to make unjustified gains, rendering the basic principle of fair and free transferability of shares unfulfilled in the equity market. This is the major motivation behind the creation of these regulations, which is to encourage free and fair stock transferability in the capital market, allowing investors to trade securities without fear of being harmed. Insider trading rules and regulations are designed to ensure that no one benefits from trading on "insider" or "unpublished" material, which is details of any transaction of company that is not disclosed to all market players. The vision is to build a fair playing field for all market players by making information available to them. Insider trading laws are enforced, which promotes liquidity in the market and reduces the value of equity

Insider trading rules support the free flow of securities-related information, resulting in more efficient stock pricing. Insider trading restrictions, on the other hand, prohibit insiders from buying or selling based on inside information, resulting in stock prices that are consistent with all accessible information.

DEVELOVEMENT OF INSIDER TRADING REGULATIONS IN INDIA

Insider trading was only officially recognised as a bad behaviour for the first time in the late 1970's. Following a succession of committee recommendations recommending strict oversight, and a regulatory authority was established in 1992.

[2] Bhattacharyya Utpal and Daouk Hazem, “*The World Price of Insider Trading*”,vol no.54 Journal of Finance, pp- 75- 108, 2002

a. **Sachar committee** The Strong Expert Committee on Companies and Monopolies and the Restrictive Trade Practices Act (MRTP) (Sachar Committee) was established in June 1977 to study the Companies Act of 1956 and the MRTP Act of 1969.[3] the Sachar Committee's report was submitted. The Committee issued two recommendations: one, complete exposure of transactions by the person who have made price sensitive information, while the other, restriction of transactions by that persons. A company director, statutory auditor, accountant, tax and management consultant or advisor, and legal advisor, among others, may engage in such actions as insiders. All public firms are required to keep a record of all transactions in the company's equity by the following individuals, plus their spouses and dependants, as well as those who are employed full-time by the company and earn a monthly income of three thousand rupees or more.

b. **Patel Committee (1987):** In May 1984, the Indian government created a Strong Committee (Patel Committee) to conduct a complete evaluation of the functioning of securities exchange and give suggestions. The committee's final report expressed grave concern about the lack of particular regulation in India to prevent the misuse of insider knowledge and advocated harsh penalties for insider trading. Insider trading is common in the country's stock exchanges, according to the research, and is one of the main causes of extreme derivative trading.[4]

c. **Abid Hussein Committee (1989)**: In 1989, the Working Group on 'Capital Market Development,' also called as the Abid Hussein Committee, was established. Insider trading must be deemed a significant offence penalised by civil and criminal sanctions, according to the alliance. Insider trading and covert acquisition bids are issues that may be largely addressed by suitable regulatory frameworks. It was recommended that the SEBI be tasked with drafting the appropriate legislation and being given the ability to enforce it.

Insider trading does not provide a greater benefit to the corporation than other forms of compensation. With unrestricted insider trading as a form of compensation, investors are unable to predict how much they will pay for management services or take cost-effective decisions about how to run the company. Insider trading can be classed according to its legality. There are various beliefs that insider trading is unlawful and unequal. Insider trading has been defended by certain economists and legal scholars. However, the current focus of our efforts is on unlawful insider trading.

ROLE OF SEBI IN REGULATING THE INSIDER TRADING

The function of a stock market regulatory organisation in a state is defined by the level of growth of that nation's stock market. With respect to the growing character of the indian market, the regulatory authority must inevitably play both developmental and supervisory roles.

Rajat Gupta, who is accused of insider trading in the America , will have to prove whether or not he profited financially from his actions at his prosecution in the America. The important

[3] Committee on insider trading, *Sachar Committee Recommendations*, No-18.104 (iv)
[4] Committee on insider trading *Patel Committee Recommendations*, No-7.26

element to remember is that Gupta was prosecuted. This had far-reaching repercussions for India's stance to insider trading regulation.[5]

Regulations and developmental roles are inextricably intertwined and share nearly identical goals. In most cases, well-regulated structures result in speedy and efficient growth. The Securities and Exchange Board of India (SEBI) is a statutory organisation that works with in the limits of Securities and Exchange Board of India Act 1992. Section 11 of the SEBI Act discusses the SEBI's powers and functions. The SEBI's duty is to safeguard shareholders' interests and regulate. Controlling the insider trading is one of the SEBI's most essential regulatory frameworks in the securities exchange.[6] Before conducting an investigation, the Board must provide proper notice to the insider. Any member, director, partner, proprietor, or employee of the insider or other people' files, accounts, papers, and digital information, as well as any significant statements, could be examined by the investigative body.

REMEDY FOR INVESTORS

More frequently than not, the insider is exonerated of all charges. Even if they are found guilty, they are required to pay a sum of money that is far less than the amount of gains they might have earned, or they are prohibited from dealing in securities for a length of time specified in the order. As a result, the insider is satisfied with the gains he is ultimately left with.

The first stage in providing compensation to shareholders is to ascertain the number of shareholders who have been wronged and to assess how much money they have lost as a result of insider trading. After convicting an individual of insider trading and telling him to pay the penalty imposed as a result of his offence, it is recommended that a public notice be issued for a set period of time, asking aggrieved investors to demand compensation for losses they may have suffered as a result of the insider's biased trading activity. Compensation would be provided from the money obtained from the charged person. If the investors do not acknowledge the warning, they would lose their right to seek repayment. Following the determination of the count of shareholders, SEBI must compute and establish the amount of cash that each investor will require independently. Calculating this number can be time-consuming, but it is quite useful.

CONCLUSION

As previously stated, India's insider trading restricts dealing, discussing, or guiding on insider trading affairs. Insider trading is a crime that is committed when these laws are broken. SEBI has the authority to bring criminal charges under section 24 of the SEBI Act 1992. Insider trading was not specifically addressed in the Indian Companies Act or the Income Tax Act.

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[5] , “Is India too soft on insider traders?” available at https://economictimes.indiatimes.com/slideshows/economy/is-india-too-soft-on-insider- traders/insider-tradingis-a-criminal-offence/slideshow/11066581.cms last seen on26/02/1995

[6] Section 11(g) of the SEBI Act 1992

The committees above given also suggested certain regulation to prohibit the insider trading. Following the adoption of the SEBI Act in 1992, SEBI drafted insider trading restrictions known as the SEBI (Insider Trading) Regulations. By amending the anti-insider trading regulations in 2002, the SEBI has reinforced the laws.

After conducting extensive research into insider trading, m finding is that no matter what laws or processes are established by regulatory agencies to preserve price-sensitive knowledge and prohibit insider trading, the scenario will never be flawless. The reason is critical for the efficient execution of a company's or firm's business that specific personnel have access to price confidential material and other trade information that are not publicly revealed. And it is the job and responsibility of these individuals to guarantee that this information is not disclosed or exploited for personal gain.

To combat insider trading and protect confidential material, those in positions of power, such as directors, officials, and other corporate members, must take responsible efforts and create high values of ethics.