



Mechanism to Prevent Insider Trading

The Securities and Exchange Board of India (SEBI) has prescribed internal controls on sharing of information.

- It has decided to **hold company promoters**, irrespective of their shareholding status, **responsible for violation of insider trading norms** if they possess **unpublished price-sensitive information (UPSI)** regarding the company without any 'legitimate' purpose.
- SEBI has specified that the term **"legitimate purpose"** will include **sharing of the UPSI** in the ordinary course of business by an insider with partners, collaborators, lenders, customers, suppliers, merchant bankers, legal advisors, auditors, insolvency professionals or other advisors or consultants, provided that such sharing has not been carried out to evade or circumvent the prohibitions of these regulations.
- Simply put, a promoter who is not an advisor in official capacity or does not hold any position on the board will not be considered a person having **"legitimate purpose"** to hold the UPSI.
- It has recommended that the board of directors shall **ensure that a structured digital database** is maintained containing the names of such persons or entities, as the case may be, with whom the information is shared.
- SEBI's decision is based on the recommendations of the **TK Viswanathan committee on fair market conduct**.

Insider Trading

- Insider trading refers to the **practice of purchasing or selling** a publicly-traded company's securities while in possession of **material information that is not yet public information**.
- Material information refers to any and all information that may **result in a substantial impact on the decision of an investor** regarding whether to buy or sell the security. E.g.:
 - A government employee acts upon his knowledge about a new regulation to be passed which will benefit a sugar-exporting firm and buys its shares before the regulation becomes public knowledge.

Corporate Governance

- Corporate governance is the system by which **companies are managed and controlled**. It involves a set of systems, processes and principles which ensure that a company is governed in the **best interest of its stakeholders**.
- **'Good corporate governance'** ensures:
 - Adequate **disclosures** and effective **decision making** to achieve corporate objectives.
 - **Transparency** in business transaction.
 - Statutory and legal **compliances**.
 - **Protection** of shareholder interests.
 - Commitment to **values** and **ethical conduct** of business.
- The **Global Financial Stability report** recently published by the **International Monetary Fund (IMF)** suggests that while corporate governance norms have improved across emerging markets, **it fell in India between 2006 and 2014**.

- **Recent initiatives** to improve corporate governance:

Kotak Panel report

- The panel constituted by **Securities and Exchange Board of India (SEBI)** under the chairmanship of **Uday Kotak** has suggested a host of changes for improving corporate governance standards of firms.
- **Chairman** of the board **cannot** be the **Managing Director/ CEO of the company**.
- Boards should have minimum **of six directors**. Of these 50% **should be independent directors** including at least one woman independent director.
- Mandate minimum qualification for independent directors and disclose their relevant skills.
- Create a formal channel for sharing of information between the company and its promoters.
- Public sector companies should be governed by listing regulations, not by the nodal ministries.
- Auditors should be penalized if lapses are found.
- SEBI should have powers to **grant immunity to** whistle blowers. Companies should disclose medium-to-long term business strategy in annual reports.

The recommendations of **TK Viswanathan committee on fair market conduct** which submitted its report in August, 2018 are:

- Among a number of recommendations on **insider trading**, is the creation of **two separate codes of conduct**.
 - Minimum standards on dealing with insider information by listed companies.
 - Standards for market intermediaries and others who are handling price-sensitive information.
- Companies should maintain details of immediate relatives of designated persons who might deal with sensitive information and of people with whom the designated person might share a material financial relationship or who share the same address for a year.
- **Such information** may be maintained by the company in a searchable **electronic format**. It may also be shared with the SEBI when sought on a case-to-case basis.
- The committee has recommended **direct power for SEBI to tap telephones** and other electronic communication devices. This is to **check insider trading** and other frauds.
 - Currently, SEBI has the **power to only ask for call records** including numbers and durations.

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