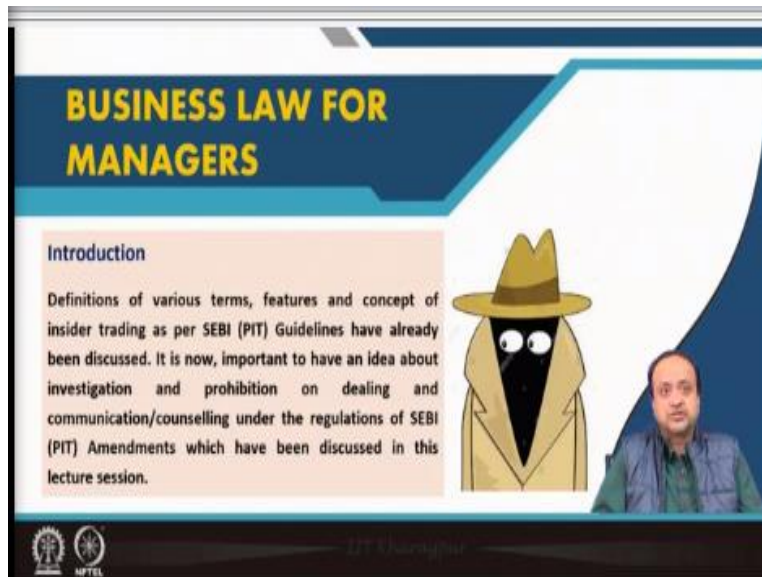


Business Law for Managers
Mr. Kaushik Mukherjee
Vinod Gupta School of Management
Indian Institute of Technology, Kharagpur
Module-3: PIT (Prohibition of Insider Trading)

Lecture-12
Investigation and Prohibition on Dealing, Counselling

Good morning, we are on lecture 12 investigation and prohibition on dealing and counselling relating to PIT prohibition of insider trading regulations.

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Now we have discussed this insider trading PIT's guidelines, now it is also important that we understand that how the SEBI the authority looks into this. End of the day if this regulation has seen the light of the day is because of the securities and exchange board of India. It has been doing all that possible to ensure that this menace of insider trading which is a very, very difficult proposition.

It is not at all easy to put a blanket ban on this, because like one cannot prevent 1 person from joining competition by carrying information. One employee leaves 1 company and joins a competition then many companies have the contract written while taking him on employment

that he cannot join competition. Well, that is not law, that law we absolutely will fall flat before the court.

Therefore, what companies have done, they have taken a cooling off period that you cannot join for 1 year or maybe 2 years maximum, even 1 year is more than enough. Now even after 1 year he joins if he carries information with him which is not in laptop, which is not in pen drive, which is not in any form but only in the brain chip, I call it the brain chip. If in the brain chip he carries it then nobody can stop it, same in case of insider trading.

To what extent one can put a blanket control, how come it can be made totally full proof? That is what the journey SEBI has undertaken. It is almost an impossible task considering the corporate scenario; however, the step SEBI has made the awareness level SEBI has done, the action SEBI has taken, the penalty SEBI has imposed and the kind of tracking SEBI has started doing is extremely important to understand and to be appreciated.

Corporate India has taken cognizance of prohibition of insider trading regulations. And it is also important to understand that many discussions nowadays when takes place in the board, the independent directors voice their concerns to note that these are all very price sensitive information which we are discussing now gentlemen. So, this should remain unpublished for some time as per law, as per requirement.

So, we should all ensure that this information does not pass even by inadvertence nor any of the recipients of the information if at all on a need-to-know basis, there is a word called need to know, somebody has to be shared this information. If that be the case to ensure the person to whom we are sharing the information also is guided by this oath of not passing the information to anybody else or to trade in the shares of the company during possessing this information. So, SEBI has done that job quite well in making corporate India understand, that they are under scanner.

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KEY POINTS

- Power to make enquiry
- Right of board to investigate
- Procedure of investigation
- Obligation of Insider on investigation
- Submission of report to board
- Prohibition on dealing, communication

The slide features a video inset of a man in a blue shirt speaking. The background of the slide is blue and white with a stylized graphic of a person walking in a window. Logos for IIT Madras and NPTEL are visible at the bottom left.

The various powers of SEBI in this direction is first of all to make a suo-motu inquiry without anybody informing SEBI, any investor informing SEBI, any whistleblower informing SEBI. There are instances where employees of the company have informed SEBI about insider trading violations. There are whistleblowers blowers within the organization who ensure that unpublished price sensitive information is not passed on and also unpublished price information is not used for buying and selling of shares.

SEBI may make it on it is own and enquiry, many times it happens that chairman of a board in a press conference when media asks question, this is a common thing. Many times, media go on asking probing questions and the chairman of the board, most time nowadays they are fully aware that if they say something which is beyond what is available in the public domain then that tantamount to breach of insider trading regulations.

Say they do not normally speak but if for any reason at any point of time, if he makes a comment stating that certain such companies being looked into for acquisition or such and such person is being looked into as head of operations or even such and such person is joining our board as independent director when there has been no information given to the stock exchange and that is published in the media.

It is for sure the next day morning before 10 o'clock the surveillance department of either Bombay stock exchange or national stock exchange or both the stock exchanges by 10 o'clock sharp a letter or the fax will come, not a fax, email nowadays will come from the surveillance department of the stock exchange asking for the clarification whether the chairman has exactly said this on what basis because no information is available in this respect in the market.

This has happened, this happens random used to happen all random now it has reduced. It has reduced because awareness has come up; it is the duty of the compliance officer the public relations head to ensure nothing goes to the press which is not going to the public, press and public together. If it goes to the press or the press gives it in the newspaper without going to the stock exchange that is violation.

Board investigates even in cases where the share prices suddenly goes up in a company, without any reason there is a certain spot in the prices of the shares and it continues for few days. Then the SEBI writes to the company, the company secretary saying that your share prices have gone up this much in the last so days and the volumes have also gone up, request to find out the reasons and let us know.

Very innocuous answer can be that we do not know anything about this, we do not control share market, it is all the case of demand and supply, if investors are demanding my shares the prices are going up, yes, there you know a straightforward answer, no one can touch you. But the question is not like that, the question is awarding you, making you aware that we are noting this.

And therefore, you on your turn make all your persons who are privy to the unpublished price sensitive information that during this period you are under double scanner do not ever try to trade down the shares of the company. Warning you, SEBI is giving a warning that we are watching your prices are going up and your volumes are going up. Even when the market exchange the Sensex is going down, your prices are going up, what have you done?

What information you are sitting on? What is that information which you have shared with few people who are buying the shares of the company? Whereas, the other retail investors are not

aware of, they are not buying, SEBI can find out also who is buying the shares of the company. So, investigation from SEBI can come for various reasons and once it starts it is quite time consuming and extremely provocative and also it brings out more than what actually has gone to it.

Because they start then digging for information, so no one actually would want an investigation from SEBI for a case like this rather they would like to comply in (()) (10:46) what SEBI has said. And when the investigation starts if you do not cooperate then it will be a criminal breach, the directors may be prosecuted. And it is a time bound investigation, it is not an investigation will go on.

The registrar should be also under question, it is almost like a CCI investigation while they check the mails, they start checking the mails of the insiders what kind of information has been passed on. So, investigations by SEBIs on their own on information from whistleblowers, on information from the market, various sources are there.

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Investigation

Power to make Investigation

- It is the power of Board which may make inquiries with persons or any other person as deemed fit, to form a prima facie opinion as suspected to whether there is any violation of these regulations.
- In that case the Board may appoint one or more officers to inspect the books and records of insider(s) or any other persons as mentioned in clause (i) of sub-section (2) of section 11 for the purpose of sub-regulation (1).

Even on a prima facie basis SEBI can start information investigation, SEBI might find out that this is just a prima facie case, like prices are going up, volumes are going up but there is no reason, the company has not made any disclosure, what can be the reason? Then SEBI must start

investigating who are buying the shares, is it a cluster of investors who are buying the shares? Is a few institutional investors who are buying the shares?

Then you will try to find out what was the investor conference said last time? What was shared in that investor conference because whatever has to be shared in the investor conference has to be shared with the stock exchange? Now if they find out we want to go through the recordings of the investor conference, all investor conference April 22 onwards has to be recorded, now it is a voluntary period, you may record, you may not record.

From April 22 all investor conferences have to be recorded, so many companies already have started recording investor conference. Now if you have given in the investor conference 20 slides, while making the presentation before the investors you have deliberated on the 20 slides but while talking on the slides you have passed on much more information than what you have contained in the slides, very common.

When a person starts talking on a slide if he is not always very aware that I may pass on price sensitive information, he may go on giving more information than what is contained in the slide. So, SEBI starts recording the slides, checks those recordings and if they can find out that the chief financial officer or the managing director has given more information to those 10 investors who have been invited in that investor conference.

Then what has been given to the public in the form of a slides 20 pages or 20 slides, then it is a clear case why this people are buying the shares of the company. And why the volumes are going up or the prices are going up, then the entire company, management, the CFO, the managing director can be show cost, can be penalized and the image of the company takes a meeting.

That you have held a press conference, investor conference, you have invited selected investors, you have passed on information much more than what you have given to the stock exchange, a clear case of breach. So, from a simple case of a share prices going up, volume going up without any reason SEBI may started investigation. Then the company will be totally at the receiving end

because company would fail would feel I have given the information to the stock exchange; I have given the slides.

But while giving the slides you have passed on more information while meeting, while giving the slides you have certain information but while meeting the investors you have passed on more information that is what we call sharing unpublished price sensitive information, a clear case of breach. SEBI has today offices almost in all metropolitan cities, SEBI is a robust body now though do not directly come in contact with the corporates, it contacts only through the stock exchanges.

But and even the corporates cannot directly approach SEBI, they can only approach the stock exchanges to keep that independence arms lengthening, SEBI does not come in direct contact with the corporate only through the stock exchange. Unless an investigation starts where it calls the corporate in its office for submission of papers, for discussions, for deliberations, for inquiries, otherwise no.

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Investigation

Right of the Board to Investigate

i. Where the Board, is of prima facie opinion that it is necessary to investigate and inspect the books of account, either records and documents of an insider or any other person for any of the purposes specified in sub-regulation (2), it may appoint an investigating authority for the said purpose.

It has all the powers like a quasi-judicial body, it can summon, it can inspect, it can cease, so all those powers it has got. It is an investigating body totally authorized, empowered that can take even help of the police.

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Investigation

Right of the Board to Investigate

ii) The purpose referred to in sub-regulation (1) may be as follows:

- (a) to investigate into the complaints received from investors, intermediaries or any other person on any matter having a bearing on the allegations of insider trading; and
- (b) to investigate suo-motu upon its own knowledge or information in its possession to protect the interest of investors in securities against breach of these regulations.

DD Manager

Complaints receive from investors, intermediaries, brokers, banks, even employees as I told whistleblowers and of course in it is own suo-motu. On his own knowledge like price is going up, volume going up, nobody is informed but SEBI starts on it is own.

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Investigation

Procedure for Investigation

- Before undertaking any investigation under regulation, the Board shall give a reasonable notice to insider for that purpose.
- Notwithstanding anything contained in sub-regulation, where the Board is satisfied that in the interest of investors or in public interest no such notice should be given, it may by an order in writing direct that the investigation be taken up without such notice.

DD Manager

Well, an opportunity of being hard is something which is to be given everywhere, SEBI is not come on a fine morning like a CCI dawn raid, no, SEBI does not do like that, knock your office, seize all everything not like that, they will give a reasonable notice to the insider for that purpose. Unless something is that important that it can be destroyed or something like that, normally does not happen, it is not like CCI. Normally gives notice and where in exceptional

cases where there may be a chance of the investors or public interest may be sabotaged, they may do it without giving such notice but these are rare cases.

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Investigation

Procedure for Investigation

- On being empowered by the Board, the investigation authority shall undertake the investigation and inspection of books of account and the insider against whom an investigation is being carried out an insider or any other person mentioned shall be bound to discharge his obligations as provided in regulation

And total cooperation, any non cooperation is something of a violation and criminal violation.

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Investigation

Obligations of insider on investigation by the board

- It shall be the duty of every insider, who is being investigated or any other person as specified under provision to produce to the investigating authority such books, accounts and other documents in his custody or control and furnish the authority with the statements and information relating to the transactions in securities market within such time as the said authority may require.
- The insider or any other person as specified under provision shall allow the investigating authority to have reasonable access to the premises occupied by such insider and also extend reasonable facility for examining any books, records, documents and computer data in the possession of the stock-broker or any other person.

Any document that they are taking, any document that they are keeping with them they will give a recedes, they will record that. All the information, premises, computers, laptops, mail exchanges, server, everywhere they have to have access, all the data they need to know. Because mails are very important sources of information, extremely good sources of information, even mobiles, WhatsApp messages. There is a case where a finance guy of a company, young person

he got to know the results of the company, he took a photo of that and shared with his friend who was actually a broker.

Broker not a broker is an employee can broker because many employees become trader. Many employees at their young minds who after discharging their official duties of course not compromising, have lot of spare time and they trade in the shares. So, he has no way connected with that company, his friend is a finance guy, he gives information to him. He buys the shares, sells the shares and his friend and him share the money, it was caught, caught unfortunately the finance guy there was a camera. Now in most companies these are cameras and, in that camera, it was shown that he was taking a photo of the financial results.

There was no need for him to take a photo, why should a finance guy take a photo of the financial results which has not yet been adopted by the board? The young man took a photo in his mobile and that ended up in his losing the job and also his friend under investigation. So, these are all instances where small child like innocent I would call it but still unpardonable. So, although mobile informations, email exchanges, even sometimes telephone calls or recorded numbers are investigated to find out what?

If they zeroing that here is the information flow then they will do all this. But in a phishing expedition normally they do not go for checking all the phones and all, first the zeroing who can be the person? Who could have done it? Maybe 1 or 2 heads, the head of department or someone like that, then all the information of those 2 persons, from there they will find out all the routes.

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Investigation

Obligations of insider on investigation by the board

- The investigating authority, in the course of investigation, shall be entitled to examine or record statements of any member, director, partner, proprietor and employee of the insider or any other person as specified under law.
- It shall be the duty of every director, proprietor, partner, officer and employee of the insider to give to the investigating authority all assistance in connection with the investigation, which the insider or any other person as specified under law may be reasonably expected to give.

They can approach anyone, any member, any director, any partner, any employee, total authority and full cooperation is required.

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Investigation

Submission of Report to the Board

- It is important that this act has provision for the investigating authority who shall, within reasonable time of the conclusion of the investigation, submit an investigation report to the Board.
- The Board shall, after consideration of the investigation report communicate the findings to the person suspected to be involved in insider trading or violation of these regulations.

They will prepare a time bound report, it is not a report like it will go on doing for years or months; normally they do it within 30 days to 60 days. They submit a report very fast on prima facie evidence is what is coming out and depending upon the report the higher authorities have SEBI take a call, what should we do? Shall we go for further or shall we close or shall we impose a fine right away?

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Investigation

Submission of Report to the Board

- The person to whom such findings has been communicated shall reply to the same within 21 days; and
- On receipt of such a reply or explanation, if any, from such person, the Board may take such measures as it deems fit to protect the interests of the investors and in the interests of the securities market

Once the report is prepared, they give a communication to the person to report. Of course, he will also have an opportunity of being heard, that this is a report against you, this is what we have gathered against you, so you give a reply that is also time-bound reply. Normally no one replies without a legal counsel whenever an employee or a senior director or somebody is getting a letter for show cause notice or something like that from SEBI or investigating report.

The first thing it does it speaks to the legal counsel and based on the legal counsel he drops a reply and gives it. Now most of the time it is seen will have case laws after this where case studies will find out. Then so many cases people have come on their own immediately getting the report admitting everything without fighting even, without contesting even, so many cases. Because the legal council must have advised him no point fighting this because case is so clear you have traded, you have violated the law.

So, your council will not give you a wrong advice that yes, you fight I will ensure that you will be in the case because he will never win the case. Because he knows the investigative report were clearly shows that he has violated the provisions, so what is to be done to pay the penalty, huge amount of parenting to the extent of crores, they pay and they accept that there has been a violation which we call compounding.

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Investigation

Prohibition on dealing, communicating or counselling

- It is well defined that no insider shall either on his own behalf or on behalf of any other person, deal in securities of a company listed on any stock exchange, when in possession of any unpublished price sensitive information.
- Also, no insider shall communicate or counsel or procure directly or indirectly any unpublished price sensitive information (UPSI) to any person who while in possession of such unpublished price sensitive information shall not deal in securities, Provided that nothing contained above shall be applicable to any communication required in the ordinary course of business

So, communication also even if you are not traded, if you have communicated, we have a famous case where only communication led to so many things. You may not have done anything, you may not be even the party to the booty the profit you have made but you only passed on the information to anybody or even your known, unknown anyone. But he has made money, you have not made money, still you are responsible, connected person and you will be charged.

You might take the please sir I have not done anything me lord, innocently I have given that information, thereafter what he has done I am not aware of, 2015 act very clear, no way. Because it is correct unless that is done you will not be able to stop the menace it has to be, the person should never pass on information whether you make money, whether you make loss, whether you do any trading or not is immaterial.

You are the source who has passed on the information you will be responsible, no company shall deal in the securities are another company associate of that other company while position of unpublished price sensitive information, this is again correct. Dealing in the shares of an associate company, that also is another menace; you invest in shares of a company knowing all the inside information about that company that also is a prohibition of insider trading regulations because you have access to price sensitive information.

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Investigation

Prohibition on dealing, communicating or counselling

- b) such company has put in place such systems and procedures which demarcate the activities of the company in such a way that the person who enters into transaction in securities on behalf of the company cannot have access to information which is in possession of other officer or employee of the company.
- c) it had in operation at that time, arrangements that could reasonably be expected to ensure that the information was not communicated to the person or persons who made the decision and that no advice with respect to the transactions or agreement was given to that person or any of those persons by that officer or employee; and
- (d) the information was not so communicated and no such advice was so given.

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Only thing it has to be ensured that as a corporate which I started by saying ensure that you have enough information in the website and any employee can go through the website and find out the dos and don'ts. It should not happen the people are not made aware of; it is the duty of the company to make them aware of the entire prohibition of insider trading regulations and from there derive the code of conduct of the company.

Every company would have his own code of conduct what is to be done, what is not to be done? Broad guideline is given by SEBI but detailed one has to be given by the company, like many companies totally banning employees after a certain level to deal in the shares of the company. Model code of conductor SEBI has never said that but you can do it, you can make your own company like that or even companies now thinking why any level? At all levels let us stop buying shares of the company, even associate companies.

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Investigation

Prohibition on dealing, communicating or counselling

➤ In a proceeding against a company in respect of regulation 3A which is in possession of unpublished price sensitive information, it shall be defended to prove that acquisition of shares of a listed company was as per the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations,

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In fact, defenses of the companies or the employees many times it seems are totally under kind of admission. Defence is not really a defence, it is a kind of admission, yes, there has been, we have taken this action and going forward will ensure must sister compliance, is a clear case of admission, no defence. Because when SEBI comes out this kind of complaints or investigation reports very little can be done.

Because these are very clear, these evidences become so clear that it becomes defenceless. It is therefore very imperative for the corporates and the senior management and the board of directors to do a review of the cases happening if any in the company and the policy. Whether

further stringent measures are required, whether further review of the policies are required and also on a test case basis have interaction with some of the employees to understand how they are looking into this prohibition of insider trading regulations whether they are facing any challenges or not.

Because all companies have not stopped buying and selling of the shares of the company at all levels. There are still 90% or more than 90% of companies which allow their employees to buy and sell in the shares of the company. The concept of trading window has come up by SEBI saying that this is the window, this is the time when the company's employees can buy the sale and shares.

And buy and sell in the shares of the company, rest of the time they cannot. So, when the trading window is closed, no employee who has access to that information should buy and sell the shares irrespective of the fact whatever the company says. Now trading window closes when? Normally the trading window closes whenever some financial results are to be disclosed to the stock exchange, before that all companies normally do is close it for a period from the quarter end.

Say for example if it is January, February, March from 1st of April till the results are out, now we get quarterly results. Earlier used to get annual results then 6 monthly, now it is quarterly, so every company comes out with quarterly results within 45 days from the end of the quarter. The law says 45 days from the end of the quarter; every company has to come out with his results.

So, SEBI has prescribed a common trading window closure for all companies, we call the closure of trading window which is from 1st April till the date your board meeting is held for consideration of results and 48 hours beyond that. So, it is a standard practice, every employee should know that I cannot trade with the shares of the company during the period of 1st April till the board meeting 48 hours after, similarly 1st July till board meeting in the month of August or 45 days thereafter.

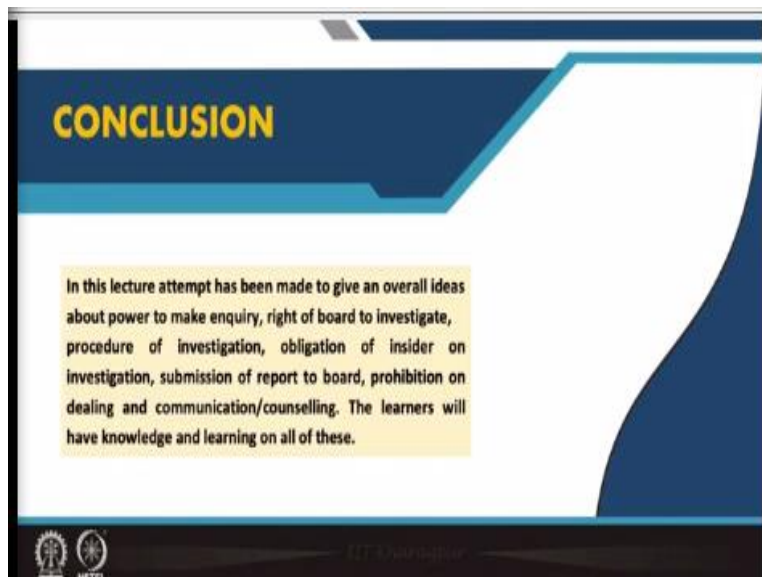
Similarly for the next quarter ending, this is the 4 blocks of around 40, 45 days when the trading window is closed, rest of the time you can buy and sell of the shares as per SEBI. Now the model

code of content of the company may further tell no you cannot any point of time, unless you disclose to the company or you have a trading plan or you are at a certain level below, above you cannot, so these are further restrictive code of conduct.

But SEBI says trading window closure very clearly from quarter end first day till 48 hours from the conclusion of the board meeting. No employee can buy and sell of the shares, trading window totally closed, employee having access to unpublished by sensitive information, they should not, designated employees. Insider trading definitely the privation, regulations is still unfolding, not for a moment I am saying that it is again a test of time as and when further developments in technology will take place.

More and more cases will come out where people are trading of shares, if it is found out then most stricture provisions will come in. I have taken references to some of these books but mostly as I always say is that from my experience and from my readings and other articles that I go through from there this is what I normally make present my cases. I do not restrict myself only to the bare acts and others, I share what I find happening actually in reality.

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Thank you so much, wish you all a very good time ahead, thank you.