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INSIDER TRADING DURING PANDEMIC TIMES – AN INDIAN PERSPECTIVE

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ABSTRACT

The ground breaking coronavirus is reshaping the financial market in previously inconceivable ways. The business world is currently in a state of financial crisis. The likelihood of engaging in COVID-19-related insider trading has increased dramatically during this moment of economic uncertainty. It's a rich opportunity for traders, especially those who understand the impact of the current situation on publicly traded corporations. Financial transactions, business disruptions, material contracts, mergers and acquisitions, and other key performance standards would enable an active participant in such a setup to anticipate and foresee unexpected benefits, allowing them to plan their trading and allocation decisions more efficiently. This, in turn, will have an impact on investors who are unaware of such market happenings. Though SEBI recently announced a number of changes to listed companies' reporting obligations in the wake of the COVID-19 outbreak, it will be interesting to observe how the industry reacts to the new insider trading regime's strict trading restrictions. Insider trading's impact and influence during pandemics are investigated in this study.

KEYWORDS: Insider Trading, Pandemic, SEBI Regulations, and corporates.

INTRODUCTION

Trading in a company's securities by someone who has access to price-sensitive information before it is made public is known as insider trading. According to section 195 of the Companies Act 2013, insider trading is defined as "the act of selling, subscribing, or agreeing to subscribe to a company's securities directly or indirectly by key management personnel or a company director who is expected to have access to unpublished price sensitive information about the company's securities." "Any individual who has access to undisclosed price sensitive information on a company's stocks," according to the Securities and Exchange Board of India (SEBI) (Prohibition of Insider Trading) Regulations, 1992.

Insider trading is defined as an individual's purchase and sale of a company's shares before it becomes available to the general public, using the company's undisclosed price-sensitive information to earn abnormal profits and limit losses. Legal insider trading occurs when a business insider trades in accordance with all regulations, however any violation of SEBI's criteria is classified as criminal or illegal insider trading. As a result, they must notify their authorised trades to SEBI as soon as possible in order for insider trading activity to be detected. Business insiders are permitted to trade in the shares of their own company. They must, however, register these actions to prevent the exploitation of price-sensitive information that is not yet available to the broader public. SEBI has introduced a variety of insider disclosure measures to boost investor confidence and enhance openness in securities trading. The purpose of requiring all information related to these transactions to be disclosed is to provide a level playing field for all market players. To avoid a SEBI investigation or disciplinary action for insider trading, organizations should review their security protocols and update their insider trading policies, ensuring that all of these policy decisions explicitly describe the prohibition of trading on unpublished price-sensitive information.

REVIEW OF LITERATURE

1. **Wronka, C. (2021)**, in their paper found out that Many financial sector stakeholders and players are responding in ways that put the entire financial sector and all of its stakeholders at great risk . As the pandemic ravages the world and pushes people and businesses to the very limits of their endurance, many financial sector stakeholders and players are responding in ways that put the entire financial sector and all of its stakeholders at great risk. The COVID-19 pandemic, in particular, has resulted in the creation of new financial crime patterns that were previously unheard of or not as prevalent. This necessitates increased prudence on the part of financial sector regulators, who must be on the alert for such financial crimes. During this pandemic, they also stress the importance of conducting regular and rigorous insider trading reviews of publicly traded corporations. Other possible financial crimes must also be anticipated and relevant remedial measures are taken.
2. **Merl, R., Stockl, T., & Palan, S. (2021)**, According to them, Modern capital markets are subject to multiple interventions and regulations, some of which restrict the execution of specific trading techniques in a market. They point out that while the individual consequences of these restrictions are evident, the picture of their combined effects is less clear. They looked at how two restrictions interact, specifically rules banning shorting of assets and cash and rules limiting insider trading, and found that earlier research showed spikes in short-selling activity surrounding the disclosure of insider information, which various studies attribute to different causes. Both allowing short positions and enabling informed trading, according to their research, causes informed traders to increase their market activity, causing mispricing and spreads to rise.
3. **Olsen, A. M. (2021)**, have examined the modifications to the European Union (EU) law on market abuse, market manipulation, and insider trading regulation introduced when the Market Abuse Regulation (MAR) was implemented to analyse the cost of the exogenous shock of insider trading. This study shows that MAR caused a plausible exogenous shock to the They then look at the effects of firm-

and country-level culture on insider trading profitability around the time of MAR's announcement, implementation, and first enforcement. After the first implementation of MAR, insiders from high ESG firms likely to engage in less profitable insider trading. In the post-announcement and post-effective periods, insiders from high ESG corporations also likely to engage in more(less) profitable purchasing (selling) activities. However, the size of the firm has an impact on these impacts. After the first MAR enforcement, high levels of uncertainty avoidance and corruption contribute to more (less) profitable selling (buying) activity. Market reactions to the announcement of MAR sanctions have been overwhelmingly negative. When the enforcement (1) involves illicit insider trading, (2) is against a legal person, (3) imposes a bigger monetary penalty, and (4) occurs before the COVID-19 outbreak, the negative reaction is amplified. This influence varies depending on the firm's and country's culture. Following the first European Securities and Market Authority (ESMA) publication of MAR enforcements, strong ESG and environmental consciousness contribute to higher corporate value. After the first ESMA report on MAR enforcements, country-level culture and insider trading profits do not add to company value.

4. **Coleman, R. (2021).**, According to him, the illegality and ethics of insider trading were a forerunner to what is today considered modern business ethics. From the concept of "shareholder primacy," which is entirely focused on profit, to many stakeholders, which is the concept of insider trading. Insider trading is intended to increase market trust by exploiting insider information to create an unfairness in a semi-strong form of market efficiency. Modern ethics places a greater emphasis on justice. Companies are praised for adopting more environmentally friendly policies while simultaneously investing in their workforce and communities. Investing in sustainable indices and enterprises has also been a new trend in ethical investing. All of these consequences have resulted from a shift in public opinion.
5. **Xiao, H., Chen, X., Fang, H., & Zhang, Y. (2021)**, note that share pledging, the practise of shareholders securing a loan by pledging their shares, has become a global phenomenon in recent years, and have investigated the impact of such corporate insider actions on outsider wealth during the pandemic, examining how firms' market value changes when corporate insiders pledge their shareholdings during China's COVID-19 outbreak. Market investors reacted negatively to share pledge announcements by companies in high-pandemic-affected countries, according to the findings. Furthermore, the pledged enterprises' state ownership and improved corporate governance systems may be able to counteract such negative consequences. During a crisis, their research focuses on a distinct externality generated by company insiders to outside shareholders.
6. **Reid, G. A., Dubow, J. A., et al. (2020)**, looked into what companies could take to defend themselves from an SEC insider trading inquiry or enforcement action. Companies should use this opportunity to evaluate their internal controls and insider trading policies, ensuring that these policies prohibit trading on material nonpublic information and adequately address the increased opportunities for such trading created by the current pandemic, according to the authors. In light of the company's remote working habits, this may include changing or enhancing business policies. Companies must also keep track of their employees' adherence to these regulations, ensuring that everyone is aware of and following the

company's insider trading policies. Companies might consider sending clear advisory communications to their employees to remind them of their commitment not to share or trade material nonpublic information learned via their employment. Given the ease with which information can spread among family members in a quarantine situation, company directors, officers, and employees should all be reminded of the significant risks associated with insider trading, as well as best practises for protecting confidential information while in quarantine. This involves reminding these personnel to only discuss material non-public information in a private environment and to keep computer screens displaying such information hidden from non-insiders. The COVID-19 epidemic will inevitably result in personal and corporate economic losses. Individuals holding material knowledge about their own or other companies may not sell stock in these companies to make up for losses unless this crucial information is first disclosed to the investing public. To prevent some of the dangers connected with nonpublic material information, corporations might consider releasing part of it in their Forms 8-K, which will reduce the likelihood that the company's material nonpublic information will be traded before it is made public. Companies should also evaluate and follow the COVID-19 disclosure guidance recently provided by the SEC's Division of Corporation Finance when producing their periodic disclosure documents. COVID-19's effects on the company, what management anticipates its future impact to be, how management is responding to emerging events, and how [the company] is planning for COVID-19-related uncertainties are all part of this guidance. Before making mandatory disclosures, companies should carefully consider the impact of COVID-19 and related government limitations on their businesses, and directors, officers, and employees should be reminded to refrain from trading on material information until these disclosures are made public.

7. **Mitts, J. (2020)**, The author discovers that when good news is released, the likelihood, share volume, and dollar volume of insider sales under 10b5-1 plans are all greater, and each of these is higher when the reported news is better. The health care sector and mid-cap corporations are the most likely to disclose good news on Rule 10b5-1 selling days, indicating that stock prices reverse following large levels of Rule 10b5-1 selling on positive news days, and that the price reversal increases with the share volume of Rule 10b5-1 selling. He also demonstrates that, whatever one may think of health-care executives' favourable stock sales while developing vaccines during the 2020 pandemic, such sales were not unusual.
8. **Bilinski, P. (2021)**, he discovered that in the early months of the pandemic, analysts significantly increased their research activity: quarterly earnings forecasts increased by 72 percent, revenue forecasts by 80 percent, cash flow forecasts by 59 percent, dividend forecasts by 11 percent, target prices by 154 percent, and stock recommendations by 88 percent in March 2020 compared to the same pre-pandemic month. When compared to a comparable pre-pandemic timeframe, forecasts published during the pandemic have significantly larger errors. Analysts update their expectations more aggressively during the pandemic than before it: the average absolute revisions vary from 142 percent for revenue forecasts to 9 percent for dividend estimates. During the pandemic, price reactions to analyst projection revisions and stock recommendations are gradually higher because to lower target prices. This effect is amplified

during times when investors are actively looking for information about the epidemic and the stock market, as evidenced by google searches. Surprisingly, investors place a higher importance on the analyst's part in uncovering private information than on their position in assessing public data during the pandemic.

9. **Hope, O. K., Li, C., Ma, M. S., et al (2022)**, investigated a large number of management guidance withdrawals during the COVID-19 epidemic and discovered that it drew significant media, investor, and regulatory attention. Their research examines the factors that lead to such withdrawals and finds evidence that they are caused by economic uncertainty caused by enterprises' exposure to the COVID-19 epidemic, rather than poor financial performance. In addition, when corporations face larger legal risk, the impact of COVID-19 exposure on guidance withdrawals is greater. Furthermore, guidance withdrawals result in unusually high trading volumes and high analyst forecast dispersion, but have no negative impact on stock prices or analyst earnings forecasts; thus, the findings have implications for understanding corporate disclosure practises during periods of heightened economic uncertainty.

SIGNIFICANCE OF THE STUDY

Insider trading restrictions are important in the stock market, and regulators' concerns about them are comparable across worldwide markets, and difficulties are more or less widespread. Insider trading is a circumstance in which certain market participants use the UPSI to make gains, as well as leaked information from various internal business sources that is used in a discrete manner to achieve private gains. This has become more prevalent across markets, and the task of regulators has become more difficult to make the uneven information with certain market elements less capable of generating private wealth for a select few, by imposing appropriate controls and regulations, thereby making the task more difficult without being detected.

The Securities and Exchange Commission (SEC) has expressly requested that companies consider the following questions: -

- What are the major operational difficulties that management and the Board of Directors are keeping an eye on and assessing?
- What is the current state of the entity's overall liquidity? Is there a meaningful impact on the entity's financial situation and outlook from any changes in cash flow from operations?
- Has the company used revolving lines of credit or obtained funds in the public or private markets to meet its liquidity requirements?
- Have COVID-19's effects hampered your capacity to obtain traditional funding sources on the same or nearly same terms as in previous periods?
- Are you in danger of breaching credit and other agreements' covenants?
- Are there any estimations or assumptions underpinning such measurements as cash burn rate, daily cash consumption, and so on, that must be disclosed in order for the metric to be accurate?
- Is the entity's capital expenditures down, and if so, how?
- Are you able to meet your debt and other commitments on time? Have the liquidity issues been adequately considered?

- Have customers been offered new terms, such as longer payment terms or refund periods, and, if so, how have these measures impacted the entity's financial health or liquidity?
- Is a company using supplier finance programmes to manage its cash flow, also known as supply chain financing, structured trade payables, reverse factoring, or vendor financing?
- Has the entity considered the impact of significant events that occurred after the reporting period ended but before the financial statements were released? Particularly in the context of capital liquidity.

In the Indian context, the SEBI issued a circular on May 20, 2020, advising on disclosure of the material impact of the Covid-19 epidemic on listed entities under the LODR (2015) regulations for the following listed entities:

i. The economic impact of the CoVID-19 pandemic;
ii. Ability to keep operations running, including factories, units, and office spaces open and closed;
iii. If there is one, make a plan for restarting operations.
iv. Steps were taken to ensure that operations ran smoothly;
v. Estimation of CoVID-19's prospective impact on the company's operations;
vi. Capital and financial resources, profitability, liquidity position, ability to service debt and other financing arrangements, and assets are all factors that will be impacted by CoVID-19. internal financial reporting and control, supply chain, and demand for its goods and services are all factors to consider.
vii. Other relevant material developments about the listed entity's business; Existing contracts/agreements where non-fulfillment of commitments by any party will have a major impact on the listed entity's business.

The SEBI has also recommended companies not to make selective disclosures and, to the degree practicable, to highlight the impact of Covid -19 on their financial statements.

METHODOLOGY

The study is an exploratory investigation of the elements that influenced insider trading during the Covid -19 period. A literature analysis of prior activities, such as those discovered globally in Insider trading during pandemics, is studied, and relevant issues are plucked out for policymakers and regulators to understand and regulate, where needed. The SEBI Appellate Tribunal's chosen and noteworthy judgements during the epidemic period are also analysed to determine the regulator's orientation in this regard, as well as how the regulator views Insider trading operations.

DISCUSSION

- The author has reviewed previous literature on the topic of insider trading and notes that different researchers have different points of view, indicating that the regulator should pay more attention to insider trading in publicly traded companies and take appropriate steps to reduce the level of insider trading.
- According to certain studies, country-level culture and insider trading profits do not add to firm value, however pledging of entity shares has a negative impact on firm value, as found in other studies. Another

intriguing conclusion in these research is that entities are withdrawing recommendations primarily owing to the Covid-19 pandemic's unpredictability rather than financial performance.

- ♠ The tail events involved in the Covid -19 times influenced analyst research publications positively during the first few months of the pandemic, possibly due to the inability to visualise the duration of the epidemic and a higher level of economic impact that could not be quantified effectively, with analysts revising forecasts aggressively during the pandemic period than during the pre-pandemic period, perhaps due to the inability to visualise the duration of the epidemic and a higher level of economic impact that could not be quantified effectively, with analysts rev
- ♠ Disclosures enforced by authorities around the world, including the SEC in the United States and the SEBI in India, have aided in keeping volatility at a range-bound level. It's also possible that pharma and health-care companies directly involved in vaccine development, as well as insiders working for the companies, received significant profits. According to SEBI's annual report (2020-21), there was a decrease in the number of insider trading cases investigated in 2020-21 as compared to 2019-20, indicating a lower degree of investigation of cases. In 2019-20, 49 cases out of 161 were tied to insider trading, while in 2020-21, 30 cases out of 94 were related to insider trading, indicating roughly similar levels at 31%.

However, the number of occurrences of market manipulation has increased from 35 in 2019-20 to 41 in 2020-21, showing the impact of Covid -19-related factors that may have tempted market participants to resort to manipulations. Miscellaneous instances involving listing conditions violations, statutory auditors, SCRA regulations, and preferential allotment have decreased from 45 percent in 2019-20 to 21 percent in 2020-21. These figures suggest that auditors are scrutinising papers more closely, and that entities are voluntarily complying with regulations, which may have aided in the reduction of instances.

CONCLUSION

The implications of insider trading's negative consequences and its role in a financial crisis arising during a pandemic cannot be overlooked, and regulators would be wise to conduct sector-specific studies to better understand the key effects that insider trading has had on each sector, and to issue appropriate modifications or guidelines, or repeal the regulations, to avoid taking retail investors and the general public for a ride. This will also help to prevent market capitalization erosion.

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