

MS. SHIVANI GUPTA & ORS. v. SEBI

Civil Appeal No.7054/ 7590 of 2021

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INTRODUCTION

This is an appeal decided by a Bench of Hon'ble JJ. Vineet Saran & Aniruddha Bose at Supreme Court of India against a judgement and order of Securities Appellate Tribunal (hereinafter "SAT").

This case relates to insider trading of securities in a matter of renowned body corporate PC Jewellers Ltd. The matter of Insider trading in securities is so sensitive and serious issue in corporate affairs that it carries criminal liability under Companies Act, 2013¹ as well as Securities Exchange Board Act, 1992. Actually the legislative objectives behind restricting, prohibiting and regulating 'insider trading' is that the public money invested in the securities of public limited companies may not be put at risk by the promoters and management of Companies. The simple idea of securities insider trading is that people engaged with the management of the companies' affairs may not be allowed to manipulate the selling-purchasing of different types of shares, stocks or debenture securities by causing artificial prices' ups and down in the security market.

The reason behind controlling the relation, intention and behaviour of companies' promoters or managers is that the reflection of financial flows of company should be maintained by security market's demand and supply rules only rather by interested stakeholder's calculative manipulation for their own personal interests. If insider trading would not be regulated, under law, incorporation of a company may be turned to be a tool to befool public. And; such frequent practices will damage the public trust dissuading them not to invest their money into public limited companies. Therefore, the Securities Exchange Board of India [SEBI], an authority has been established through a legislation called 'Securities Exchange Board of India Act, 1992' and further a separate regulation called SEBI (Prohibition of Insider Trading) Regulation, 2015 that regulates all issues relating to insider trading.

¹ . Section 195 of Companies Act, 2023.

The impugned case is very pertinent from the insider trading perspectives. Two major legal contentions have been raised in this case. The first contention relates to the interpretation of the term “connected person” defined under section 2(1)(d)(i) and second is “insider” under section 2(1)(g) of the SEBI (Prevention of Insider Trading Regulations), 2015 [hereafter “PIT Regulations”].

The core factual contention of SEBI’s argument in this case is that three close relatives (hereafter referred as “relatives”) of a listed company i.e. *PC Jeweller Ltd. Co.* chairman and managing director traded in shares of the impugned company based on certain undisclosed and unpublished price sensitive information (UPSI) which was allegedly obtained from the chairman and managing director and hence ‘insider trading’ was contended in this case. Such allegations were made by SEBI that the Chairman and Managing Director of the company communicated UPSI to the appellant in violation of the SEBI Act and SEBI (Prohibition of Insider Trading) Regulations, 2015. SEBI alleged that the way appellant invested in the impugned company’s security; is based on the information passed by alleged parties to their relatives that is Son and daughter-in-law.

BACKGROUND

The *P. Chand Jeweller Pvt. Ltd.* was initially established and incorporated as a Private Limited Company in 2005 but later on through a resolution in 2011 passed by shareholders; it was turned to be a Public Limited Company i.e. *PC Jeweller Ltd.* (hereafter ‘PCJ’).

The present dispute arised from an order² dated 17.12.2019 of SEBI against appellants and issuing a show cause notice dated 24.04.2020. The allegations made in the impugned SEBI order as well as show cause notice were as follows that, “Padam Chand Gupta (P.C. Gupta) was the Chairman of PCJ during the relevant period and was a ‘connected person’ in terms of Regulation 2(1)(d)(i) and an ‘insider’ under Regulation 2(1)(g) of the SEBI (Prevention of Insider

Trading Regulations), 2015. Balram Garg, who is the brother of P.C. Gupta and the Managing Director of PCJ is also a ‘connected person’ in terms of Regulation 2(1)(d)(i) and an ‘insider’ under Regulation 2(1)(g) of the PIT Regulations, 2015.³”

The allegation was made that appellant in Civil Apl. No.7590/2021, namely, Sachin Gupta, Shivani Gupta and Amit Garg traded in securities in pursuance of an ‘Unpublished Price Sensitive Information’ (for short ‘UPSI’) received from P.C. Gupta and Balram Garg between the time span of 01.04.2018 to 31.07.2018 who were their close relatives by blood. This allegation was made because Sachin Gupta and Smt. Shivani Gupta was the son and daughter-in-law of Balram Garg’s deceased brother of late P.C. Gupta. Moreover, Amit Garg is the son of Amar Garg, who was also the brother of Balram Garg. It was also alleged that all the appellants were residing in the same households.

Insiders are prohibited from trading in securities or stocks during the possession of unpublished price-sensitive information which is material or potential to influence the market of securities during that period with such information.⁴

An ‘insider’ of a company means an individual who possesses such securities price sensitive information is not permitted to share or even mention it to anybody else⁵. Any individual may be held as ‘insider’ of a company with respect to ‘securities/shares trading’ under two circumstances as given under Regulation 2(1)(g) of SEBI PIT Regulation, 2015.

The first one is; when someone who is or was directly ‘connected’ with the company or has ties/ dealing with the business of the company in such a way that provides her/him access to UPSI with respect to any particular issue of shares or stocks. And, another situation wherein an individual who has access to or possession of UPSI of such company is also amounts to be an insider. The provisions defining an ‘insider’⁵ reads as such, “an ‘insider’ means any person who is: a connected person; or in possession of or having access to unpublished price sensitive information.” Here, the term which is crucial to understand ‘insider trading’ is ‘connected person’.

2 Judgment Copy available on https://www.sebi.gov.in/enforcement/orders/apr-2022/judgment-of-the-hon-ble-supreme-court-in-civil-appeal-no-7054-of-2021-balram-garg-vs-sebi-and-civil-appeal-no-7590-of-2021-ms-shivani-gupta-and-ors-vs-sebi_59462.html Page No. 2, Para-2.

3 .Ibid

4 Section 12-A (e) of the SEBI [PIT] Regulation Act, 2015

5 .Section 2(e) of the Securities and Exchange Board of India ([prohibition of Insider Trading) Regulations, 1992



Section 2(1)(d) of the SEBI PIT Regulations, 2015 defines the term 'connected person' as such, "a 'connected person' includes any individual as connected person in matters of insider trading of securities of any listed company who is an individual associated with alleged company at any time during last six months prior to the alleged trading or an immediate relative in the holding/associate/subsidiary company of such impugned company or any office of stock exchange, clearing corporation, any Banker of the company, any concern, firm, trust, HUF, company or any association of persons wherein above said individual having interest or holding more than 10% legal consultant, auditors and other person having direct or indirect interest with such company."

The Chairman as well as MD of a company is insider person since they have a close connection to the business management and financial decisions. The general assumption is that they possess UPSI, unless contrary is proven. They are not permitted to use UPSI in trading or to reveal UPSI to third parties. The Chairman and the Managing Director are accused of communicating the UPSI to their immediate family members or relatives in abeyance of the legal regulations against insider trading. Whether a person is 'immediate relative' or not under PIT Regulation of 2015, lastly amended in 2021, the parameter to ascertain has been given in this regulation. It reads as, "if a person is of spouse, parents, kids of the other or financially dependents on 'connected person' or seeks advices of connected persons while trading in shares, shall be amounts to be the immediate relative for the purposes of insider trading under the SEBI PIT Regulation, 2015.⁶ Therefore, it can be said that whether UPSI has been pass on to close/direct relatives like wife/husband, parent, kids, siblings or not, if they are found to have trading in connection with any UPSI, they should be treated immediate relatives immaterial of whether they are financially dependent on the insiders or not. Second, even if they do not meet the definition of immediate relatives, a relative acquires insider status if they own UPSI.

6 .Section 2(c) of the Securities and Exchange Board of India ([prohibition of Insider Trading) Regulations, 1992.

ANALYSIS

With reference to the aforementioned legal provisions, the Hon'ble Supreme Court of India observed that SEBI was supposed to prove that the Chairman and the Managing Director informed their family members about UPSI before charge them under the said regulation of 2015. In reference to the term 'relatives', according to the said regulation, SEBI had to prove that either both of the parties were 'close family members' or they traded while in possession of the UPSI. To put it another way, SEBI accusation may sustain against the relatives only if SEBI could prove beyond reasonable doubts that they were close relatives or connected persons even though there was no concrete proof that they had exchanged any UPSI.

The Chairman and Managing Director, on the other hand, tried to prove that they did not inform the families about any UPSI. Similarly, the family members attempted to prove that neither they were immediate family members as per the legislative requisite nor they possessed any UPSI. The impugned order of SEBI is not supported by any evidence.

Two pieces of information in this situation meet the criteria for UPSI. The first is the business's choice to repurchase its shares. The second; the alleged UPSI is the withdrawal of the buy-back offer due to the lead bank's failure to provide a no-objection certificate. The accusation was that while they were in possession of UPSI, the family or their accomplices traded in the company's stock.

The trading behaviour and timing of the relatives served as the foundation for the accusations. Before the buy-back announcement, one of the cousins was offering to sell the company's shares for lesser value. However, she ceased selling the shares; before the buy-back offer was announced, protecting herself from losses. She once more sold her shares before the buy-back option was withdrawn, protecting herself from a loss. Additionally, a business owned entirely by two of the relatives had a short position with regard to the company's shares right before the buy-back offer was withdrawn in order to profit from the decline in share price following the withdrawal. Other than these facts, SEBI lacked to prove by any letter, emails or eyewitnesses that the alleged 'connected persons' informed their family members about UPSI.

The Supreme Court determined that the aforementioned facts are insufficient to support the charges of insider trading in securities. The court held that it was SEBI's responsibility to substantiate both the fact that the Chairman and Managing Director spoke with the relatives often and their physical possession of the UPSI. The timing and pattern of their trading did not amount enough circumstantial evidence to prove them guilty for insider trading in securities.⁷

It was essential that SEBI confirm the communication with and ownership of UPSI by way of convincing evidence, such as letters, emails, or witnesses. The relatives in question do not meet the definition of immediate relations. The Chairman, the Managing Director, and the relatives were ruled to be alienated by the court. In addition, the family members had left their jobs at the business. The relatives made their judgments on their own, without consulting the chairman or the managing director because they were financially independent. Because of this, relatives are not considered to be immediate relatives (and hence they themselves are not connected persons). Therefore, it cannot be assumed that they have the UPSI. They had to have had UPSI on them when they traded, and the SEBI had to prove it with convincing proof.

CONCLUSION

It seems that a “*new standard of proof*” has been developed through this judgment in the matters of insider trading cases. It is not entirely unreasonable for the court to anticipate that a person should not be held guilty of insider trading just because s/he having family connection but long time gapping in interaction and not sharing common households. The level of proof that applies to close relatives will not be affected by this ruling. They will be given the same treatment as connected person under SEBI PIT, 2015 and be assumed to have UPSI. However, in the eyes of others, timing and trading patterns alone are insufficient to demonstrate ownership of UPSI. Unless there is proof that the UPSI was really communicated, the connected parties will not be held guilty for communicating UPSI.

7 .Page No. 29, Para-24 of the SC Judgment [Balram Garg vs. SEBI, civil-appeal-no-7590-of-2021]

But, the other side of this judgment reflects that it would not be difficult for wrong doers to establish that they had no connection in the matters of securities trading with the insiders. Actually insider trading of securities is a highly subtle and sensitive issue under corporate affairs. The judiciary should not only adopts the literal interpretation of legislation in such circumstance rather should go through the purposive interpretation of the legislation and for that matter court should also consider the circumstantial evidence of transaction, timing and pattern of trading. It won't be difficult for the violators to make sure that there is no such material or witness if the court is seeking for material proof, such as written communication or witnesses who can directly attest the communication of UPSI between immediate relative and insiders. Finding such tangible proof to support the real communication of UPSI becomes much more difficult when the tipper and the tippee are close friends or family members.

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