

## **Insider Trading Laws and Market Fairness**

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### **ABSTRACT**

Insider trading is one of the most critical challenges faced by modern securities markets. It involves buying or selling securities based on unpublished price-sensitive information (UPSI), giving an unfair advantage to individuals who possess privileged access. This paper examines the concept of insider trading, its impact on market fairness, and how India—led by the Securities and Exchange Board of India (SEBI)—has developed regulatory safeguards over time. The research thoroughly assesses SEBI Regulations (2015), important case laws, comparative international practices, and weaknesses that still affect enforcement. It argues that stronger surveillance mechanisms, quicker investigation processes, and improved corporate governance are essential to maintain the integrity of the market. The paper concludes that investor trust and fairness can be strengthened only when insider trading laws are implemented rigorously and consistently.

### **KEYWORDS**

Insider Trading, SEBI Regulations, Market Fairness, UPSI, Securities Market, Corporate Governance, Investor Protection.

### **1. INTRODUCTION**

A fair and transparent securities market is essential for economic stability and investor confidence. Investors participate in trading activities with an expectation of equal access to information. When certain individuals exploit confidential information for their personal benefit, the balance of fairness is disrupted. This misuse of unpublished price-sensitive information gives rise to insider trading.

Historically, insider trading has been one of the most difficult forms of market manipulation to detect and regulate, because the information flows privately and informally within companies. Directors, executives, auditors, lawyers, analysts, employees, and connected persons often gain access to UPSI through their position. When such information is used before it becomes public, they gain an unfair advantage over ordinary investors, thereby undermining the health of the market.

India has taken significant steps to regulate insider trading, especially through the SEBI Act, 1992 and SEBI (Prohibition of Insider Trading) Regulations, 2015. These regulations attempt to clearly define "insider," "connected person," and "UPSI," along with imposing restrictions on trading activity and obligations for maintaining confidentiality.

Insider trading is not just an economic crime—it is also an ethical issue. A market that allows insider trading cannot be trusted, and without trust, investors hesitate to participate. In such a scenario, capital formation suffers, and overall economic growth is weakened. Therefore, studying insider trading laws and their impact on market fairness is essential for ensuring a strong and transparent financial system.

## **2. RESEARCH METHOD**

The methodology adopted for this research is doctrinal, analytical, and comparative. It includes:

### **2.1 Doctrinal Method**

The study relies on an examination of statutory provisions, SEBI regulations, case laws, and official guidelines. The legal texts form the foundation of understanding how insider trading is defined and regulated in India.

### **2.2 Secondary Sources**

The research uses secondary materials such as textbooks on securities laws, commentaries, research articles, and journals related to market regulation. Reports issued by SEBI, NSE, BSE, and international market regulators have been used for analysis.

### **2.3 Case Study Approach**

Important cases such as the Hindustan Lever Limited (HUL) case, the Rakesh Agrawal case, and the Samir Arora case have been examined to understand judicial interpretation and enforcement issues.

### **2.4 Comparative Analysis**

The Indian framework is compared with international practices—especially regulations enforced by the US Securities and Exchange Commission (SEC), the UK Financial Conduct Authority (FCA), and Singapore Exchange (SGX).

## **3. RESEARCH SCOPE**

### **3.1 Review of Literature**

Several scholars and economists have studied the adverse effects of insider trading. Literature suggests that markets become efficient only when all investors have equal information. Insider trading distorts price discovery mechanisms, causes unfair gains, and leads to a loss of investor confidence. Researchers also argue that strong surveillance and stringent laws improve market

fairness. Many publications highlight that Indian markets have improved significantly after the introduction of SEBI Regulations, but enforcement challenges persist.

### **3.2 Research Gap**

Despite strong laws, insider trading continues in India because:

- UPSI communication often occurs informally and is hard to trace.
- Proving intent behind trades is legally challenging.
- SEBI investigations sometimes face delays.
- The burden of proof is difficult in complex corporate structures.
- Surveillance technology needs further strengthening.

These gaps indicate a need for deeper analysis and stronger enforcement mechanisms.

### **3.3 Hypothesis**

Effective implementation of insider trading laws significantly improves market fairness and increases investor confidence.

### **3.4 Objectives of the Study**

1. To understand the concept of insider trading and its effect on the market.
2. To examine SEBI's legal framework and enforcement mechanisms.
3. To analyze important case laws.
4. To evaluate how insider trading impacts fairness and transparency.
5. To suggest measures to strengthen insider trading laws in India.

## **4. MEANING OF INSIDER TRADING AND KEY CONCEPTS (HEADING 14)**

### **4.1 Insider Trading**

Insider trading refers to buying, selling, or dealing in securities by individuals who possess unpublished price-sensitive information. It involves taking advantage of information that the general public does not have access to.

### **4.2 Insider**

An insider includes:

- Directors, officers, promoters
- Immediate relatives of insiders
- Employees of the company
- Connected persons who have access to UPSI

### **4.3 Unpublished Price-Sensitive Information (UPSI)**

UPSI includes information relating to:

- Financial results
- Dividends
- Mergers and acquisitions
- Changes in capital structure

- Key managerial changes
- Any major policy decision affecting share value

#### **4.4 Connected Person**

A connected person is someone who is associated with the company in any capacity and is reasonably expected to have access to UPSI.

### **5. INSIDER TRADING IN INDIA: LEGAL FRAMEWORK**

#### **5.1 SEBI Act, 1992**

Gives SEBI the authority to regulate securities markets and prevent unfair trade practices.

#### **7.2 SEBI (Prohibition of Insider Trading) Regulations, 2015**

These regulations strengthened the definition of UPSI, introduced stricter reporting obligations, and imposed penalties for violations.

#### **5.3 Key Features of 2015 Regulations**

- Clear definition of insider and UPSI
- Code of Conduct for companies and intermediaries
- Trading window restrictions
- Pre-clearance of trades
- Maintenance of structured digital databases
- Stronger investigation and enforcement powers

### **6. IMPACT OF INSIDER TRADING ON MARKET FAIRNESS**

Insider trading has severe consequences:

1. Destroys investor trust
2. Reduces participation in the market
3. Unfair advantage to a few individuals
4. Distorts share prices
5. Damages the reputation of capital markets
6. Affects long-term economic growth

A market cannot be considered fair if some investors always have better information systems than others.

### **7. CASE LAWS ON INSIDER TRADING IN INDIA**

#### **7.1 Hindustan Lever Limited (HUL) Case (1998)**

SEBI alleged that HUL used UPSI in its purchase of shares of Brooke Bond Lipton India Ltd. Although the case was complex, it established early guidelines on information misuse.

### **7.2 Rakesh Agrawal vs. SEBI (2003)**

Agrawal, the Managing Director of ABS Industries, was accused of insider trading during a takeover. The Tribunal held that although UPSI was used, his intention was not personal profit. The case highlighted the role of *mens rea*.

### **7.3 Samir Arora Case**

A prominent fund manager accused of insider trading. SEBI banned him, but later the SAT overturned most findings. The case exposed challenges in proving information flow and intent.

## **8. COMPARATIVE INTERNATIONAL PRACTICES**

### **8.1 United States (SEC Regulations)**

The US has the strongest insider trading laws. SEC uses:

- Advanced surveillance
- Heavy monetary penalties
- Criminal prosecution

### **8.2 United Kingdom (FCA Regulations)**

UK laws focus on market abuse as a whole, not just insider trading. Strong whistle-blower protection exists.

### **8.3 Singapore (SGX Model)**

Known for some of the strictest penalties and efficient enforcement.

### **8.4 Lessons for India**

- Faster investigations
- Criminal prosecution in major cases
- Protection for whistle-blowers
- Greater technological surveillance

## **9. CHALLENGES IN ENFORCEMENT**

1. Difficulty in tracing UPSI communication
2. Informal information channels
3. Complexity of corporate structures
4. High burden of proof
5. Delay in investigation
6. Limited resources for surveillance
7. Use of family members for trading
8. Cross-border trading issues

## **10. FINDINGS OF THE STUDY**

- Insider trading continues despite strong laws.

- Enforcement needs greater speed and transparency.
- Market fairness improves when insider trading is minimized.
- Technology-driven surveillance is important.
- Investor confidence depends on consistent enforcement.

## **11. CONCLUSION & SUGGESTIONS**

### **11.1 Conclusion**

Insider trading is harmful not only to individual investors but to the entire financial system. Strong laws are necessary, but they must be backed with effective enforcement. SEBI has made major progress, especially after the 2015 Regulations, but challenges remain. Ensuring market fairness requires continuous improvement in technology, governance, and regulatory oversight.

### **11.2 Suggestions**

1. AI-based surveillance systems to track suspicious trades.
2. Stricter penalties to deter violations.
3. Fast-track investigation mechanisms.
4. Mandatory digital trail for UPSI.
5. Stronger whistle-blower policy.
6. Regular training programs for company employees.
7. Greater international cooperation.
8. Better investor awareness programs.

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