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## Insider Trading Laws - Problems and its solution in comparison with US & UK

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*Legislature Insider Trading Regulation is not a very old thing in India because the country has still been progressing and its regulations are always changing. India now adheres to the SEBI (Insider Trading Regulation) of 2015. Countries like the United States of America have had these rules for a long time, and as a result of the United States of America's securities, various other countries tried to follow the same methodology and enacted Insider Regulations in their own countries. Corporations in India are also permitted to enact their own Insider Trading Regulations, which must be consistent with the Insider Trading Regulation Act. And by looking at all of these circumstances, it became clear that they needed to be examined and analyzed. This research compares and contrasts the Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015, and the United States of America's Insider Trading Legislation. It also covers the difficulties and obstacles with implementing Insider restrictions in India, as well as possible alternatives through the US as well as UK legislation.*

**Keywords:** *insider trading, SEBI, India.*

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## INTRODUCTION

**Stock market** - A stock market is a public market that facilitates the purchase, sale, and issuance of publicly traded firm stock. It's a framework that includes dealing in financial products easier by involving participants in the process. The stock market serves a dual purpose, which is reflected in the legislative structure that governs the market.<sup>1</sup>

**Insider trading** - Insider trading can be defined as the intentional use of unreleased data or information having an impact on the prices, acquired through or from a fortunate connection to earn a profit (or avoid a loss) at the expenditure of the innocent participants when the premium of the financial products would be drastically affected if the information has been revealed. In straightforward terminology, Insider trading may be described as trading done by any individual who currently has or can gain the access to some relevant data that is not known to the public in general, and on the premise of that knowledge, he seeks to generate profit for himself. The SEBI Act, 1992 didn't clearly define what exactly does the term Insider Trading means, rather it has defined the terms Insider and Price Sensitive Information.

**Insider** - "Insider" is simply defined as a person who is connected or in possession of or having access to some relevant data or information which has a huge impact on prices and is not released in public.<sup>2</sup>

**Unpublished price sensitive information** - It refers to any non-public corporate data or information about the corporation or its financial products that, when made public, has the potential to substantively influence the valuation of the financial products. It typically includes but is not limited to, earnings reports, dividend income, working capital changes, consolidations, de-mergers, and procurements.<sup>3</sup>

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<sup>1</sup> Soumya Jain, 'Laws Governing the Stock Market in India' (*Ipleaders*, 27 September 2021) <<https://blog.ipleaders.in/laws-governing-the-stock-market-in-india/>> accessed 02 January, 2022

<sup>2</sup> SEBI (Prohibition of Insider Trading) Regulation, 2015, Reg 2(1)(g)

<sup>3</sup> SEBI (Prohibition of Insider Trading) Regulation, 2015, Reg 2(1)(l)

## KINDS OF INSIDER TRADING LEGISLATION IN DIFFERENT COUNTRIES

### 1) India

**SEBI Act, 1992 and 2015 Regulations** - "Insider" refers to somebody who is either a connected individual or has undisclosed value-conscious- conscious knowledge in their possession or accessibility. As a result, it encompasses those who are linked because of a commercial, financial, or employment connection that gives them access to "unreported price-sensitive information" ("UPSI"). UPSI is defined as a document that is not widely available and has the potential to influence pricing. This definition includes a criterion for identifying price-sensitive information and also a framework for the release of that information.<sup>4</sup>

**The Companies Act, 2013** - "Insider trading" is defined by the Act as "any conduct of adhering, buying, selling, trying to deal, or consenting to buy, sell, or deal in any financial products by any board member, competent authority, or other corporate entity, whether as principal or agent, if he is normally assumed to have direct exposure to any non-public price-sensitive information in regard of the shares of a company."<sup>5</sup>

### 2) The US

Intended to assist the SEC, the US courts have recognized the necessary legislation about insider trading, as shown below:

**The Classical or Disclose or Abstain theory** - Before making a transaction, the insider should reveal their UPSI to the marketplace or they should refrain from making any trade at all. This theory can be applied to executives, authorities, workers, and other people who are related or connected to them.

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<sup>4</sup> Nishith Desai, 'Indias SEBI Approves New Regulations on Insider Trading' (*Bloomberg Law*, 6 December 2014) <<https://news.bloomberglaw.com/securities-law/indias-sebi-approves-new-regulations-on-insider-trading-delisting-listing-obligations-and-disclosure-requirements>> accessed 02 January 2022

<sup>5</sup> Kirithana Singh, 'Insider Trading laws in India in comparison with the laws in US and UK' (*Legal Service India*) <<http://www.legalservicesindia.com/article/2567/Insider-Trading-laws-in-India-in-comparison-with-the-laws-in-US-and-UK.pdf>> accessed 02 January 2022

**The Misappropriation theory** – In this theory the hypothesis is intended to defend the credibility of financial markets from individuals with access to UPSI who may have an impact on the security and compliance valuation if exposed, but who generally owe no financial or any other obligation to the people who have bought the shares of the company. In contrast to Indian legislations, which are frequently criticized for being inefficient, lax, and poorly implemented, US rules and regulations are far more strict.

### 3) The UK

The UK's insider trading legislation is governed by the Financial Services and Markets Act of 2000 ("FSMA") and the Criminal Justice Act of 1993 ("CJA"). The FSMA establishes various guidelines for avoiding market exploitation and allows the UK Financial Services Authority ("FSA") to penalize those who do so. Market manipulation is defined as any behavior in which an insider trades, or seeks to make a deal, in a qualified investment or connected investment on the premise of insider knowledge relevant to the investment in the issue, according to Section 116(2) of the FSMA.

Trading in valuation instruments on the premise of insider knowledge, encouraging another individual to trade in price-affected instruments based on privileged information, and intentional revelation of unreleased personal data to someone else, are all prohibited under the CJA. Insider trading and price manipulation may result in prison terms of up to eight years or more and infinite fines. The terms 'price-sensitive knowledge' and 'insider' are defined similarly under Indian and British statutes. Both criminal and civil culpability are dealt with under one common legislation in India, whereas both responsibilities are dealt with under separate legislation in the United Kingdom. <sup>6</sup>

### WHERE THE INSIDER TRADING LAWS LACK

**1) Lack of Skilled Manpower** - SEBI's successful authorization actions can have the dual effect of penalizing the wrongdoers on the one hand, and creating a major impediment on the other.

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<sup>6</sup> Naom Noaked, 'Differences Between the US and UK Market Abuse Regimes' (*Harvard Law School Forum on Corporate Governance*, 7 April 2012) <<http://blogs.law.harvard.edu/corpgov/2012/04/07/differences-between-us-and-uk-market-abuse-regimes/>> accessed 03 January 2022

However, for such impediment effects to be realized in India, SEBI should prepare themselves so that it can deftly gather evidence with the purpose of "examine to contest." SEBI will need to assemble a team of data scientists, mathematicians, legal educators with experience in incorporation law, programming architects, and academics. People demand a high level of study in their specialized fields as well as a broad range of abilities across all reasonable topics. SEBI could also develop its market learning by a consistent review of measurable research and feedback from middle-person advisors.<sup>7</sup>

**2) Lack of Anticipatory Action** - SEBI has the authority to investigate the SEBI Act only where a mediator or other person who is associated with the financial market has disobeyed any of the provisions of the Act or the Rules and Regulations adopted by the Board, or the directives issued by the Board. Nevertheless, there may come a time when SEBI becomes more aware of a handful of anticipated instances of insider trading through a whistleblower and attempts to keep up a key separation from all of this.<sup>8</sup>

**3) No Application Outside the Territory of India** - Because of the globalization of international economies, the globe has become a global city, and insider trading has started to spread beyond geographical boundaries. The Indian legislation is inverted in this way because it requires administration outside of India, i.e. intraregional administration. The primary goals of transboundary application of national legislation have been to protect local marketplaces and domestic shareholders' rights against foreign players' actions. There is no provision in Indian law to impose penalties or even follow up on an outside citizen who has committed the insider trading violation. As the SEBI Act will not apply to domains beyond India, and it will generate appropriate use of this Act, there is no mention in the Legislation about the registration of criminal affirmation against executives of local organizations proactive in residential trade who have engaged in insider trading.<sup>9</sup>

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<sup>7</sup> 'Report of the Committee on Corporate Governance' (SEBI.gov, 5 October 2017)  
<[https://www.sebi.gov.in/reports/reports/oct-2017/report-of-the-committee-on-corporate-governance\\_36177.html](https://www.sebi.gov.in/reports/reports/oct-2017/report-of-the-committee-on-corporate-governance_36177.html)> accessed 03 January 2022

<sup>8</sup> Securities and Exchange Board of India Act, 1992, s 12C

<sup>9</sup> Amir Kumar Pathak, 'How to Tackle Insider Trading in India: An analysis of current law and regulation through judicial decision' (Corporate Law Reporter, 28 March 2012)

**4) Power to Tap Phone Calls** - Because SEBI lacks fundamental investigation capabilities, current regulations are unable to have a strong impact on insider trading malfeasance, resulting in little punishment. This is exemplified by the fact that SEBI was only given the authority to request phone data records in 2014, and it still lacks the authority to tap phone records, as suggested by the Vishwanathan panel. Other governments, such as the United States, rely on the ability to wiretap phone calls to acquire evidence against insider trading suspicions for investigative purposes and their successful prosecution. SEBI was deprived of this power due to alleged "misuse." Wiretapping draws its power from the Indian Telegraph Act of 1885. The Securities and Exchange Commission (SEC) of the United States, on the other hand, obtained significant information by eavesdropping on Raj Rajaratnam and Rajat Gupta's talks, which resulted in their imprisonment.<sup>10</sup>

## EFFECTIVENESS OF INSIDER TRADING LAWS

The supervision of insider trading has proven to be the most challenging of the key concerns that SEBI must address. The unpleasant moniker of "the unwinnable fight" has been applied to such legislation, prompting a rethinking of the subject. According to the SEBI's Annual Report for 2016-2017<sup>11</sup>, Insider trading accounted for 14% (34 cases) of SEBI's investigations in 2016-2017, compared to only 10% (10 instances) the previous year. Insider trading is common, and it's getting worse every year. In addition, only 16 of the 35 cases that were investigated were finished. As a result, it is a cause for considerable worry. Insider trading allegations are harder to identify and prosecute since they are primarily dependent on corroborating evidence. Even when it is discovered, the probability of successful prosecution is extremely less. Despite the existence of a strong legislative structure, SEBI lacks the technological capabilities necessary to conduct efficient investigations. There has been a severe scarcity of resources and personnel. As a result, the achievement rate of the indictment is extremely less.

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<<http://corporatelawreporter.com/2012/03/28/tackle-insider-trading-india-analysis-current-laws-regulations-judicial-decisions/>> accessed 03 January 2022

<sup>10</sup> Bhavya Bhandari, 'Why SEBI is failing regulating insider trading in india' (*India Corp Law*, 20 February 2018) <<https://indiacorplaw.in/2018/02/sebi-failing-regulating-insider-trading-india.html>> accessed January 6, 2022

<sup>11</sup> 'SEBI's Annual Report for 2016-2017' (*SEBI.gov*, 14 August 2017) <[https://www.sebi.gov.in/reports/annual-reports/aug-2017/annual-report-2016-17\\_35618.html](https://www.sebi.gov.in/reports/annual-reports/aug-2017/annual-report-2016-17_35618.html)> accessed 03 January 2022

## COMPARATIVE ANALYSIS OF INSIDER TRADING REGIMES IN INDIA, US, AND UK

**1) Criminal and Civil Liability** - In the perspective of the statutory application, India and the United States have similar laws, with the same legislation being inapplicable to both criminal and civil responsibility, however, the position in the United Kingdom is somewhat different. The Indian Insider Regulation primarily applies to publicly traded firms; however, this type of criterion is not followed in the other two nations. In India, any individual is considered a "related person" if they were in any way associated with the corporation ten months before the occurrence, although this is not the case in the United Kingdom.<sup>12</sup>

**2) Surveillance System** - To capture anyone who has engaged in insider trading, contemporary and technical advancements, as well as a stronger monitoring system, is required. In contrast to India, the SEC and stock exchanges in the United States have a highly effective surveillance mechanism. SEBI does not have a lot of technical know-how in this domain. Even though both the SEC and the SEBI have computerized monitoring systems, the SEC has a far superior alternative, giving them an advantage over the others.

**3) Similarity with the Foreign Laws** - Globalisation has brought the globe closer together, and with it, the link of the wrongdoing has also spread to other nations. If a foreign citizen commits a crime, Indian courts do not have the authority to investigate or punish him. In foreign territory, Indian laws are not applied extraterritorially. However, industrialized nations, such as the United States, have a language in their regulations that allows for extraterritorial applicability. However, in certain situations, investigations have been launched in other nations. This occurred as a result of bilateral agreements between India and the United States, including the Mutual Legal Assistance Treaty and various Memorandum of Understandings. However, this is of little utility because it does not encompass the majority of countries.<sup>13</sup>

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<sup>12</sup> Kirthana Singh (n 6)

<sup>13</sup> RupanshiSashar & Dr. M. Azfal Vani, 'Regulation Of Insider Trading In India: Dissecting The Difficulties And Solutions Ahead' (*Jcil*, 2019) <<https://jcil.lsyndicate.com/wp-content/uploads/2017/01/Roopanshi-Dr.-Afzal.pdf>> accessed 03 January 2022

## WAY FORWARD

The absence of a robust investigation procedure is one of the legislation's fundamental flaws since many cases involving insider trading are not adequately evaluated as a result. Many offenders evade the law or receive light sentences due to a lack of a suitable investigative procedure and factual verification. This, in turn, encourages the criminal activity of insider trading because these gaps may now be exploited. As a result, the investigation mechanisms used in insider trading instances can be strengthened by the following –

- 1) Extending the number of workers or regulators designated by SEBI to supervise the operations of listed firms to the point where there is enough personnel to supervise each organization separately, as opposed to the current situation where one person is responsible for all publicly-traded company interactions. That is one company's personnel or supervisor.
- 2) Because investigators in other nations were able to intercept phone conversations of potential insider traders, many insider trading instances were managed to be identified. For instance, in the case of Securities Exchange Commission versus Rajat Gupta and Raj Rajaratnam, the whole scenario was brought to the forefront as a consequence of the SEC's wiretapping of Rajat Gupta's phone calls, which were then used as evidence against him. As a result, it would make SEBI's work a lot simpler if they were also involved in a similar practice, which is tapping suspected persons' calls to keep an eye on their questionable behavior.<sup>14</sup>
- 3) The SEBI Act of 1992, Section 11B(3), which enables the SEBI to conduct investigations, expressly restricts its authority by naming certain members from whom help for the case might be obtained. As a result, the scope of this clause might be expanded significantly so that SEBI can complete its inquiry without delay.
- 4) Foreign nationals who engage in insider trading activities will not be penalized because the Regulation makes no mention of it. As a result, it's a good idea to add clauses that make it

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<sup>14</sup> Abhirami B & Arya Kirtan, 'Insider Trading Laws in India- Pertinence and Problem' (*The Law Brigade*, 2020) <<https://thelawbrigade.com/wp-content/uploads/2019/05/Abhirami-Arya.pdf>> accessed 04 January 2022

illegal for foreign corporations registered on Indian stock exchanges to engage in such unlawful activities.

5) Every insider trading case should have a fixed time limit so that the matter does not go on further than required, diluting the situation's gravity.<sup>15</sup>

## CONCLUSION

The financial sector is critical for capitalist countries' progress, advancement, and resilience, and the strength of the financial market determines an economy's development. As a result, it's important to look into the many financial market's legislation and rules. The need of the hour is for the current regulations to be continuously adapted and modified so that they can make insider dealing more difficult, preventing insiders from engaging in such transactions and ensuring and enhancing investor trust in the financial market. Insider trading is not only illegal, but it is also unethical and immoral. It also goes against the reasonable market idea. Insiders have access to information that provides them a competitive advantage over other market participants, allowing them to profit from the financial markets. Insiders violate the fiduciary obligation by betraying the confidence of the shareholders of the company, buyers, and employees. The current Insider Trading Legislation of India, 2015, does not address all of the legal issues raised in the paper, such as the necessity for precautionary measures, a stronger monitoring system, and the implementation of this regulation in other countries, among others. As we previously noted, the United States' Insider Trading Regime has a wide range of authorities and a far superior monitoring apparatus to deal with the complicated challenges of insider trading.

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<sup>15</sup> Pranav Sharaswat, 'Elements of Effective Insider Trading Regulations: A Comparative Analysis of India and U.S.A' (SSRN, 6 July 2021) <[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3870326](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3870326)> accessed 06 January 2022