Transparency and Insider Trading during COVID-19
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Insider Trading During COVID 19: Opportunity Amidst a Crisis

The novel coronavirus is moulding the securities market in unique and unprecedented ways. Currently, the corporate world is facing financial upheaval. In this time of economic uncertainty, opportunity and intention to engage in COVID-19-related insider trading has increased significantly. It poses as a profitable opportunity for traders, especially those who have insights into the impact of the prevailing state of affairs in listed companies.

Such information about key performance standards, like financial transactions, business disruptions, material contracts, mergers or acquisitions, etc., would allow an individual who is an avid part of such setup to foresee and anticipate unexpected benefits and hence plan their trading and make allocation decisions efficient. This, in turn, will impact the investors in general who are unaware of any such developments in the market at large.

Though SEBI has recently come out with a series of relaxations on filing requirements by listed companies in light of the COVID-19 pandemic, it would be interesting to witness how the industry copes up with the strict contours of trading restrictions under the latest insider trading regime[1].

The existence of a fair, vibrant and efficient securities market is one of the essential ingredients for the economic growth of a country. To instil confidence, trust and integrity in the securities market, the market regulator needs to ensure fair market conduct and it can be ensured by prohibiting, preventing, detecting and punishing such market conduct which leads to ‘market abuse’.

Market abuse is generally understood to include market manipulation and insider trading, as such an activity which erodes investor confidence and impairs economic growth. Therefore, it is of utmost importance to have certain regulations governing the security market in order to ensure that no person gets undue profits from trading on some price-sensitive inside information of the company which has not been put into the public domain.

After the recent amendment, the SEBI (Prevention of Insider Trading) Regulations, 2015[2] (“PIT Regulations”) was introduced to curb the peril of insider trading in India. The motive behind this is to provide a fair chance to all the investors regarding the market and its functionaries.

The primary objective of PTI Regulations is to prohibit the trading in the listed securities of a company based on its Unpublished Price Sensitive Information (“UPSI”) by those persons who are aware of the internal workings of the company, also known as “insiders”, and ensuring adequate disclosures in the market place of price sensitive information of the company and its securities.

In order to achieve such objectives, the concept of trading window norms was introduced in the code in respect of employees or connected persons or designated person and their immediate relatives, in the organization. The trading window is to be closed when such related or designated persons can reasonably be expected to possess unpublished price sensitive information. During such a closure period, no trading shall be permitted by such persons.

In accordance with the circular issued by SEBI dated June 30, 2020[3], the financial results were extended till July 31, 2020, in order to provide relaxations from the compliance requirements during Covid-19. Therefore, the problem is further aggravated by the fact that the trading window closures will be automatically get delayed for another two months unless those are specifically exempted by the regulators. Many companies would take advantage of the SEBI’s decision of extension of filling of compliances as their corporate insiders likely will have access to crucial business information and the ability to trade on such material corporate information for an extended time before that information is made available to investors.

Further, company insiders are likely to have non-public price sensitive information not only regarding how COVID-19 might impact their own companies’ financials but also regarding how the pandemic might impact other entities, including customers, vendors, merchants and other third parties with which their companies interact on a regular basis. Considering the severe impact that COVID-19 has had on virtually all industries, much of the price-sensitive information regarding its impact is likely to be material. Together, these factors create unique and unprecedented opportunities for insider trading.

In India, insider trading is a strict liability offence and the PIT Regulations prohibit selective communication of any UPSI and also penalize trading whilst in possession of such information. In furtherance to avoid such a situation, SEBI has adjured listed companies to formulate a code of conduct, blackout periods, pre-clearance mechanisms wherein any person having access to such data, and using it for profits or improper gains could be penalized. This will facilitate SEBI to keep a check on the market activities and in the protection of their financial and other sensitive information.

In recent years, the security market watchdog has also stepped up enforcement and investigations, using technology to enhance surveillance of what is often a difficult transgression to clamp down on. However, Covid-19 will undoubtedly pose unique challenges to the security market watchdog on this front. Although the listed companies are required to make disclosures of material events leading to any such situation of insider trading, it will be a practical challenge to quantify or meaningfully articulate the potential impact of such a dynamic crisis on shareholders.

Finally, the Security market regulators took all these crucial factors into consideration and an amendment vide circular No. SEBI/LAD-NRO/GN/2020/23[4] was brought under Regulation 3 of the PIT Regulations. The regulation deals with the communication or procurement of price-sensitive information in which sub-section 5 was substituted with regulations including maintaining a structured digital database containing the nature of unpublished price sensitive information and the names of persons who have shared such crucial

internal information.
Also, there are certain relaxations provided to the stakeholders through the automation of the process of filing disclosures to stock exchanges, restriction on the trading window not to be made applicable for transactions as prescribed by SEBI. Entities are required to file the non-compliances of code of conduct with the stock exchanges and amounts if any collected for such non-compliances shall be credited to the Investor Protection Education Fund administered by the Board as per the SEBI PIT Regulations.
Since the pandemic and the measures to combat it are evolving rapidly, the plausibility of investor’s communication and investments will naturally be hampered. Consequently, the assessment of whether any information actually comprises of "price sensitivity" or not, can never be a technical one. When it comes to the personal trades of the directors, key managerial personnel, or promoters trading in the company’s stocks, have to ensure they abide by the code of conduct of the company.
However, the code of conduct shall stipulate the sanctions and disciplinary actions, including a wage freeze, suspension, recovery, etc., that may be imposed, by the listed company required to formulate a code of conduct under sub-regulation (1) of regulation 9 of the Act, for the contravention of the code of conduct.
Risk in work from home set up
The concept of working from home and remote workforces is not a contemporary concept, it has always been there. However, with the unforeseen circumstances of Covid-19, wherein most of the organizations are suddenly forced to practice this work from home culture, this has certainly opened doors for the increased possibility of a hike in information leakages and breaches targeting business arena.
Now that Board meetings have gone digital due to the current pandemic, incidental persons like IT professionals involved indirectly in such meetings, are considered to be in possession of any price-sensitive information which could be discussed in such business meetings and they should be taken under the purview of the insider trading PIT regulations of SEBI. They are very much on a pedestal as they can use such information for unfair trade and gains against the public or investors in general. In such circumstances, the possibility of "accidental" tipping is bound to arise, since the work from home environment will naturally create headroom for information leakage and questionable employee conduct.
The security market regulator should come up with additional stringent guidelines, which will regulate these individuals who receive such price sensitive information of a company’s business transactions which can affect the investor’s interest in the market in general.
In an effort to stroll the tide of the pandemic and soften its impact, the government has taken appropriate measures and has issued orders placing restrictions on and providing relief for businesses and individuals. Altogether, these restrictions and relief actions have increased significantly both the opportunity and motive for individuals to trade on material non-public corporate information, thereby heightening the risk that companies might require to subject themselves to government investigations or SEBI enforcement actions related to COVID-19 insider trading.
Keeping a check on Insider Trading during COVID 19
The corporates in order to protect themselves from the threat of SEBI

investigation for insider trading or any enforcement action should take all kind of precautionary measures such as evaluating their internal controls and revising the insider trading policies of the organization, and ensure that these policies are clearly demarcating the prohibition of trading on material price sensitive information, and adequately addressing the increasing possible opportunities for such trading that might have been created due to the pandemic. This would require corporates to revise their other supplemental policies in light of their current business practices.

Not only revising policies but also, the companies must ensure that the employees' are aware and abiding by such policies strictly. Further, companies should consider disseminating to their workforce clear advisory communications to remind employees of their obligation to refrain from sharing or trading on material sensitive information which are not available to the public in general and that they received through their employment in such organization.

Considering the ease with which information may be disseminated among family members in a quarantine environment, company directors, officers, and employees and all stakeholders should be reminded of the substantial risks associated with insider trading, and best practices for protecting confidential information during the quarantine.

Also, now that the security market regulator has come up with such proactive, detailed regulations, it would be interesting to witness if that would set the standards up for expected market conduct. SEBI has considered the interest of the investors as well as the stakeholders and has cut some slack over stringent insider trading rules amidst the COVID-19 condition to make it easier for companies to raise capital from the market. However, the regulator has also instructed the companies to maintain a structured record regarding all unpublished price information and details of people who have access to it.

- [1] https://www.sebi.gov.in/legal/regulations/jan-2019/securities-and-exchange-board-of-india-prohibition-of-insider-trading-regulations-2015-last-amended-on-january-21-2019-_41717.html
- [2] https://www.sebi.gov.in/legal/circulars/jun-2020/relaxation-in-timelines-for-compliance-with-regulatory-requirements_46967.html

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