**Business Law for Managers**
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**Module-3: PIT (Prohibition of Insider Trading)**

**Lecture-14**
**Model Code of Conduct for PIT, Trading Initiatives**

Good morning, we are on lecture 14 on model code of conduct for PIT and trading initiatives, PIT stands for prohibition of insider trading.

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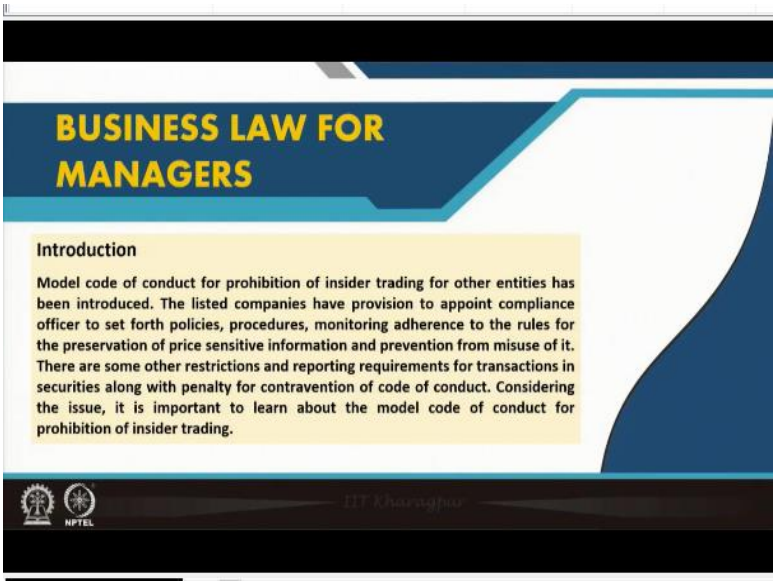


The model code of conduct is basically a guiding tool prescribed by SEBI to be followed by the corporate, to be adopted by them as per their requirements. It can be stricter than what is mentioned in the model code of conduct, but ideally should not be easier than what has been stated. So, depending upon the circumstances of the company the company may further tighten it, regulate it, but not loosen it up. That is the purpose of this h model code of contact for probation of insider trading.

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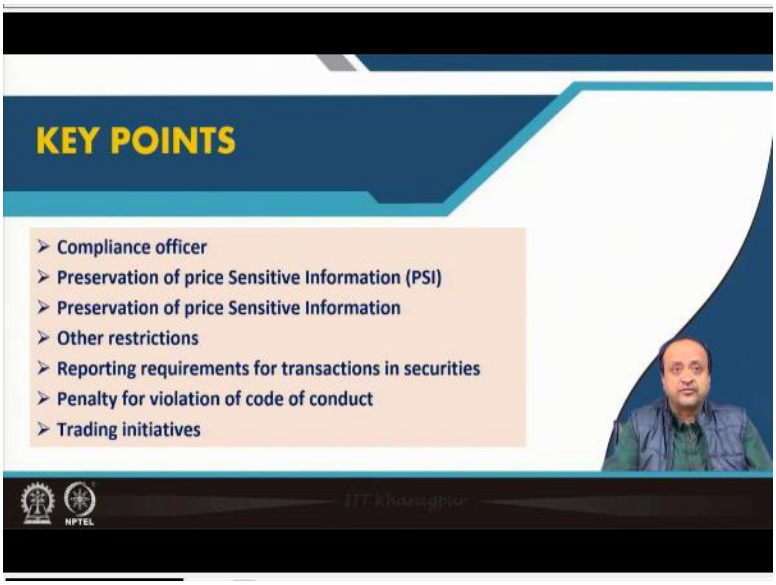


Now whose responsibility is this to do? The first and foremost responsibility arises from the compliance officer of the company, it is his responsibility, he has to ensure that the prohibition of insider trading regulations, the model code of conduct is understood and then a code of conduct for the company is prepared. And then that is made known to all the employees, deliberated with some of them on a test check basis to understand how far they have understood.

If required make a presentation before them and also make a presentation before the board of directors the audit committee, get their approval consent and finally put it in the company's website, this is the introduction part of it. But while introducing this itself is a challenge because there may be observations given by the employees and others of fact that. When the model code of conduct is saying this why the company is putting so much h interpretations and making it so strict for the company for the employees to do.

Why not allow the employees to do exactly as per the model code of conduct. So, this debate was going on in all companies. Now it all depends how the board of directors feels; what is the mindset of them? An example of this can be that the board of directors of the company may allow employees to trade in the shares up to a certain designation beyond that no. Or they may totally ban all the employees, model code of conduct has not said anything about that, all employees can trade only not during the trading window closure when persons having price sensitive information will not trade, other persons even during that time they want to trade they have to disclose.

But most of the companies have made it very clear to the employees not to trade during the closure of trading window. Even then there was reluctance of the employees that what is the problem if I disclose even lot of young GTs when they are recruited, they said why is the company's policy is not to trade in the shares? Do you not feel that the employees also to have been the owners of the company ownership, they bring out stewardship or ownership of the company which is largely right; there is nothing wrong in that asking.

But again, the company's policy depends, but as of now most of the companies allow their employees to trade in the shares during the non trading disclosure, I mean non trading closure period up to a certain level. This is the position as of now. Preservation of price sensitive information is very important; it is important that this does not get by any chance disclosed to others other than on a need to no basis. Reporting requirements, we will see as we unfold and penalty for violations of code of content very stringent, very stringent violations are there for code of conduct and even the fine can be quite high in certain cases, some companies have asked employees to go also.

Modern code of conduct does not say it leads to the company to take the disciplinary action and some companies have taken the extreme action of even asking the employees to go for repeating violation in prohibition insider trading not one single case but repeat. It has been happening again and again for employees; those employees have been asked to leave the organization because of violation of prohibition of insider trading regulations.

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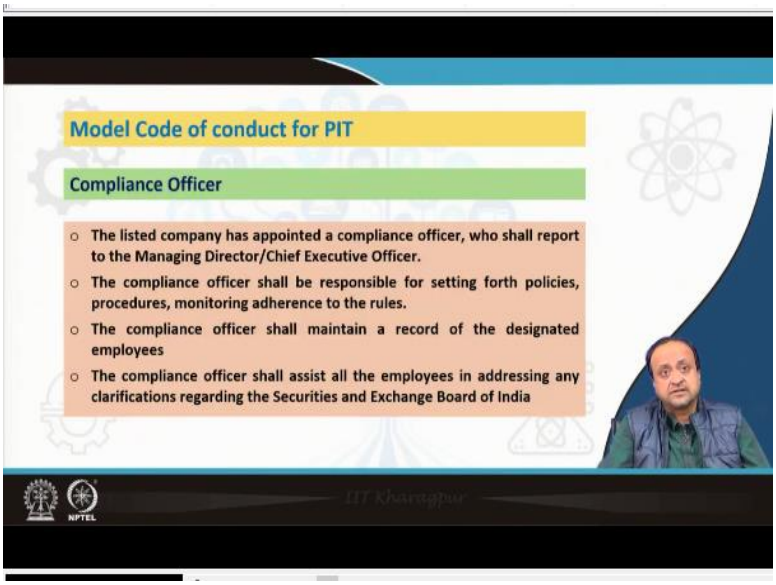

Now this compliance officer as we are taking is the internal custodian of implementing, insider trading prohibition, insider trading regulations in the company. He is the sole internal custodian. He will be responsible for setting for the policies, procedures, monitoring and errands. So, while setting for the policies he will take the help of the board the audit committee, get invaded by them. And also, some companies likely do to the risk management committee because there is a huge risk of insider trading.

So, the risk management committee of the board also is taken into consideration and is involved in setting force the policies, the procedures and also time to time the risk register is placed in which any violation of the insider training regulations are highlighted to the risk committee of the board and their suggestions are taken. There should be a clear-cut record of all the designated employees of the company, by designated employees means employees who are privy to or who have access to unpublished price sensitive information including connected persons.

So, all this list has to be mentioned any particular point of time if somebody asked who are the designated employees? Now again if a designer employee leaves the organization it has to be updated. If somebody joins as a designer employee it has to be updated also. So, continuous monitoring and updating is required for the list of designer employees. The compliance officer will be the single point of contact for addressing all clarifications regarding the sequence exchange board of India's model code of conduct.

There will be lot of questions on trading plan. There will be questions on selling the shares, how long I have to hold the shares? If I buy the shares, can I go for a reverse transaction the next day? No, the law says minimum 6 months holding. If you buy the shares, if you go on buying first buy, second buy, third buy, there is no gap in that, you go on buying, but once you buy to sell there should has to be a gap of 6 months. So, the holding has to be 6 months. That is the model code of conduct saying. Some company makes is 1 year.

Employees disagree, if the model says 6 months you can make it, why should you make it more than 6 months? So, fair enough 6 months, but from the last buy. So, the first buy may be in on 1st of Jan, the second by may be 30th of Jan, the third by may be 5th of February. So, from 5th of February 6 months you cannot sell, not 1st of January in a series of buying. Similarly in selling, if you are selling first, second, third and the buy will come after 6

months. So, there is to a lock-in period of 6 months, both in case of selling and in case of buying.

This is a model code of conduct, some companies make it 9 months, some make it 1 year, but again employees of the companies sometimes they have deliberations with the compliance officer, why are you making it more sector, what is that purpose is to be served? So, it all depends but again the compliance officer if he feels that it should be done then he will place it before the risk committee and the audit committee to decide. Now if the risk committee, audit committee is convinced it has to be 1 year then the employees have to agree because that is the policy making of the board.

So, compliance officer has to balance between these 2 requirements the employees needs and what is the law saying and how much to really put it in the code of conduct of the company. It requires lot of deliberations, it requires understanding. Unnecessarily it should not be forced upon the employees, at the same time the code of contact should look robust, strict and something which is also exercisable, doable.

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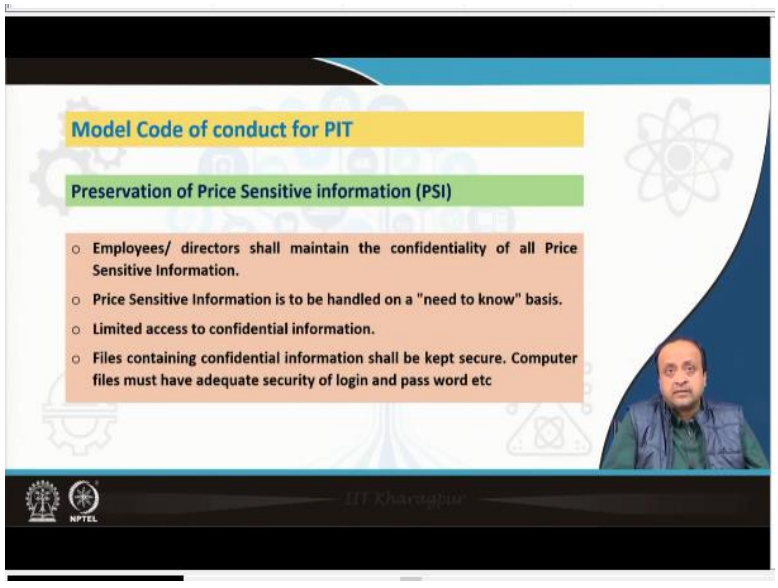


Confidentiality of information, it should be actually a culture in an organization, today in many companies they do not even talk to any vendor, any consultant, without signing an NDA, a non disclosure agreement. This is the culture of an organization, the moment you enter to a company they say hello, hi, have a cup of tea and then let us start talking on the subject on consultancy.

What do you do? I do this, I can help you in this, fine hold on we have a standardized NDA agreement, let us sign that first and then we talk. The company gives the NDA to the consultant. The consultant goes through and gives these observations on the NDA, non-disclosure agreement based on which they start talking. So, it has to be something of a process that no information flows to anyone unless and until we sign some kind of a confidential disagreement.

Because I need to give it that information to you, I need to tell you certain information which perhaps is confidential in nature; I am not sure but can be confidential in nature. So, why not enter into an NDA that is also a very good step, where you have ensured that you enter into an NDA. Now if the vendor discloses that to another party, he will be responsible not you, but you have not entered into an NDA and he discloses that you will be also responsible.

So, as a corporate you need to ensure that the system is robust in an organization, it is a culture that we do not share any information which is unpublished and any information which we think can be confidential in nature. Even if it is published it is not no longer confidential, but if it is unpublished, it is confidential and some people only know. So, I cannot share that information with you?

Yes, you need to know, a consultant need to know many information before he can give a consult, it is right, if he is not given that information how do? You give you the advice, for example somebody is making a strategy for you, say for example ESG environments societal and governance is a buzzword now. So, you create an overarching strategy for that. Now that group or gentleman or person who is leading the consultant he might or she might ask for information from each of the departmental heads including the management committee members, the board.

He will interact with the vendors, he will interact with the customers, he will interact with the employees. So, if he asks for information which are absolutely confidential. Then if you cannot share that information no strategy can be formed. So, how to share that information? You share the information by entering into an NDA non disclosure agreement. Now if you enter into an NDA in that case you are protected, you have given the information very clearly that he will you use it only on a need-to-know basis.

He will not disclose this information to anybody unless he ensures that person also maintains confidentiality of that information. If there after he trades, if there after he does anything you are protected that NDA protects you, need to know basis, price sensitive information is to be handled on a need-to-know basis, by PSI here we all mean unpublished price sensitive information, if an information is known in the market, then no need to know, unpublished price sensitive information is to be handled on a need-to-know basis.

I have to give you this information. Say for example the CFO has to give this information to the treasury head on the results of the company. Now he gives it on a need-to-know basis only to him and only when it is required to him not before that. He is not required to be given 10 days before, he has to be required to be given just 1 day before, even to the board of directors many companies are sending the financial results along with the board agenda which is as per law the agenda has to be sent 7 days before the board meeting.

So, 7 days before the board meeting even if the results are ready no one sends to the board of directors, they send without the results to the board of directors' agenda. Now the board will be asking, the director should be asking, send me the result so that I can come and make a deliberation on the results, you give it to him only a day before and that too after the trading hours. Trading hours ends on 3:30.

So, 4 o'clock you send him the results. He goes to the results and comes next morning. He might be unhappy, but if the company policies we share the results with the directors only a day before after trading hours that is also a practice. Because many times in the board there are not only directors, there are also nominee directors. Now nominee directors are directors who are nominees of the financial institutions.

Any information to them also would be definitely confidential, they are all directors but why take a chance in providing information any beforehand, you provide it when it is absolutely essential, need to know. He needs to know on the evening before the board meeting because reading a financial result for a financial literate person does not take a whole night and that to an UFR which is a limited version of the results.

Annual report we all understand it takes time. In any case that is sent 21 days before. So, for 21 days one can study that big fat document, but this is a one-page UFR it does not take few

hours than to in fact an hour is more than enough to study the result. What is the point giving it 10 days before, 7 days before, 5 days before? So, companies have stopped it and they are giving it only a day before night after the trading hours.

Even some companies are doing it on the table, as soon as the meeting starts the results are displayed and let us deliberate on the results for the whole 2 hours, 3 hours, no problem but then and there only not beforehand. This practice also has come in limited the access, it should be extremely limited and only on a need-to-know basis. Today nobody can take from the computer, a pen drive, most companies have stopped it.

Some companies even have stopped taking camera photos from the laptop, you cannot take mobiles are kept outside the office, while you are entering in the reception, any emergency calls numbers are given, manufacturing companies still not, but IT companies most of them trying to do that. So, much information is passed on, may be manufacturing companies also would be doing it.

Because pilferage of information, sharing information, data is so powerful, data is the costliest thing under the sun. If you have information about competition, you have everything in your hand. So, that is what everybody is looking for information on the competition. All unpublished price sensitive information they are looking for. At the same time this is something we need to be shared on a need-to-know basis.

How do you protect the files of confidential information, how protective is your environment, what kind of security you have got? All these are bonding questions and need to be looked into because confidentiality of information sharing your information sometime happens to hacking also.

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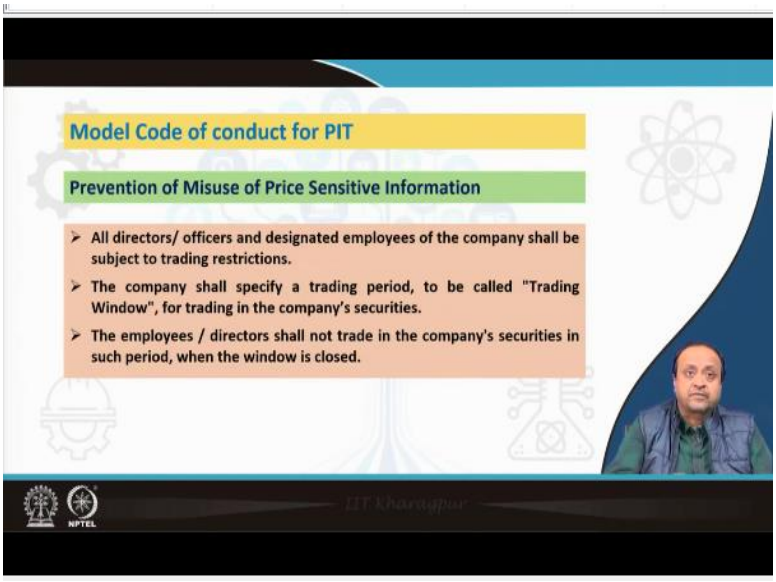


Trading restrictions, applicable for all, all designated employees, director's officers. Now data's officers are fully under the definition of designated employees. No director can say I am not private or unpublished by sensing information, he is always privy to unpublished by sensitivity information, it cannot be a ground for him, he is knowing all the unpublished by sensitivity information, he cannot escape that.

Now somebody may not attend the board meeting, somebody say I am not attending the board meeting therefore I was not aware of this. No, he is supposed to know even when he is not meeting the board to get the agenda of the board and after the agenda to get the minutes of that board meeting, what happened, what discussed? Minutes of the board meeting is something which is recording of the proceedings of the board meeting.

A member of the board who has not attended the meeting he also gets the minutes of the meeting, because he continues his journey as a board member. So, he cannot escape that, trading window is always open, accepting when it is closed, when it is closed their instances when it is closed, we will discuss that. No trading in company shares when the window is closed of whom of the designated employees. Please understand. Not all employees of the designated employees.

Now if one is not a designated employee then he can trade in the shares but he runs the risk actually. If it can be proved that though he was not a designated employee but still he was for that particular month or year or period private to unpublished prices in information and therefore he made the buy. Then in that case he is he will also be prosecuted. And it will be

the owners on him to prove that he was not private to unpublished price sensitive information just because he was not the designated employee will not save.

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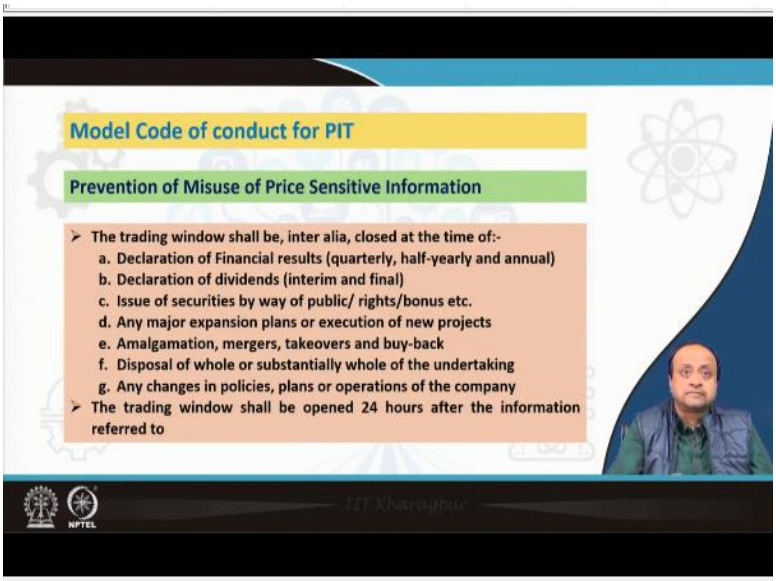


Now this is where inter alia; the word inter alia means amongst others, this is not an exhaustive list, this is an inclusive list. So, trading window shall be closed at the following times, declaration of financial results. This is perhaps one of the most information bearing document, earlier company used to come out with annual results. Now it is quarterly and then halfway when the 2 quarters March it becomes half year that is 30th of September. And finally, 4 quarters it is becomes annual.

Each quarter contains host of information, it contains the revenue for the period, it contains the materials consumed for the period, it contains the total employee expenses for the period, it contains the total depreciation for the period, it contains the total tax for the period, the profit for the period before the tax for the period and profit after the tax for the period. Detailed breakup not only that, it contains for the quarter, it contains for the preceding quarter last year or corresponding quarter last year and the preceding quarter as well as the whole year.

So, it contains a total box of information in a comparative analysis basis. Say for example we are preparing quarterly results for 30th September 21. Now 30th September 21 will include 30th June 21 that is the preceding quarter. And the corresponding quarter last year that 30th September 20, so that you can make a comparison quarter and quarter and preceding quarter

and it will also contain since it is 30th September it will contain half year for 30th September 21 and half year for 30th September 2020 and then the full year for 31st March 21.

So, all this information competitive analysis will come in one page to you with the total revenue, the other income, the total raw materials consumed, total expenses. Expenses on employees, freight, insurance, interest, detail expenses come, may be freight and insurance will not be able to get in one shot, may be clubbed but interest will come, depreciation will come, tax will come. So, all these information you are getting. Now supposing all this information will be placed before the board of directors and adopted by them then only it becomes public.

And this is done within 45 days from the end of the quarter. So, supposing 30th September the board meeting can be held within 14th November any date, now supposing board meeting is held on 10th November. So, from first October to 10th November you are sitting on that document which is getting prepared and all the designated employees may be privy to that information or a cluster of that information or some information in that document.

Therefore, to safeguard all this trading window has been closed, no buying selling can be done by this designated employee from 1st of October till 48 hours from the conclusion of the board meeting. That is on 10th member is a board meeting, so another 48 hours 11, 12, on 13 only they can trade in the shares. This is the law, trading window closure for financial results quarterly and half early same for annual. 45 days you can have the board meeting, supposing you have it on the 30th day or 40th day. So, from first to 40th plus 48 hours no trading by then employees of the company.

So, that is the law, but the question still remains here is little understanding is required that even before that say the period from 15th September or 30th September? Many of these guys have their information and they can trade in the shares during that time. Therefore, SEBI makes all those kinds of investigations when they are actually getting the digital database and they say movements in the shares, huge up and down movement in the shares during this period because trading is taking place from fast trading window is closed for this employee to trade in the shares but other public are always buying and selling, so there is up and down in the share prices.

If there is too many up and down SEBI will start seeing these persons have not bought and sell during this period is okay, but what about the preceding period. 15th March to 30th September is actually the red period, the period of caution, the red flag period when if you see that any of these designer employees at port purchase the shares and has made money then that employee is gone. He will be definitely prosecuted that you had unpublished price sensitive information and you have traded in the shares.

Now you prove you do not have, owners will be on you to prove, same declaration of dividend very important interim and final. Interim is dividend, dividend declared, any time before the final dividend during the year from 1st of April to 31st March anytime you can declare dividend, interim on the financial results of the company for the 1st April to 31st March.

No company does it before 6 months because unless you cover 6 months you do not get a picture line of sight for the whole year and you are declaring dividend on the proposed profit for the whole year, proposed profit. So, 1st April to 31st March your proposed profit you have to anticipate you can only anticipate when you have done a journey, you have done a run. Run should be at least more than 6 months, so what happens really 99.9% of the companies they declare their dividend after the 9 months that is after 31st December.

In the third quarter meeting which again has to be held within 45 days from the end of the 31st December say within 14th of February. In that meeting they declared interim dividend same. When the interim dividend is declared there has to be a closure of trading window. The moment our intubation goes you close the trading window, but again the question comes before closing the period that is the red zone, I call it.

That is that zone when you have not told to close the window but you are aware of, you cannot say we are not aware of. Now you prove you are not aware of, if you have traded in that shares same for final dividend, issue of shares by public rights and bonus is another trading restrictions. Major expansion programs I have already discussed. Marginal amalgamation I have discussed, disposal of whole or substantial whole of the undertaking again you do not dispose whole of substantial, whole of the undertaking selling and undertaking overnight.

There is a preparedness for that, there is a discretion for, that there is a deliberation for that, there is a due diligence for that and that takes months, months and months and who is privy to that? The boards of directors are privy to that. Now the board of directors cannot say we were not privy to that, you are very much aware that this is going to happen the company is going to sell that undertaking; you sold all your shares when the prices were high.

And you made huge profit, it has happened, a live example is there in a big company and that director was caught, penalized fine, he sold of the shares having distinct information the company is selling and undertaking and knowing fully well the share prices will nose dive, he sold the shares when the prices were quite high and made good money. Whereas, the poor investors, the retail investors came to know much later when the prices were low, they could not even sell the shares because there are no buyers, you can only sell the shares in the market provided there is a buyer.

People say I can make, I can sell the shares, I can buy the shares, you can neither sell the shares, you can neither buy the shares unless there is corresponding seller or the buyer. So, it is a meeting of minds. So, this gentleman sold the share smartly having this piece of information, any changes in policies plans or operations of the company who comes to know? This designated employee comes to know first.

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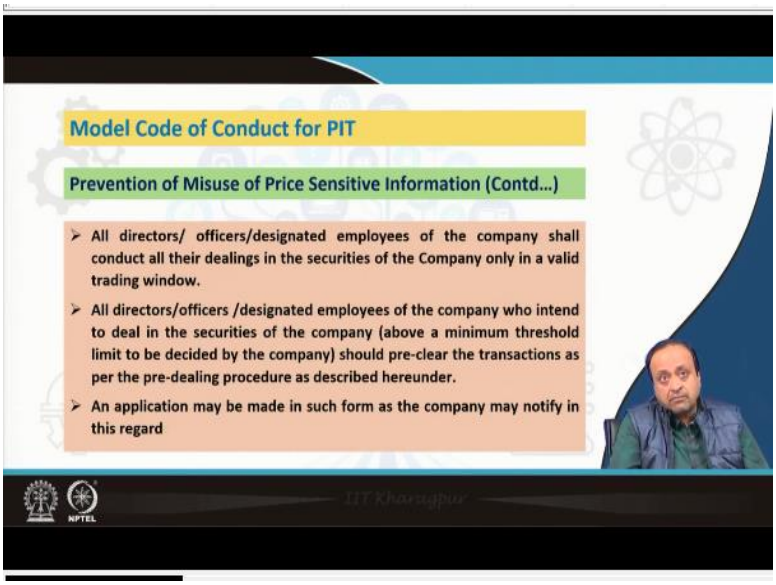


So, prevention or misuse of price sensitive information is one of the areas which semi-insider trading requires a regulation is looking at. Applications are made to the company for pre-clearance; permission is taken from the company to trade the shares.

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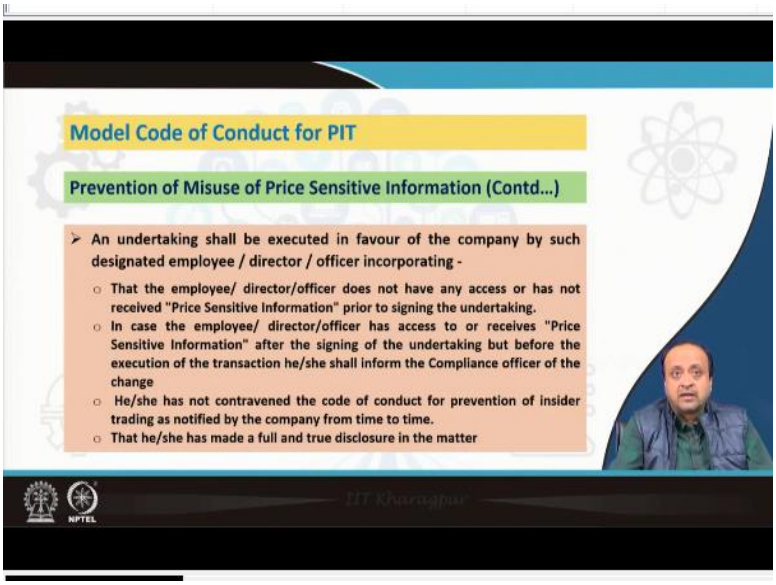


Disclosure undertaking in favour of the company by such decision employees are always taken that he has not done it, as I say yearly annual ritual, where he has to write that he has not traded, he has not done any violation of insider trading regulations because it will not be possible for the company to know whether he has really bought and sold the shares or if Keith and Keen has sold the shares if it does not disclose. SEBI can track for the company is difficult to track, in fact.

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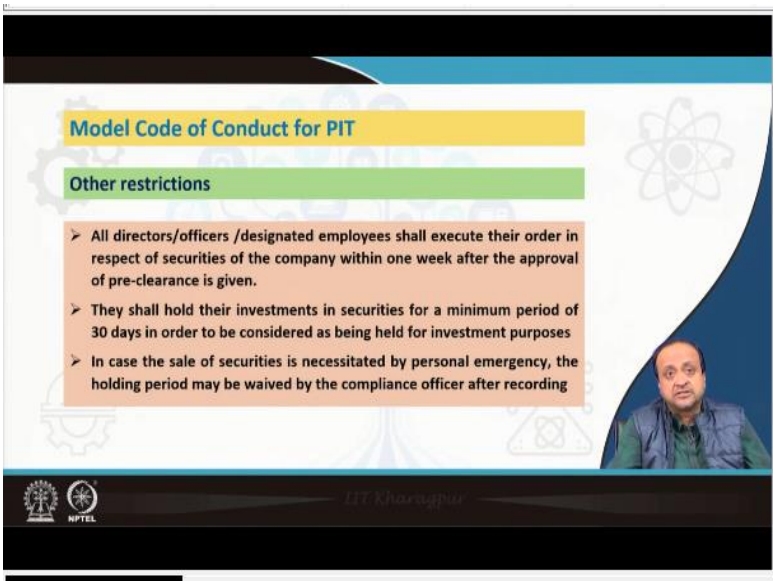


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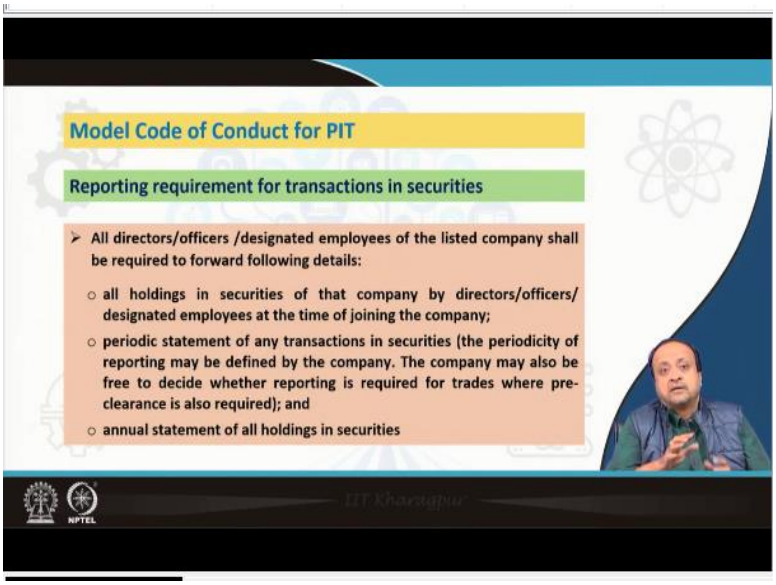


They cannot report requirements, annual statement of all holdings and securities, periodic statement of buying and sell. All holding securities of the company directors at the time of joining.

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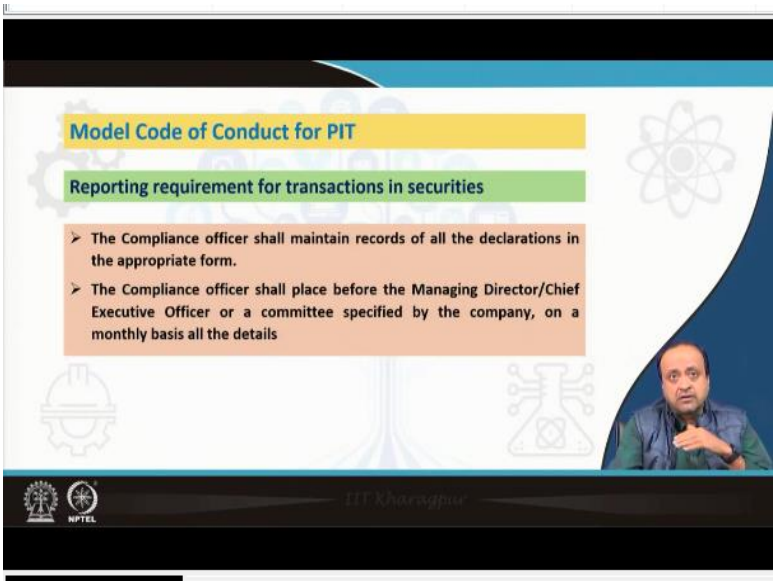


These are all regular routine compliances, responsibly goes to the compliance officer to ensure that it is done. Any annually he has to report to the audit committee and the risk management committee.

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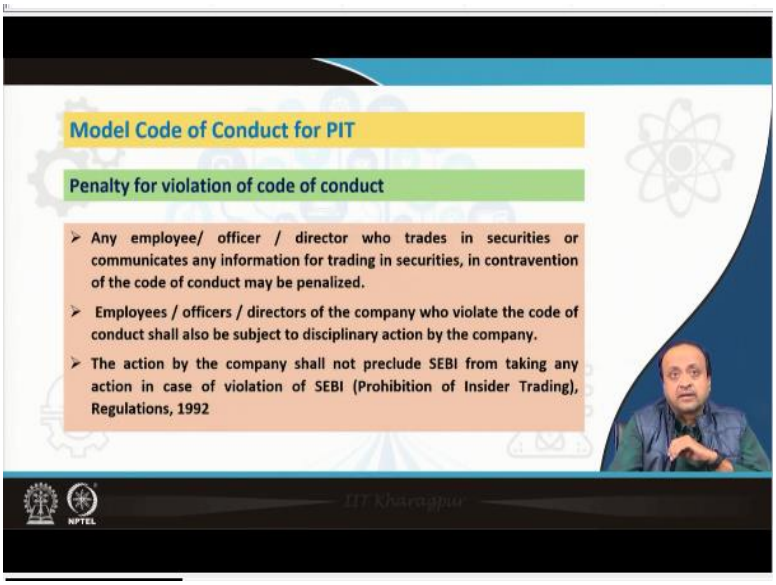


Penalty is huge, all employees' directors who trade in shares conservation and securities so they may be penalized.

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And sometimes the penalty is so high that companies ask the employees whether they would like to continue or not? It is better that they discontinue, penalties imposed by SEBI for violations are extremely high, company model code of conduct leaves it to the companies to do that, some of the companies have levied, some of the companies have given warnings first offenses. Most companies do that unless he has made a huge profit in the very first offense.

If he has made a loss in the first offense normally it is waver, but if it is repetitive then the penalty is so high it is better for the employee to leave and with the conditional undertaking.

That in case SEBI puts any blame on the company for this the entire thing has to be paid by him, that kind of undertaking is taken from him.

He may join, he may go, he may be paid his dues also, but with a clear undertaking if SEBI imposes fine on the company, it will be borne by him. So, these are some of the references that I have taken, but if you can to go through my lectures you will find mostly it comes from my experiences and interactions in different forums. But these are definitely some of the references that I have taken.

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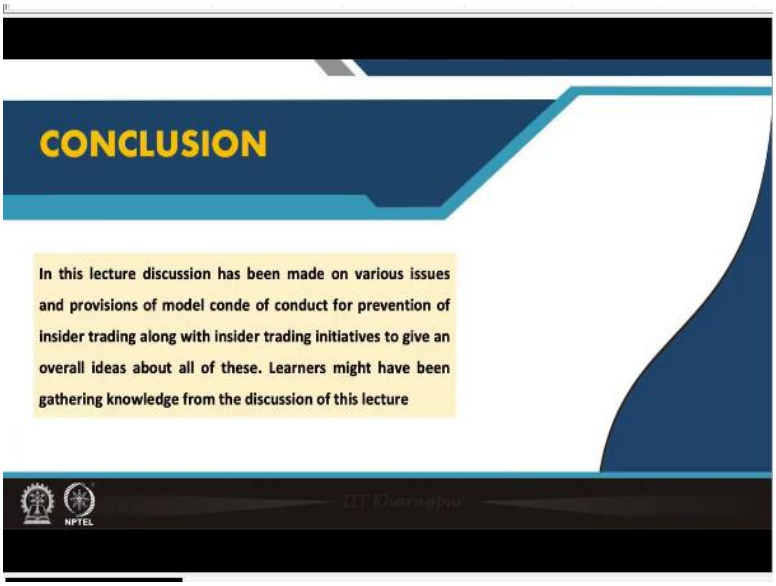


Thank you so much, wish you all a very good time ahead, thank you.