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Shruti Vora *v* Securities and Exchange Board of India: Analysing the India's Insider Trading Regime

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The decision delivered by the SAT in the famous WhatsApp Leaks case currently stands as one holding precedential value for adjudicating future disputes. However, this paper significantly highlights the dangerous implication of this verdict on India's insider trading regime. It is argued that the Court substantially contradicted the legislative intent of the provisions of the SEBI (PIT Regulations) of 2015. Simultaneously, it is to be noted that the Court's creation of a caveat of a knowledge requirement in insider trading is self-made and without any substances and as such an overreach of its powers.

Keywords: *insider trading, SAT, knowledge, innocent tippee, legislative intent.*

INTRODUCTION

The Securities and Appellate Tribunal [the "**SAT**"] on 22 March 2021, in the case of ShrutiVora ("**Appellant**") vs Securities and Exchange Board of India[1] ("**SEBI**"), [this "**Case**"] delivered its judgement adjudicating on the legal question of whether the circulation of a "forwarded as received" message on a Whatsapp group concerning the financial results of a Company, before

[1] *Shruti Vora v SEBI* (2020) Appeal (L) No. 28/2020

said results were disclosed in the public domain, would constitute unpublished price sensitive information[2] ("**UPSI**") under the provisions of Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015.[3] ("**PIT Regulations**") This has come to be one of the significant judgements from Indian Courts that address the relevance of the requirement of knowledge, that the information received was actually UPSI, while determining the liability of the accused. The present case comment begins with a brief narration of the position of India's insider trading regime on the question of inclusion of men's rea, with help from statutes and case laws. The second part provides an analysis of the potential implications of how the SAT dealt with the question of the element of knowledge while determining the liability of the Appellant. Finally, the third and final part argues that while the holding of the present case nudges toward the development of an innocent tippee defence within the PIT Regulations, it is inconsistent with India's current insider trading laws in the status-quo.

UNDERSTANDING THE DEVELOPMENT OF INDIA'S INSIDER TRADING REGIME: WHERE DOES KNOWLEDGE FIT?

India possesses one of the strictest regimes worldwide when it comes to the area of insider trading, with India's capital markets regulator, the SEBI, taking the forefront in governing the same.[4] Post, the 2008 Amendment to the SEBI (Insider Trading) 1992 Regulations[5], the definition of insider was amended to include any person who has received or has had access to UPSI.[6] This was done by adopting the "parity of information doctrine."[7]Currently, the provisions relating to insider trading are largely contained in the PIT Regulations, which have undergone several amendments.[8]

[2] SEBI (Prohibition of Insider Trading) Regulations, 2015, Reg. 2(1)(n)
[3] Shruti Vora (n 1)
[4] Varottil, Umakanth, Due Diligence in Share Acquisitions: Navigating the Insider Trading Regime' (2017) (1) Journal of Business Law, 2017 <https://ssrn.com/abstract=2759771> accessed 25 June 2022
[5] SEBI (Prohibition of Insider Trading) (Amendment) Regulations, 2008, Reg. 2(e)
[6] *Ibid*
[7] Varottil, Umakanth (n 4)
[8] SEBI (Prohibition of Insider Trading) Regulations, 2015, Reg. 2(1) (g)

One can better understand the relevance of the holding in this case by first understanding the general consensus of Indian Courts on the consideration of any sort of mental element/state of mind (generally men's rea) while adjudicating insider trading disputes.[9] Interestingly, the SAT in the landmark verdict delivered in the case *of Rakesh Agarwal v SEBI*[10]emphasized that the motive/intention of the accused must be taken into cognizance for the purposes of ascertaining liability even though the SEBI Regulations do not mandate this.[11] However, the verdict of the Hon'ble Bombay High Court in *SEBI v Cabot International Capital Corporation* [12]took us back to the conventional practice of not including men's rea by opining that penalties for insider trading under the SEBI Act as well as SEBI Regulations are not for a criminal offence (thereby not requiring men's rea) but rather non-observance of a statutory obligation or breach of a civil obligation.[13] This view was further supplemented by the holding of the Supreme Court of India ("SCI") in *SEBI v Shriram Mutual Fund*[14] wherein they observed that the "penalty is attracted as soon as the contravention of the statutory obligation as contemplated by the SEBI Act and the Regulation is established and hence the intention of the parties committing such violation becomes wholly irrelevant."[15]In light of the aforementioned judgements, the reasoning of the SAT in Rakesh Aggarwal can be said to have been impliedly overruled.[16] To summarize the jurisprudence of Indian courts on the question of consideration of men's rea, we can adequately conclude that an individual would be liable for the offence of insider trading by merely being in possession of UPSI, even accidentally or without knowledge of the same.

[9] *Ibid*
[10] *Rakesh Agarwal v SEBI* (2004) 49 SCL 351 (SAT)
[11] *Ibid*
[12] *SEBI v Cabot International Capital Corporation* (2004) 51 SCL 307 (BOM)
[13] *Ibid*
[14] *SEBI v Shriram Mutual Fund* (2006), AIR 2287
[15] *Ibid*
[16] Mehta, Rahul, 'The Redundant Nature of Prevalent Insider Trading Laws' (2021) 1 (1) (July 12, 2021). Indian Journal of Corporate Law and Policy, 97-106 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3884828> accessed 20 June 2022

AN ILLUSTRATION OF OVER EXCEEDING POWERS: ANALYSING THE SAT'S FLAWED JUDGMENT

In the aforementioned context, it is pertinent to understand how the SAT concluded its judgement. The following observations with respect to this conclusion are made:

No Mention of Precedents in the Judgment: At the outset, reference shall be made to the infamous statement made by Justice Holmes proclaiming that "great cases, like hard cases, make bad law." It is astounding to note that there has been no substantial mention of precedents within the judgement generally and absolutely nothing with respect to knowledge requirement. It is submitted that this illustrates that the SAT did not really have a basis for making its conclusion as is visible from the precedents that have been discussed above.

Highlighting the Relevance of the N.K Sodhi Committee Report: It is submitted that the SAT could have made a reference to the Report in order to enhance the authenticity of its reasoning. This is because the contents of this Report could practically be the only basis under the Indian legal framework for insider trading that would have aided the SAT: (a) The Report defines insider trading as not only a civil wrong but also a crime.[17] This could possibly have been used to tackle the judgement given by the Supreme Court stating that a charge of insider trading is a breach of a statutory obligation (a civil offence) as opposed to a crime.[18] As such, the element of mens rea in the form of knowledge could have been adequately relied upon by the SAT by making reference to said definition; (b) As per the Proposed Regulations on insider trading put forth in the Report, they advocated for the inclusion of an innocent tippee defence under Proposed Regulation 4(3)(ii).[19] This defence clearly indicates having a knowledge requirement. In fact, in the case of re Manappuram Finance Ltd, the SEBI made reference to this Report to hold that "the accused was not in a position to know that the information that was distributed in the research report or discussed in the conference call or being covered by media was UPSI.[20] As such, this holding can be co-related to the fact that they did not have knowledge

[17] SEBI Act, 1992, s 24(1)
[18] SEBI (n 14)
[19] *Ibid*
[20] *Ibid*

that it was not UPSI and thus were innocent tippees. However, it is significant to note that the current PIT Regulations do not include such a defence. Although the accused has a chance to prove their innocence as provided under Regulation 4, the Note to Regulation 4 clearly mentions that "when a person who has traded in securities has been in possession of UPSI, his trades would be presumed to have been motivated by the knowledge and awareness of such information in his possession;"[21]and c) Through its judgement, it is noticed that the SAT has placed the burden of proof on the SEBIto prove the state of mind (having knowledge) of the accused. However, it is submitted that this is not in consonance with the proposals of the Report and PIT Regulations. Therefore, it is argued that though the Report could have formed a basis for the SAT's reasoning, it would still be in contradiction with the PIT Regulations. As such, the SAT could have taken the opportunity in the present case to question the legislative intent of the PIT Regulations to advocate for the inclusion of a knowledge requirement and address the debate on the inclusion of the same.[22]

Clear Contradiction of PIT Regulation 2(1)(g) and Note to Regulation 4: The literal rule of interpretation states that while interpreting statutes, the content of the relevant provision must be read in terms of its general meaning and no attempt should be made to widen the scope of the words.[23] Here, we must consider the wordings of Regulation 2(1)(g) of the PIT Regulations and the Note appended to it.[24] It is substantially clear that any individual in possession of UPSI would be an insider. Further, the Note clarifies that said individual would be an insider no matter how or in what way they came in possession of the UPSI.[25] As such, it is submitted that the SAT has added the requirement of knowledge in the sections itself and wrongfully acquitted the Appellants on this ground.[26]

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[21] SEBI (Prohibition of Insider Trading) Regulations, 2015, Reg. 4
[22] Roopanshi Sachar & Dr. M. Afzal Wani, 'Regulation of Insider Trading In India: Dissecting The Difficulties And Solutions Ahead' 2 (2) Journal on Contemporary Issues of Law <https://jcil.lsyndicate.com/wp-content/uploads/2017/01/Roopanshi-Dr.-Afzal.pdf> accessed 22 June 2022
[23] Abhinav Palsikar, 'Critical Analysis of Literal Rule of Interpretation' (*SSRN E-Journal,* 30 December 2020) <https://ssrn.com/abstract=3720368> accessed 22 June 2022
[24] *Ibid*
[25] SEBI (Prohibition of Insider Trading) Regulations, 2015, Reg. 2(1) (g)
[26] *Ibid*

Non-Usage of Judgements from Other Common Law Jurisdictions: Further, it is noticed that the SAT did not make use of case laws from other common law jurisdictions such as the United Kingdom ("**UK**") and the United States of America ("**USA**") (cumulatively, "**other jurisdictions**") to buttress the element of knowledge. I submit that it is important to realize the distinction in the approaches followed by the insider trading regimes of India versus other jurisdictions: a) USA: The Securities Exchange Act of 1934 provided that criminal liability will be imposed for insider trading only when there is a "willful violation" thereof,[27] thereby implicitly recognizing the element of men's rea.[28] However, in order to make the requirement explicit, the U.S House of Representatives passed the Insider Trading Prohibition Act, which sets forth the knowledge requirement.[29] b) UK: Similar to the USA, the intention is also considered an important element in the UK when it comes to insider trading contained in section 53 of the Criminal Justice Act of 1993.[30]Thus, the insider trading regimes in these other jurisdictions are evidently distinct from India's, which does not account for mens rea. It is to be noted that the SCI in a number of judgments has opined that making reference to judgements of foreign jurisdictions in reaching a conclusion is subject to the requirement that significance must first be given to what is contained within the Indian law.[31] As such, it is again emphasized that the SAT should have made use of case laws from other jurisdictions to only signal a pertinent need for a change in Indian insider trading legislation rather than merely making a mention of the knowledge requirement on its own in contradiction to the PIT Regulations.

Ambiguous connection made between general information and requirement of knowledge: In the present case, the SAT opined that generally, available information would not be UPSI under the PIT Regulations.[32] In the next line of their order, they go on to state that "information can be UPSI only when the person getting it had knowledge that it was UPSI."[33]

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[27] Securities Exchange Act, 1934, s 10(b)
[28] *United States v Murdock* [1933] 290 U.S 389, 394 (1933); *United States v Dixon* [1976] 536 F.2d 1388, 1397 (2d Cir. 1976); *United States v O'Hogan* [1998] 139 F.3d 641, 647 (8th Cir. 1998)
[29] Insider Trading Prohibition Act, 2019, s 16A (b)
[30] *R v McQuoid* (2009) 4 All ER 388
[31] *State of West Bengal v B.K Mondal & Sons* (1962), AIR 779
[32] *Ibid,* 15
[33] *Ibid*, 16

It seems that they have attempted to make a remote connection between information being generally available and the accused thinking that it is generally available and thus not having the knowledge that the information was UPSI. However, it is submitted that there is absolutely no basis within Indian statutes as well as case law to make such a connection and it is inherently flawed.

CONCLUDING REMARKS AND THE WAY FORWARD

To conclude, it is submitted that the SAT was evidently erroneous in its judgement in the present case. The SAT does not possess the powers to overreach the provisions of the law and add qualifications to it. However, one must realize that this judgement brings forth pertinent questions about the inclusion of mens rea in determining the liability of innocent tippees. It is noticeable that the SAT has in various instances attempted to impute a knowledge requirement within insider trading, most notably in ***Rakesh Agarawal v SEBI*** and the present case. This signals a need for reform in the PIT Regulations. It is argued that the recommendations of the Sodhi Committee Report must be re-considered to bring India's insider trading regime in consonance with other jurisdictions.

The non-inclusion of mens rea serves no purpose in terms of mitigating undue advantage to a particular person and in fact, goes against the foundations of criminal law. In his article, Prateek Bhattacharya comments on India's insider trading regime by stating that "SEBI is well poised to tackle future threats to investor confidence and market integrity."[34] In light of this, it is clarified that India's strict insider trading laws are a right fit for its peculiarities and it is only suggested that: (i) an innocent tippee defence be introduced wherein (ii) the burden of proof would be on the accused.

[34] Bhattacharya, Prateek, 'India's Insider Trading Regime: How Connected Are You?' (2019) 16 (1) NYU Journal of Law & Business, Fall, <https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=&cad=rja&uact=8&ved=2ahUKEwjL7bDNhZv3AhWuzjgGHd2TB4wQFnoECAkQAQ&url=https%3A%2F%2Fpapers.ssrn.com%2Fsol3%2Fpapers.cfm%3Fabstract_id%3D3512313&usg=AOvVaw3gxQWtkOAH9TLSURFRLPZp> accessed 22 June 2022