DHARMASHASTRA NATIONAL LAW UNIVERSITY

Jabalpur, Madhya Pradesh

Established by Act 24 of 2018 of the Madhya Pradesh Legislature

Special Volume I January 2024

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A Double-Blind Peer-Reviewed Journal of DNLU, Jabalpur.

DNLU
Student Law
Journal

Dharmashastra National Law University, Jabalpur

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All inquiries regarding the journal should be addressed to:

Editor-in-Chief,

Student Law Journal,

Dharmashastra National Law University, Jabalpur,

Madhya Pradesh, 482001

Email: dnluslj@mpdnlu.ac.in

Website: dnluslj.in

Cite as: Special Vol-1-DNLU-SLJ (2024)

Published by:
Registrar,
Dharmashastra National Law University,
South Civil Lines, Pachpedi, Lekha Nagar, Jabalpur, Madhya Pradesh 482001

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Special Volume I January 2024

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FOREWORD

The Indian financial markets operate in a dynamic landscape where securities law plays a crucial role in upholding transparency, fairness, and safeguarding investor interests. As the Indian economy integrates with the global financial system, the need for a robust and adaptable regulatory framework becomes paramount. The foundation of securities regulation in India lies in a comprehensive legislative framework, including Acts such as the Securities Contracts (Regulation) Act, 1956; the SEBI Act, 1992; the Depositories Act, 1996; and the Companies Act, 2013, along with their accompanying rules and regulations. Notably, the adaptability of Indian securities regulation is evident through amendments made over the years to address emerging challenges and align with international standards.

SEBI spearheads efforts in ensuring market integrity and regulatory excellence, overseeing aspects such as the registration and regulation of market intermediaries, governance monitoring, and enforcement of market norms. The collaborative engagement between regulators and market participants is pivotal for the resilience and growth of the Indian securities market. The judiciary, including the Securities Appellate Tribunal (SAT) and the Supreme Court of India, frequently endorses SEBI's initiatives. In instances of variance, there lies an opportunity for research and growth.

Securities Law, with its multifaceted dimensions, underscores the growing impact of technology on securities markets. The advent of electronic trading, dark web, colocation, blockchain, robo advisory and other fintech innovations presents both opportunities and challenges. Striking a balance between innovation and investor protection is crucial for the sustained growth of the Indian securities market. In navigating the intricate landscape of securities law, staying informed about the latest developments is crucial for legal practitioners, market participants, and regulators.

Despite the existence of the securities market in India for over a century, and under SEBI for more than 30 years, organized and quality research has been limited. This preface aims as a starting point for those seeking to '*Ponder and Pen'* the regulatory framework governing securities in India. I proudly endorse Dharmashastra National Law University, Jabalpur (DNLU) for taking the lead in inspiring law students to '*Contemplate and Craft*' Indian Securities Law.

Let's break down the barriers between academia and real-world legal practice, fostering a new generation of legal professionals ready to navigate the challenges of our dynamic Indian legal landscape.

Sumit Agrawal

MESSAGE FROM THE PATRON

Dear Contributors, Editors, and Readers,

It is with immense pleasure and pride that I address you as the Vice-Chancellor of Dharmashastra National Law University and the Patron of the DNLU Student Law Journal. I extend my warm greetings to all of you on the occasion of the release of the Special Volume, a result of the 1st DNLU-Student Law Journal Essay Writing Competition 2023.

As we delve into the pages of this remarkable publication, I am filled with admiration for the intellectual prowess and scholarly achievements displayed by our students. The DNLU Student Law Journal stands as a testament to the dedication, hard work, and academic rigor exhibited by our budding legal minds.

This Special Volume, born out of the selected articles from the Essay Writing Competition, is a celebration of the profound exploration into the intricate dimensions of Capital Markets and Securities Laws. The essays presented here are not just a collection of words; they are a testament to the dedication, hard work, and depth of understanding in the field of Capital Markets and Securities Laws. I am delighted to see how this competition has been instrumental in furthering deliberations on securities laws and providing a platform for budding legal minds to contribute meaningfully to this domain.

The DNLU Student Law Journal, through initiatives like this competition, strives to bring together a community of legal experts and scholars dedicated to advancing the study and understanding of securities law. It is heartening to witness the enthusiasm and dedication with which our students have embraced this opportunity to delve deeper into this complex area of law.

I extend my sincere appreciation to all the contributors who have meticulously crafted their articles, contributed fresh insights and advanced our understanding of securities law. Your unwavering commitment to excellence and relentless pursuit of knowledge are truly commendable, enriching the legal community and contributing to the development of jurisprudence.

I also commend the tireless efforts of the editorial team, who have upheld the highest standards of academic excellence by reviewing and refining the articles. Their commitment to the integrity of legal scholarship and the quality of the journal is invaluable.

To the readers, I invite you to actively immerse yourselves in the content, question the notions presented, and set forth on your unique intellectual exploration. Allow the research encapsulated in these pages to spark your inquisitiveness, fuel your scholarly pursuits, and mold your viewpoint regarding the dynamic landscape of law, with a specific emphasis on Capital Markets and Securities Laws.

As our journey in legal education unfolds, the DNLU Student Law Journal stands firm as a pivotal aspect of our academic pursuits. It embodies our dedication to outstanding legal scholarship and mirrors the intellectual development of our student body. Let us hold this journal dear as a testament to our shared quest for knowledge, justice, and adherence to the rule of law.

In closing, I extend my sincere congratulations to the entire team involved in the DNLU Student Law Journal for their tireless efforts, unwavering dedication, and steadfast commitment to nurturing a culture of scholarly exchange.

May this journal continue to flourish and serve as a wellspring of inspiration for future generations of legal scholars.

Prof. (Dr.) Manoj Kumar Sinha
Vice-Chancellor,
Dharmashastra National Law University (DNLU).

EDITORIAL NOTE

It gives me immense pleasure in writing this editorial note for the much-awaited E-volume of the DNLU Student Law Journal on ‘Capital Markets and Securities Laws’. Writing always represents a higher form of intellectualism gripped in the flesh of words. Certainly, it goes without saying that DNLU Student Law Journal is turning out to be a great platform for amplifying meritorious scholarship. As the journal is garnering more academic respect in the academic fraternity, it becomes more of a responsibility, nay duty, of the student body to ensure that the kind of academic standard that was envisioned at the initiation of this journey continues to guide the path of the Journal for future issues. The present issue addresses a distinct but relevant area of research, something that has remained untouched from larger academic discussion. The articles were called on competitive basis, which is reflective in the quality of the pieces.

The article titled ‘*ESG Reporting: Regulatory Progress and Future Imperatives*’ explores the evolution of Environmental, Social, and Governance (ESG) criteria in India, focusing on SEBI’s role in shaping transparency reporting. Emphasising the need for standardized ESG rating providers, it highlights the benefits of ESG reporting for investors and companies, paving the way for a more sustainable business landscape.

The article titled ‘*Navigating the Maze of Market Manipulation: Creating Effective Insider Trading Plans*’ appraises India’s insider trading plans. It analyses the current mechanism’s shortcomings, offers a cross-jurisdictional perspective on trading plans, and suggests recommendations to make them more attractive to insiders.

The article titled ‘*Crypto in India: Time for SEBI to Take the Lead*’ delves into India’s approach to regulating crypto-assets, advocating for SEBI’s proactive role in shaping a comprehensive regulatory framework. Highlighting operational intricacies and global examples, the article emphasises the need for SEBI to lead in regulating India’s crypto market.

The article titled ‘*Decoding the Code: Algo Trading in India*’ provides an overview of algorithmic trading's impact on global finance, addressing concerns in India. Proposing a voluntary Code of Conduct and a Regulatory Sandbox, the analysis aims to balance innovation and ethical standards in India's maturing algorithmic landscape.

The article titled ‘*Amidst Market Whims: Challenges in SEBI’s Market Rumour Regulation*’ critically assesses SEBI's response to market rumours through amended LODR Regulation 30(11). It highlights challenges, advocates for a nuanced approach, and urges SEBI to reconsider the stringent timeframe, aiming for a balanced regulatory framework fortifying investor trust.

With these articles, the DNLU Student Law Journal continues to serve as a beacon for scholarly exploration, addressing crucial aspects of Capital Markets and Securities Laws.

This editorial note will not be complete without our sincere gratitude towards our Honourable Vice-Chancellor Professor (Dr.) Manoj K. Sinha for his unparelled motivation towards academic excellence. To our supportive Honourable Registrar, Professor (Dr.) Shailesh N. Hadli for his motivating attitude and words throughout this process. To our beloved and ever-motivating Dean of Student Welfare Dr. Praveen Tripathi, Associate Professor at DNLU. Dr. Praveen has always ensured that academics and student welfare goes hand-in-hand, that is reflective in his words and actions. I also take this opportunity to thank our intellectual powerhouse Dr. Manwendra Tiwari, Associate Professor at DNLU, his mere presence has ensured that the ambience in the University is serene & intellectually stimulating. I am thankful to Dr. Gargi Chakrabarti Ma'am, Associate Professor at DNLU, she is a moral authority in academics to reckon with, with her ever-engaging discussions and unique viewpoints, Ma'am is a strong backbone of academics at DNLU. I extend my gratitude to Ms. Shruti Nandwana, Assistant Professor, for her co-ordination and expert guidance in overseeing the inaugural DNLU Student Law Journal Essay Writing Competition.

Finally, at the cost of repetition, I will again extend my heartfelt gratitude to the authors of this E-volume. It is truly their undeterred efforts and academic commitment that has brought a quality journal in the making. With a deep sense of appreciation, we want to thank all the authors for their intellectual effort, and hopefully, in near future they will consider sending in their work to our forum.

Ashit Srivastava & Shantanu Singh
(On behalf of the Editorial Board)

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AMIDST MARKET WHIMS: CHALLENGES IN SEBI'S MARKET RUMOUR REGULATION

—Sejal Trehan & Shashwat Sharma***

Abstract

Market rumours wield the power to disrupt market stability by triggering rapid and often erratic fluctuations in securities of the company along with erosion of investor confidence. SEBI's response, the amended LODR Regulation 30(11), mandates prompt clarification of market rumours by top listed entities, aiming to overcome such challenges. However, this regulation hurdles timely verification, especially in sensitive situations like mergers and acquisitions governed by non-disclosure agreements. While designed to bolster investor confidence, the regulation's rigid 24-hour compliance window raises concerns of inadvertent market volatility. Drawing insights from global practice, this article critically assesses SEBI's initiative. It advocates for a nuanced approach, incorporating exemptions for ongoing negotiations, inspired by global best practices, while urging SEBI to reconsider the stringent timeframe. By melding global wisdom with domestic needs, a balanced regulatory framework can emerge, fortifying investor trust while navigating the complexities of market rumour verification.

Keywords: *Market rumors; listing obligations; non-disclosure agreements; unfair trade practice*

I. INTRODUCTION

The recent growth of social media platforms and means of communication has resulted in rapid exchange of information. This information exchange has affected all areas of business transactions, and consequently, can have extremely detrimental outcomes. Within the securities market, the Securities and Exchange Board of India ("**SEBI**") is constantly faced with the challenge of addressing the issue of unverified information that has the potential to disrupt market stability and investors' confidence. The magnitude of such disruption is evident from the recent Adani-Hindenburg row, which led to the erosion of $134 Billion from the Adani

* Student, Rajiv Gandhi National University of Law, Patiala. Corresponding author's Email: sejaltrehan21007@rgnul.ac.in.

**Student, Rajiv Gandhi National University of Law, Patiala. Corresponding author's Email: shashwatsharma21014@rgnul.ac.in.

group's market value.[1] To counter the issue of market rumours SEBI amended the Listing Obligations and Disclosure Requirements ("**LODR**") (Second Amendment) Regulations, 2023.[2]

Regulation 30(11) of the LODR has been amended to mandatorily require the top 100 listed entities by market capitalization to either accept or deny any market rumour within 24 hours, effective from February 1, 2024. Further, the regulation shall apply to the top 250 listed entities effective from August 1, 2024.[3] This regulation has been brought about by analysing the practices in other advanced jurisdictions, with the board note particularly referring to Section 202.03 of the New York Stock Exchange Listed Company Manual ("**NYSE Manual**").[4] The primary objective of this amendment is to reduce information asymmetry, promote transparency, enable the investor to make a well-informed choice and mitigate the undesirable consequences arising from unverified market rumours and speculations.

By delving into the nature and implications of market rumour verification, one can understand the effects of the aforesaid regulation on market stability, investors and the listed entities. In this article, the authors provide a critical analysis of market rumour verification regulation, along with its consequences in the Indian securities market and investors, followed by suggestions for its successful implementation.

II. CHALLENGES OF TIMELY RESPONSE

Regulation 30(11) specifies a 24-hour period within which an entity must clarify market rumour from the reporting of the event or information in mainstream media. The 24-hour time period is manifestly insufficient to comply with the necessary compliances and obligations to ascertain the veracity of the rumour. In situations wherein the rumour emanates from a third-party source, an entity requires time to conduct internal inquiries and investigations to be in a position to rightfully verify the information.[5]

For instance, in the Adani-Hindenburg short-selling controversy, despite Adani Enterprises' prompt denial of the report within 24 hours, the situation intensified. Stocks of Adani

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[1] Amit Mudgil, 'Adani Group CFO recalls first two days of 88 Hindenburg allegations, says this' Business Today (22 February, 2023) <https://www.businesstoday.in/markets/company-stock/story/adani-group-cfo-recalls-first-two-days-of-88-hindenburg-allegations-says-this-371083-2023-02-22> accessed 23 November 2023.

[2] Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) (Second Amendment) Regulations, 2023, reg. 30(11).

[3] *Ibid*.

[4] New York Stock Exchange Listed Company Manual, s 2(202.03) ["***NYSE Manual***"].

[5] SEBI Board Meeting, 'Amendments to requirements for disclosure of material events or information by listed entities under SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015' https://www.sebi.gov.in/sebi_data/meetingfiles/apr-2023/1681703089597_1.pdf accessed 25 November 2023 ["***Board Note***"]

Enterprises and its subsidiaries continuously hit lower circuits.[6] This demonstrates that 24 hours is not a sufficient period for entities to clarify rumours to the satisfaction of the investors. Alternatively, had the rumour been clarified after taking the requisite time and providing the public with the necessary documents that supported the denial by Adani Enterprises, the losses incurred could have been avoided.

Furthermore, unverified rumours, confirmed or denied by an entity, which are subsequently disclosed to be otherwise, have the possibility of facing regulatory scrutiny under section 4(2)(f) of the SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 ("**PFUTP Regulations**")[7] as it will be an unfair trade practice to knowingly publish any information which is either not true or which the person does not deem to be true. Furthermore, SEBI's guidelines in Annexure II of the Continuous Disclosure Requirements Circular stipulates that an event must be disclosed after attaining a definite level of certainty.[8]

In the particular instance of mergers and acquisitions, there are multiple hurdles in the implementation of this regulation. Firstly, deal negotiations are governed by Non-Disclosure Agreements ("**NDA**") that restrict the disclosure of any information beyond the parties.[9] Further, negotiations are shrouded with uncertainty, and it may not be possible to clarify any rumour relating to the deal until the deal is concluded. There have been numerous instances where initial negotiations fell through, and confirming any rumour pertaining to them would have attracted the provisions as mentioned earlier on the entity. In addition, the board note on this amendment suggests that the stage of the negotiation may be provided, even if it is at a nascent stage.[10] Such disclosure during preliminary negotiations may prove to be disadvantageous for the parties involved, as it may alter the upper hand and control that the listed entity may have exercised over the deal.[11]

III. MARKET VOLATILITY AND INVESTOR CONFIDENCE

Financial rumours lead to significant fluctuation in the stock prices of a listed entity. Capital markets throughout the world remain prey to such rumours and move accordingly. The

[6] Astha Rajvanshi, 'India's Richest Man Accused of Pulling the 'Largest Con in Corporate History' Time (25 January, 2023) <https://time.com/6250052/adani-hindenburg-fraud> accessed 22 November 2023.
[7] Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulation, 2003 [Last amended on 25 January, 2022].
[8] Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 [Last amended on October 23, 2023], reg(s) 30 and 30A.
[9] Vinod Kothari, 'Silence no more golden: New regulatory regime forces top listed companies to respond to rumours' (Vinod Kothari & Consultants, 12 July 2023) https://vinodkothari.com/2023/07/silence-no-more-golden-new-regulatory-regime-forces-top-listed-companies-to-respond-to-rumours/ accessed 27 November 2023 ["***NDA Agreements***"].
[10] Board Note.
[11] Nitin Kumar, 'M&A Deal Leakage' (Medium, 22 December 2021) https://medium.com/mergers-acquisitions-and-divestitures/m-a-deal-leakage-9f9b4ff6c629 accessed 26 November 2023.

amendment focuses on preventing such situations and maintaining investor confidence. However, the regulation may amplify rather than stabilise the market volatility due to the susceptibility to false positives and negatives.[12] For instance, a scenario involving a rumoured merger between listed entities 'X' and 'Y'. Under amended disclosure regulations, entity X is obligated to clarify its position. Even if the rumour holds truth, entity X may officially refute it. In contrast to more developed jurisdictions, Indian companies operate without regulatory barriers like standstill periods. Consequently, despite official refutation, Entity X may proceed with a speculated merger at a later juncture. This action could ultimately undermine market sentiments, leading to a situation of instability in the market.

To counter this, in the UK, an advanced regulatory framework under section 2(6) within the Takeover Code comes into effect when there is a rumour announcement. [13] Under this provision if a rumour surrounding negotiations floats, the concerned entity has to either announce an offer within 28 days or verify that they will not be making an offer, triggering a six-month standstill period, in which they cannot make any offer in respect of the denied negotiation. Such stringent regulations help maintain stability in corporate negotiations as opposed to the Indian landscape.

IV. GLOBAL STANDARDS: SUGGESTIONS FOR INDIA'S MARKET RUMOUR VERIFICATION REGULATION

The regulatory approach to counter the negative impact of market rumours is not novel. Several advanced jurisdictions have already established rules for listed entities to verify such rumours. The framing of rules to verify market rumours by listed entities demonstrates a proactive stance of regulators in mitigating potential market disruptions. These regulations aim to instil confidence in market integrity and investor trust by encouraging accountability in information dissemination.[14]

The NYSE manual also provides for the confirmation of market rumours, however, unlike the Indian regulation, there is no timeframe for clarification. It merely states that the entity is obligated to provide an immediate and candid statement to the public. This provision overcomes the challenge posed by the 24-hour time period and provides the requisite time for the entity to conduct inquiries and investigation, and consequently, be able to accurately ascertain the veracity of the rumour.[15] In this manner, the entity is no longer under the threat of facing regulatory scrutiny for wrongful disclosures, as highlighted by the authors above.

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[12] Affluence Advisory Pvt Ltd, 'Mandatory Verification of Market rumours' (CaClubIndia, 01 July 2023) https://www.caclubindia.com/articles/mandatory-verification-of-market-rumours-49912.asp accessed 26 November 2023.

[13] The City Code on Takeovers and Mergers 2016, s 2(6).

[14] Board Note.

[15] NYSE Manual.

Similarly, the UK market abuse regulation[16] allows for delayed verification of the rumours in case of legitimate interests being compromised. This includes ongoing negotiations, financial stability and future prospects of the entity. This contrasts the Indian regulation and provides an exception to entities from disclosing highly sensitive and confidential information, which is not possible to provide at nascent stages and is detrimental to the interests of the negotiating entities.

Additionally, Chapter 3 of the European Union Market Abuse Regulation[17] also addresses rumour verification. It allows entities to postpone disclosures in cases that could harm their legitimate interests. This provision safeguards business confidentiality, shielding entities from the adverse impacts caused by market rumours. However, compliance requires listed entities choosing to delay clarification to provide explanations to regulators. This mechanism prevents misuse of the provision for unfair advantage, fostering an environment of transparency and accountability.

The Hong Kong Securities and Futures Ordinance[18] Section 307(B), (C) and (D), in parallel, requires listed corporations to make public insider information, in a manner that is prompt, however, there is no timeframe to adhere to. Further, the regulation provides that an entity has failed to make public insider information if the information so made public is incorrect or deceiving as to a material fact. This measure ensures that an entity provides true and accurate information that allows investors to make well-informed choices. However, an entity is exempted from such disclosures when the information relates to an ongoing negotiation or a trade secret.

Therefore, it is discernible that Regulation 30(11) falls short of adequately addressing market rumours while keeping the interests of the investors and entities in mind. To counter this, the regulation must incorporate some changes, such as introducing exemptions from disclosures when the information relates to ongoing negotiations or trade secrets, taking inspiration from the UK, EU and Hong Kong regulations.[19] Further, the authors suggest that the 24-hour timeframe should be removed, however, not in a similar vein as the above jurisdictions. A timeframe is required to prevent entities from escaping the obligations of prompt clarifications. Additionally, there may arise a situation in which an entity releases a statement right before the official corporate announcement. This may jeopardise the regulatory intent behind the introduction of the regulation.

V. CONCLUSION AND WAY FORWARD

[16] The Market Abuse (Amendment) (EU Exit) Regulations 2019, SI 2019/310 [“***Abuse Regulations***”].
[17] Council Regulation (EU) 596/2014 on market abuse regulation; Repealing Directive 2003/6/EC; Council and Commission Directives 2003/124/EC; 2003/125/EC; 2004/72/EC.
[18] Securities and Futures (Amendment) Ordinance 2012, s 307 SI 2012/9 [“***Securities Ordinance***”].
[19] *Ibid.*

Market rumours pose an imminent threat to the stability of financial markets and investor confidence. Their mandatory verification by listed entities, therefore, is a welcome move in the Indian regulatory landscape. However, challenges arise in complying with the stringent 24-hour timeframe, especially in cases where rumours stem from third-party sources. Moreover, such disclosures made under regulatory pressure can attract regulatory action under PFUTP regulations. Additionally, corporate negotiations are marred by NDA agreements thereby leading to uncertainty, which operates as a challenge to such clarifications. While the regulatory intent is to curb market volatility and maintain investor confidence, its implementation might inadvertently amplify volatility due to false positives and negatives.

Thus, the experiences from global markets, such as the UK's "Put Up or Shut Up" Rule and provisions in the EU and Hong Kong, offer valuable insights.[20] These regulations allow for delayed verification in sensitive negotiations, safeguarding entities from premature disclosures that could compromise negotiations or reveal trade secrets. Such provisions balance transparency with the protection of legitimate interests.

In light of these global standards, Regulation 30(11) could benefit from revisions, including exemptions for ongoing negotiations and removing the strict 24-hour timeframe while ensuring timely disclosures. Striking this balance is crucial to prevent entities from evading their obligations while allowing sufficient time for accurate verifications.

In conclusion, while SEBI's amendment aims to enhance transparency and curb market rumours, a revision of the regulation is imperative. By incorporating elements from established global standards and adjusting the time frame, SEBI can achieve a more balanced approach that safeguards investor interests while ensuring the accuracy of disclosures.

[20] Abuse Regulation.

ESG REPORTING: REGULATORY PROGRESS AND FUTURE IMPERATIVES

—Siddhu Sanghavi[*] & Sameer Rahman[**]

Abstract

*The concept of sustainable business practices has evolved globally through the emergence of the Environmental, Social, and Governance ("**ESG**") criteria aimed to benefit the institutions, those investing in such institutions, and society. The essay focuses on the evolution of the ESG from Corporate Social Responsibility ("**CSR**") in India by way of disclosure regulation that enables companies' transparency reporting. This essay examines the central role that SEBI has played in recent times, especially on the latest Business Responsibility and Sustainability Report ("**BRSR**") norms. It emphasizes the need for standardized ESG rating providers and illustrates how India can shape its own unique ESG narrative drawing upon lessons from global experiences. It further highlights the multifaceted benefits of ESG reporting for both the investors and the companies, paving the way for a more sustainable and responsible business landscape.*

Keywords: *ESG, CSR, BRSR norms, Ethical Business Conduct, Greenwashing.*

I. INTRODUCTION

In today's dynamic business landscape, a strong environmental, social, and governance (ESG) rating is crucial for successful enterprises and investors. "*ESG is a framework that helps stakeholders understand how an organization is managing risks and opportunities related to environmental, social, and governance criteria (sometimes called ESG factors).*"[1] For instance, a company that encourages diversity, and environmental conservation and has robust anti-corruption measures would be considered to have a higher commitment towards ESG Goals.

[*]Student, National Law University, Odisha. Corresponding author's Email: 22bba045@nluo.ac.in.

[**]Student, National Law University, Odisha. Corresponding author's Email: 22ba084@nluo.ac.in.

[1] United Nations Department of Public Information, 'The Global Compact, Who Cares Wins: Connecting Financial Markets to a Changing World' (December 2004) 57899-December 2004-2,000.

Investors use ESG criteria as benchmarks which help evaluate whether the given company is responsible enough and compliant with its stakeholders' expectations. ESG reporting happens when the company provides details about how it performs on environmental, social, and governance issues.[2] Therefore, this reporting may be considered as presenting investors with a broad-stroked snapshot of how the organization impacts key issues for decision-making for consumers in line with their personal values.

The practice of embracing the environmental, social, and governance (ESG) framework has proven beneficial for both investors and companies. Such an approach increases inflows of funds of varied character from different countries, therefore, building up brand value for the company. Consequently, investors get an avenue to match their values with investments, often yielding returns comparable to or better than the traditional approaches, particularly when investing in brands that prioritize ESG values.

Additionally, ESG engagement contributes to a competitive strength in the relevant market. Surveys among consumers and professionals in different fields suggest that a growing number of people are prepared to opt for green products and IT solutions from companies that uphold strong ESG practices.[3]

Moreover, investors and lenders have expressed interest in integrating environmental, social, and governance (ESG) reporting. Businesses seek for investments as an emerging trend whereby earnings reports are coupled with separate "ESG" figures' disclosures. More than one-fourth of investment companies are showing keen interest in sustainable investing funds which project an increase in number within a few years.[4] In response to growing concerns after the COVID pandemic, climate change, and resource misuse, investors are increasingly drawn to businesses aligning with sustainable practices while scrutinizing those lagging behind with outdated approaches.

In addition, ESG covers investor's interests as well as boosting the company's financial results. Simple measures of sustainability such as cutting down on paper usage as well as the adoption of energy-efficient upgrades may increase a company's profitability and provide better returns.[5] Adherence to ESG regulations is also about risk management; it implies less exposure to penalties from regulators for non-compliance of ESG regulations which in turn

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[2] UN Global Compact, 'Private Sustainability Finance'(unglobalcompact.org) <https://unglobalcompact.org/take-action/action/private-sustainability-finance> accessed 26 November 2023.
[3] Anne Field, 'Americans Want To buy Green, But They Don't Trust Companies' (Forbes, 26 June, 2022) <https://www.forbes.com/sites/annefield/2022/06/26/americans-want-to-buy-green-but-they-dont-trust-companies/?sh=2c7c2c2a73f0> accessed 26 November 2023.
[4] Gallup Inc, 'Where U.S. Investors Stand on ESG Investing' (Gallup.com, 23 February 2022) <https://news.gallup.com/poll/389780/investors-stand-esg-investing.aspx> accessed 26 November 2023.
[5] David Silk and Carmen Lu, 'Environmental, Social & Governance Law USA 2023' (ICLG.com, 26 January 2023) <https://iclg.com/practice-areas/environmental-social-and-governance-law/usa> accessed 26 November 2023.

results in stronger earnings. The example of Nestle making the commitment to moving from traditional plastic to food-grade recycled plastics shows that such ESG commitments may be used to reduce costs associated with compliance as well as reduce the carbon footprint of a business.[6]

II. EVOLUTION OF CSR AND ESG NORMS

The Evolution of Environmental and Social Governance in India can be traced back to the amendments to the Companies Act[7] in 2015, which made India the first legal regime to make Corporate Social Responsibility ("**CSR**") mandatory. It is the groundwork that was laid down by CSR which will now help us build a resilient, comprehensive, and transformative ESG framework.

The concept of CSR was aimed at changing how companies function and using a certain amount of profits of the companies for the benefit of society.[8] While this idea does sound wonderful, the lack of effective enforcement has always been a major challenge. According to the KPMG report[9], more than 52 out of the country's 100 largest companies failed to spend the required amount on CSR activities. Amongst these issues, another issue that had arisen was the fact the Companies Act 2013 had no clear guidelines as to what constituted CSR Activities. This led to a lack of transparency and companies not meeting their statutory obligations for CSR Reporting.

Therefore, a need arose for companies across industries to implement sustainability with their business strategy itself, combining sustainability and social obligation with their business ideas itself. This led to the creation of ESG which not only helps in meeting the CSR objectives but also helps get a greater return on investment.

Further, it is important to note that there has been a change in investment patterns wherein investors have now started to incorporate ESG factors into their decision-making.[10] It is important to understand that it is always the role of capital and investors that will drive sustainability efforts more than any obligation that has been imposed on corporate boards.

[6] Nestlé Press Release, 'Nestlé creates market for food-grade recycled plastics, launches fund to boost packaging innovation' (nestle.com, January 16 2020) <https://www.nestle.com/media/pressreleases/allpressreleases/nestle-market-food-grade-recycled-plastics-launch-fund-packaging-innovation> accessed 26 November 2023.

[7] The Companies (Amendment) Act 2015.

[8] The Economic Times, 'What Is Corp Social Responsibility? Definition of Corp Social Responsibility, Corp Social Responsibility Meaning' (economictimes.indiatimes.com, February 18 2024) <https://economictimes.indiatimes.com/definition/corp-social-responsibility> accessed 20 February 2024.

[9] KMPG India, India's CSR Reporting Survey 2015 (December 2015).

[10] So Ra Park and Jae Young Jang, 'The Impact of ESG Management on Investment Decision: Institutional Investors' Perceptions of Country-Specific ESG Criteria' (2021) 9 (3) IJFS <https://www.mdpi.com/2227-7072/9/3/48>.

However, even though ESG is essentially a market-driven concept, regulators around the world including the Securities and Exchange Board of India ("**SEBI**") have framed rules and guidelines for ESG reporting and disclosure.

The first such guideline was in the form of a guidance note issued by SEBI in 2012[11], which mandated top 100 listed companies to file Business Responsibility Reports ("**BRR**") from an ESG perspective. This was then updated in 2015 wherein SEBI issued its LODR Regulations (Listing Obligations and Disclosure Requirements)[12] wherein BRR mandated a more detailed report, such as reporting on Greenhouse Gas Emissions, energy consumption and water usage among others. This circular led to BRR being extended to the top 500 listed companies. Subsequently, over the years, SEBI has been consistently issuing circulars and guidelines[13] to enhance reporting measures.

In a landmark move in May 2021, SEBI radically improved ESG reporting with the introduction of the Business Responsibility and Sustainability Report[14] ("**BRSR**"), it enhanced the scope of ESG and mandated the top 1000 listed companies to file BRSR reports and disclose non-financial performance. Through the BRSR Reporting, SEBI allowed for ESG disclosures in a standardized manner for the listed companies. This led to the creation of a comprehensive set of guidelines which has improved the consistency of ESG reporting in India. The BRSR norms made requirements for ESG Reporting along the lines of the 9 principles given in the National Guidelines for Responsible Business Conduct[15] ("**NGRBC**") which was introduced by the Ministry of Corporate Affairs ("**MCA**") in 2019. In comparison to the BRR norms, the metrics related to climate and social issues have been further expanded and refined for greater attention to detail providing for a more detailed assessment. Further, disclosures related to value chain partners have been made mandatory, ensuring greater coverage of the company's environmental and social impact through its supply chain.[16]

Furthermore, the BRSR framework replaced the five reporting sections of the earlier BRR with a more concise three-section structure. However additional disclosures have been made mandatory within each section therefore enhancing overall reporting.

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[11] SEBI Circular CIR/CFD/DIL/8/2012.

[12] Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 [Last amended on October 23, 2023].

[13] Ministry of Corporate Affairs, Government of India, 'National Guidelines on Responsible Business Conduct' (10 December 2018) <https://www.mca.gov.in/Ministry/pdf/NationalGuildeline_15032019.pdf>.; SEBI (Listing Obligations and Disclosure Requirements) (Fifth Amendment) Regulations, 2019.

[14] Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) (Second Amendment) Regulations, 2012 (No. SEBI/LAD-NRO/GN/2021/22, 5 May 2021).

[15] Ministry of Corporate Affairs, Government of India, 'National Guidelines on Responsible Business Conduct' (10 December 2018) <https://www.mca.gov.in/Ministry/pdf/NationalGuildeline_15032019.pdf>.

[16] Umakanth Varottil, 'The Legal and Regulatory Impetus towards ESG in India: Developments and Challenges' [2023] SSRN Electronic Journal <https://www.ssrn.com/=4323313> accessed 26 November 2023.

The three sections in BRSR include, firstly, the **General Disclosures**, to obtain basic information such as the size, location, and number of employees in the company. Secondly, **Management Disclosures**, wherein the companies must disclose information on policies and processes related to the NGRBC Principles, encompassing leadership, governance, and stakeholder engagement. Thirdly, **Principle-Wise Disclosure**, which requires the companies to disclose the company's performance against the Principles and the Core Elements of the NGRBCs. Companies are required to demonstrate their commitment to responsible business conduct through concrete actions and outcomes.[17]

Further, BRSR requires both mandatory and optional indicators and encourages companies to focus on sustainability challenges, and elaborate on their ESG targets, goals and achievements. Therefore, BRSR serves as an effective mechanism for a company’s non-financial disclosures and is a significant advancement in ESG reporting.

III. CHALLENGES OF ESG REPORTING AND THE WAY FORWARD

One of the biggest challenges faced by regulators during ESG disclosures is the issue of greenwashing. SEBI defines greenwashing as “*making false, misleading, unsubstantiated, or otherwise incomplete claims about the sustainability of a product, service, or business operation”*.[18] Therefore the reliability of the data disclosed by corporations has always been an issue since there exists no way to ascertain the truthfulness or falsity of the allegations. An example of the same can be seen in the fashion industry, wherein clothing brands like H&M have claimed that their clothes are eco-friendly and sustainable, but there have been increasing allegations of increased waste generation and an increase in the carbon footprint.[19]

To combat these issues ESG rating providers (ERP) will have a significant role to play. ERPs are independent agencies that assess entities and provide ratings that help the investor to decide a corporation's commitment towards sustainability. However, in India these ERPs are largely unregulated. To address this issue SEBI in July 2023 amended the SEBI (Credit Rating Agencies) Regulation, 1999[20] to regulate the accreditation of ESG rating providers. According to these regulations a person or an entity that wants to act as an ESG rating provider must obtain a certificate of registration from SEBI.

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[17] Indian Chamber of Commerce & EY India, ‘Business Responsibility and Sustainability Reporting (BRSS)’ (ey.com, 21 April 2023) <https://www.ey.com/en_in/climate-change-sustainability-services/brsr-reporting-and-the-evolving-esg-landscape-in-india> accessed 26 November 2023.

[18] Shiwangi Singh, ‘Evolution of ESG Regime in India: Challenges and way forward’ (iiprd.com, 21 September 2023) <https://www.iiprd.com/evolution-of-esg-regime-in-india-challenges-and-way-forward/> accessed 26 November 2023.

[19] Matthew Stern, ‘H&M Case Shows How Greenwashing Breaks Brand Promise’ (forbes.com, 13 July 2022) <https://www.forbes.com/sites/retailwire/2022/07/13/hm-case-shows-how-greenwashing-breaks-brand-promise/?sh=2f0d59381171> accessed 27 November 2023.

[20] Securities and Exchange Board of India (Credit Rating Agencies) Regulation 1999.

This concept of ERPs is not a novel idea and is prevalent in jurisdictions like the United States of America and the European Union. The USA predominantly has four major ERP'S (MSCI, ISS ESG, Sustainalytics, and FTSE Russell),[21] however, these companies don't have a standardized measure for assessing the performance of a corporation on environmental, social and governance factors. The factors considered for accreditation by these four majors are different which has resulted in chaos and failure in achieving the intended objective.

Therefore, India must take lessons and learn from the mistakes committed by other jurisdictions such as the EU and the USA which are currently a step ahead of India in ESG reporting and regulating ERP'S. To ensure that a similar problem is not faced in India, a standardized comprehensive code is in the need of the hour.

IV. CONCLUSION

In today's volatile global economy, the importance of ESG has significantly increased. ESG can be called both a compass that directs a company towards ethical practices and an integral criterion for the investor wishing to follow ethical norms and values. It offers a pathway to infuse a sense of heart and humanity into the business world, presenting a revolutionary shift needed in today's landscape.

The transition from CSR to a comprehensive ESG reflects a significant shift in the Indian business landscape. The journey from CSR requirements laid out in the Companies Act to the current importance put on ESG reporting shows the country's commitment to transformative business practices.

The mandates by SEBI including the BRSR norms have solidified India's position. These regulations have bolstered transparency, pushing companies to integrate sustainability into their core strategies, ensuring a broader societal impact beyond mere profit accumulation.

However, the part towards a robust ESG framework will not be one without its own challenges. To tackle this, the need for a standardized code to ensure consistency will be crucial. Further learning from the experiences of the jurisdictions such as the USA and the EU, where ERPs do not have a standardized measure, India can regulate ERPs to achieve the intended objectives. Moreover, the role of Independent Directors should not be underestimated and SEBI's recognition of their importance and issue of directives highlighting expertise in ESG subjects will have an integral role to play to drive corporations towards sustainable ESG practices.

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[21] Brian Tayan and others, 'ESG Ratings: A Compass without Direction' (corpgov.law.harvard.edu, 24 August 2022) <https://corpgov.law.harvard.edu/2022/08/24/esg-ratings-a-compass-without-direction/> accessed 20 February 2024.

Going forward, India is at crossroads and must look back to global practices while forging its own independent approach. To follow this route in India, bridging regulatory gaps and ensuring ethical business conduct is essential for building a future where ESG doesn't remain confined as merely a regulatory framework but becomes an intrinsic part of the corporate ethos and the investor decision-making. Mandating ESG practices today may help avoid problems tomorrow, which will enable businesses to grow profitably in a changing economic landscape.

DECODING THE CODE: ALGO TRADING IN INDIA

—Mahira Gupta[*]

Abstract

Algorithmic trading is rapidly transforming global finance through automated, AI-driven systems that enable ultra-fast analysis and execution of trades. In India, algorithmic trading accounts for over 50% of equity transaction volumes and SEBI's regulations aim to harness benefits while minimising risks. Concerns remain around opaque marketing claims and lack of oversight for third-party algorithms marketed to retail investors. This analysis proposes two alternative regulatory approaches customised for India's maturing algorithmic landscape: (i) A voluntary industry Code of Conduct upholding ethical standards around transparency and investor protections without legalistic prohibitions that may constrain participation, and (ii) A specialised Regulatory Sandbox to rigorously stress-test retail algorithms through simulations before controlled launch, allowing vetted strategies to benefit from relaxed promotion norms unavailable normally. Together, these customised mechanisms encourage consultative governance and industry collaboration to balance stability and innovation in this disruptive domain critical to the technological advancement of India's capital markets.

Keywords: *Algorithmic Trading; SEBI Regulations; API Access; AI-driven Finance.*

I. INTRODUCTION

From market monitoring to investment decisions, artificial intelligence algorithms are reshaping global finance; capital markets stand on the threshold of a technology-driven revolution spearheaded by these adept automatons designed to detect patterns and capitalise on opportunities faster than the blink of a human eye. A vanguard technology propelling the ascent of Artificial Intelligence ("**AI**") across global finance is algorithmic trading, also known as algo trading, where intricate AI systems rapidly digest real-time data and events to autonomously execute buy and sell decisions absent human discretion. Algorithmic trading holds immense disruptive capacity. Algo trading uses algorithms, or a pre-defined set of commands, to dictate

[*] Student, NALSAR University of Law, Hyderabad. Corresponding author's Email: mahira@nalsar.ac.in.

the exact criteria for buying and selling stocks and other assets such as futures and options, commodities and currency derivatives.[1]

A simple example to illustrate this is an algorithm instructing the system to buy 100 Infosys shares every time the rupee depreciates 5 per cent against the US dollar. The trades take place faster and manual monitoring is done away with.

In India, to provide an algo hosted and managed by the broker to an investor, the algo requires approval of the respective stock exchange. When the broker orders the algo to the investor, such algo runs on the broker's system and not on the investor's. Whenever the algo generates a signal based on the matched criteria, an order automatically gets punched into the investor's account with no human involvement. Several Indian stockbrokers provide Application Programming Interface ("**API**") access to their clients to establish an online connection between them and their clients. The API access enables a client to use third-party applications or build its front-end features for making investments.[2]

Algo trading is not a new element in India's financial markets. As early as 2008, the Securities and Exchange Board of India ("**SEBI**") had introduced and allowed it.[3] It started with Direct Market Access and for a long period was restricted to institutional investors. In 2012, when stock exchanges started leasing co-location servers to brokers and fintech firms, retail participation displayed marked gains.[4] Subsequently, the regulator introduced board guidelines for algo trading in the securities market.[5]

There has been, however, an exponential increase in the utilisation of algo trading owing to the advent of technology. According to a study conducted by the National Institute of Financial Management in 2018, algo trading has a 50 per cent share of the Indian financial market.[6]

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[1] Jocelyn Fernandes, 'MC Explains | What is algo trading, why SEBI is seeking to regulate the segment' (Moneycontrol, 28 June 2022) <https://www.moneycontrol.com/news/business/markets/algo-trading-rules-all-you-need-to-know-about-why-sebi-is-seeking-to-regulate-the-segment-8748961.html> accessed 29 November 2023.

[2] Prakhar Dua and Kishore Joshi, 'Regulatory Hotline: SEBI'S CONCERNS ON ALGORITHMIC TRADING BY RETAIL INVESTORS' (Nishith Desai Associates, 22 June 2022) <https://nishithdesai.com/generateHTML/6177/4#:~:text=Considering%20that%20the%20algos%20that,'%20interests%2C%20especially%20retail%20investors> accessed 29 November 2023.

[3] Hitesh Malviya, 'Algorithmic Trading Rules and Regulations' (shareindia.com, 2021) <https://www.shareindia.com/knowledge-center/algo-trading/algorithmic-trading-rules-and-regulations> accessed 11 December 2023.

[4] National Institute of Financial Management, 'Report of the Committee on Algorithmic Trading in the Securities Market' (Ministry of Finance, Government of India 2021). <https://dea.gov.in/sites/default/files/NIFM%20Report%20on%20Algo%20trading.pdf> accessed 11 December 2023.

[5] Securities and Exchange Board of India, 'Broad Guidelines on Algorithmic Trading' (Circular CIR/MRD/DP/ 09 /2012, 30 March 2012).

[6] DEA-NIFM Research, 'NIFM Report on Algo trading' (National Institute of Financial Management 2018) 12

II. REGULATORY FRAMEWORKS

SEBI introduced initial algorithmic trading regulations in 2012 to strengthen systems, enhance oversight of algo providers, and address risks. Stock exchanges had to upgrade capacity, enforce limits on order-to-trade ratios and order flooding to detect manipulation, check algo order prices/quantities, and intervene against dysfunctional algos.[7]

Additionally, SEBI mandated periodic audits and pre-deployment software checks in 2013 to improve algo governance. By stipulating that exchanges test algo software pre-rollout alongside requiring brokers to conduct regular audits of systems post-deployment, SEBI aimed to minimise disruptions.[8]

In 2016, SEBI extended governance to commodity derivatives algos while customising certain provisions like order size/price protections, assessing algorithms' impact on price discovery, and evaluating retail liquidity effects before enabling algos in smaller contracts.[9]

Since 2018, SEBI has eased select restrictions to enable greater participation while augmenting transparency. Key relaxations include higher ceilings for order-to-trade ratios and orders per second to support growth, removal of mandatory algorithmic trading auditor empanelment to reduce compliance overheads, and mandated provision of tick-by-tick data feeds to members free of cost to ensure a level playing field. Concurrently, SEBI has expanded oversight such as through 2018 order-to-trade ratio limits encompassing liquidity enhancement scheme orders to cover potential misuse.[10]

Through progressive relaxations to boost innovation alongside measures promoting transparency and continuous risk calibration, SEBI has signalled a balanced approach to governing algorithmic trading. This aims to facilitate ecosystem growth while safeguarding market quality as algo activity rises. For instance, higher order-to-trade ratio limits, supported by audits, checks, and data availability for monitoring, demonstrate preparedness for higher volumes.

III. NEW CHALLENGES

[7] Securities and Exchange Board of India, 'Broad Guidelines on Algorithmic Trading' (Circular No. CIR/MRD/DP/ 09/2012, 30 March 2012).
[8] Securities and Exchange Board of India, 'Memorandum to the Board No. 58/2014 Report of the Depository System Review Committee' (28 July 2011).
[9] Securities and Exchange Board of India, 'Broad Guidelines on Algorithmic Trading for National Commodity Derivatives Exchanges' (Circular No. SEBI/HO/CDMRD/DMP/CIR/P/2016/97, 27 September 2016).
[10] Securities and Exchange Board of India, 'Introduction of Managed Co-location Services' (Circular No. SEBI/HO/MRD/DP/CIR/P/2018/62, 9 April 2018).

A recent regulatory concern is that retail investors utilising third-party algorithms or custom-building algo strategies via APIs escape oversight, as their trades cannot be identified as algorithmic by brokers or exchanges. SEBI rightly worries unchecked algos can enable manipulation and mis-selling.

Hence, in its 2021 consultation paper,[11] SEBI proposed classifying all API orders as algorithmic and requiring unique IDs reflecting exchange approval. It stated brokers must assume responsibility for all trading algorithms on their platforms, with exchanges not recognising external algo creators. Additionally, SEBI sought clarity on whether third-party algo services constitute investment advice. It asked brokers to ascertain if clients obtain advisory services. For transparency, SEBI suggested brokers either use in-house vendor algorithms or outsource from approved external providers.[12] Subsequently, in March 2023, given inadequate investor safeguards and grievance redressal around algo trading, SEBI barred brokers from mentioning past or potential algo profitability/effectiveness. Brokers also cannot partner with entities making such claims. Exchanges must swiftly implement notification changes and secure broker compliance confirmation within 60 days. Through these directives, SEBI aims to extend governance, transparency and accountability to the algorithmic trading ecosystem for investor protection while facilitating innovation.[13]

IV. EFFECT OF THIS CIRCULAR ON RETAIL INVESTORS AND TRADERS

The stock brokers have argued against this regulation. They contend that requiring pre-approval of the multitude of algorithmic strategies activated via application programming interfaces would pose an onerous administrative burden. They note that third-party vendors can design and deploy limitless customised algorithms tailored to discrete client needs, making algorithm-by-algorithm ratification an impractical proposition and less viable than alternate models of accountability. With growing retail participation in online investment platforms, clarity around appropriate regulatory classification is imperative.[14] This issue was highlighted in the action instituted by SEBI against Mr. Amit Mohan Jeswani, the proprietor of Stallion Asset. A settlement order against Mr. Jeswani, a research analyst offering model portfolios seemingly categorised such activities as portfolio management.[15] This is confusing given research reports may cover securities generally. Similarly, the lack of guidance on whether

[11] Securities and Exchange Board of India, 'Consultation Paper on Review of Certain Provisions Related to Preferential Issue Guidelines' (26 November 2021).

[12] ibid.

[13] The Securities and Exchange Board of India, 'SEBI Circular dated March 16, 2023' (Circular No. SEBI/HO/MIRSD/MIRSD-PoD-1/P/CIR/2023/37, 16 March 2023).

[14] Reghu Balakrishnan, 'SEBI comes out with guidelines for stock brokers providing algorithmic trading services' (The Hindu BusinessLine, 12 May 2022). <https://www.thehindubusinessline.com/markets/sebi-comes-out-with-guidelines-for-stock-brokers-providing-algorithmic-trading-services/article65842716.ece.> accessed 11 December 2023.

[15] Securities and Exchange Board of India, Settlement Order No. SO/GR/BM/2022-23/6631, 'In the Matter of Mr. Amit Mohan Jeswani (Proprietor of Stallion Asset)- Research Analyst' (Application No. 6631/2021), 6 May 2022.

third-party algorithm providers are investment advisers muddies obligations. As evinced by this enforcement action, in the absence of transparent rule-making, reactive settlements can engender regulatory uncertainty, allow mislabelling of services, and disadvantage retail investors reliant on fintech innovation. Hence, as retail participation accelerates, proactive steps by SEBI to delineate regulatory perimeters and disclosure requirements for business models like online research, model portfolios, and algorithmic trading tools are needed to enable sustainable growth under proper oversight. It was largely accepted that the regulator's proposed framework had issues because categorising all API trades as algorithmic trades was imprecise and unjust. While the proposal was well-meaning, it risked hampering the thriving API sector. Additionally, the framework would have placed a large burden on stock brokers without considering the essence of algorithmic approaches.

It appears that SEBI's primary worry with algorithmic trading is the misleading marketing of algo services and strategies through touting past returns, predicting future gains, and assigning ratings. While such promotional tactics can undoubtedly entice unaware investors in an undesirable way, SEBI seems to disregard that publicising historical performances is commonplace in securities markets. For example, mutual funds routinely cite previous returns as an indicator of fund success. Another perspective is about how else an investor determines if a particular algo strategy or service suits their needs, without performance parameters. SEBI's move will likely hinder the algo industry since investors have been stripped of a viable metric for judging appropriate algo services or strategies. Without effectively evaluating the benefits of an algo offering or comparing different algos, investors may avoid algorithmic trading services altogether. Algo strategies provided by brokers via third parties or directly would already be approved by exchanges with necessary risk controls in place. By barring brokers from advertising algos' track records, SEBI may inadvertently push investors towards unregulated players that still provide performance markers. Also, past success may not guarantee future gains. This is precisely why such indicators have accompanying disclosures and disclaimers, as with mutual funds.

V. ALTERNATIVES

Some alternatives for the regulation of algo trading are the Voluntary Code of Conduct for Algorithmic Trading Advisors and the creation of a Segregated Regulatory Sandbox for Retail Algo Products.

A voluntary industry code of conduct can promote best practices without heavy-handed regulation. Such a code would enshrine principles around qualifications, transparency, testing protocols, and investor safeguards for algorithmic strategy developers sans formal eligibility criteria or penalties. The code could crystallise norms around robust backtesting, informative disclosures, ethical advertising, risk management, and grievance mechanisms. The code has been developed in consultation with key stakeholders like SEBI and investor associations, and administered via an industry consortium, it would signify adherence to client-centric product

development and commerce. Such a compact would organise the nascent algo advisory space and offer standards for evaluation before potential issues necessitate stern policymaking. It empowers advisors' commitment to equitable, prudent practices. Progressive entities adopting the code gain reputational advantages and client trust.

The success of such a framework can be assessed from some global examples. The UK Financial Conduct Authority maintains a voluntary set of good practice standards for algorithmic trading in wholesale markets. These norms emphasise governance, development processes, operational resilience and fair market access. Adherence is assessed annually.[16] Hong Kong's Securities and Futures Commission instituted a voluntary Code of Conduct for automated trading services. The principles-based code covers risk management, transparency, conflict handling and technology usage. Periodic disclosure of compliance is mandated.[17]

There are certain ways in which the execution for the same can be undertaken. Development can happen via industry working groups consisting of algo developers, advisor platforms, exchanges, SEBI and investor associations. Extensive discussions are critical. The code's administration could be undertaken by recognized self-regulatory bodies like the Association of National Exchanges Members of India ("**ANMI**")[18] or the Association of Investment Advisors ("**AIA**").[19] SEBI will play a critical role in issuing guidance on qualified investor eligibility, given the associated complexity risks. Basic awareness programs for retail investors seem imperative too.

Certain limitations can pose some challenges. Sans formal oversight processes, violations may elicit limited consequences, thereby making the code more symbolic. Client awareness of the code can be low, diluting impact. An industry body administering the code risks conflicts of interest and needs heavyweight sector participation to be credible. However, with proper collaboration among various stakeholders and extensive deliberations, the limitations can be diluted and increase the code's provisions to balance advisor flexibility with investor protection.

Secondly, SEBI could demarcate a supervised regulatory space where only algorithms intended for retail consumption undergo simulated testing before controlled rollout. Rigorously vetted products launched successfully from this sandbox would be certified as "Retail Algo" strategies. The sandbox would facilitate the easing of restrictions around past performance

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[16] Financial Conduct Authority, 'Algorithmic Trading Compliance in Wholesale Markets - Multi-firm reviews' (2018) <https://www.fca.org.uk/publications/multi-firm-reviews/algorithmic-trading-compliance-wholesale-markets> accessed 1 December 2023.

[17] Securities and Futures Commission (SFC), 'SFC supports and sponsors the development of an industry-led voluntary code of conduct for ESG ratings and data products providers' (31 October 2023) <https://apps.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=23PR126> accessed 31 October 2023.

[18] Association of National Exchanges Members of India, estb. 1996.

[19] Association of Investment Advisors, estb. 2013.

advertising and rating assignments for certified products, given their governance. The specialised sandbox allows customised oversight aligned to risks in complex retail algo strategies - protecting investors while supporting innovation. Products proving robust performance and conduct within the sandbox can be offered flexibilities unattainable normally to aid transparency. Priority sandbox access for strategies adhering to specified developmental guardrails could be granted. The Retail Algo label boosts advisor accountability and client trust. The UK FCA pioneered the concept of regulatory sandboxes in Project Innovate. Its framework supervises innovative propositions in a customised environment and extends certain relaxations to vetted products.[20] ASIC's regulatory sandbox for fintech facilitates product piloting before public licensing applications. Extensive consumer data access aids curated testing and oversight.[21]

Executive guidelines that can prove to be helpful are that rigorous pre- and post-market simulations should mimic segments of the live market ecosystem. Controlled exposures to genuine clients will fine-tune safeguard mechanisms and performance. Real-time risk monitoring capabilities are imperative too. Entry criteria must establish safety thresholds, like ethical track records, financial cover and investor protection protocols. Assured sandbox access for public-good innovations could promote inclusion. Exit norms must cover certification terms for retail launch after stringent evaluations of resilience, conduct and return through sandbox testing phases.

It is to be kept in mind that demanding technological and human capital investments are needed to design the bespoke sandbox supporting simulation, surveillance and certification functionalities. Criteria for sandbox entry and certified product advantages need balanced, consultative policymaking. Extensive monitoring is essential along with deterrence mechanisms for violations by certified products. Retail investor awareness regarding the sandbox and brand value of the Retail Algo label warrants nurturing.

VI. CONCLUSION

As algorithmic trading gains dominance globally, India has witnessed proliferating adoption with algos accounting for over half of equity transaction volumes as per recent estimates. In response, SEBI has enacted important regulations around systemic safeguards, governance and access to harness the liquidity and efficiency benefits of algos while improving oversight. However, concerns remain around opacity in performance marketing for retail offerings and lack of supervision for third-party API strategies. Hence, fresh approaches are needed to enable balanced innovation aligned with market risks.

[20] Financial Conduct Authority (FCA), 'Regulatory Sandbox' (First published: 27/03/2022; Last updated: 01/08/2023) <https://www.fca.org.uk/firms/innovation/regulatory-sandbox> accessed 29 October 2023.

[21] Australian Securities and Investments Commission (ASIC), 'Enhanced Regulatory Sandbox' <https://asic.gov.au/for-business/innovation-hub/enhanced-regulatory-sandbox/> accessed 29 October 2023.

This analysis suggests two targeted regulatory alternatives custom-fit for India's maturing algo landscape - a voluntary Code of Conduct underscoring ethical product design alongside transparent disclosures, and a specialised Regulatory Sandbox to rigorously stress-test retail algos before controlled rollout. The principles-based code will promote accountability in the nascent algo advisory space without legalistic prohibitions that can constrain participation. The tailored sandbox allows intensive simulations to evaluate retail algo resilience, with only vetted strategies earning flexibility around access and promotion unavailable normally. This attempts to balance stability and growth by curtailing investor risks from unvetted offerings through tiered evaluations rather than outright bans.

Together, these customised mechanisms recognise the need for consultative governance encouraging industry collaboration to supplement rule-based directives, helping regulation keep pace with relentless disruption. As India charts an ambitious, technology-powered future for her capital markets, agile regulation around algo trading will determine balanced advancement.

CRYPTO IN INDIA: TIME FOR SEBI TO TAKE THE LEAD

—Harsh Mittal[*] *& Anshupal Singh*[**]

Abstract

This article delves into India's cautious approach to regulating crypto-assets and explores the pivotal role that the Securities and Exchange Board of India (SEBI) could play in shaping a comprehensive regulatory framework. SEBI's hesitancy arises from the inherent challenges posed by the decentralised nature of crypto-assets and the divergence between Indian legislation and global benchmarks. The article emphasises the operational intricacies of crypto-assets, including their anonymity and cross-border complexities, which complicate traditional regulatory approaches. Highlighting the potential legal vulnerabilities and global repercussions of inaction, the article argues for SEBI's proactive intervention. Drawing on international examples, it discusses the evolving regulatory landscape in the European Union, the United States, and the United Kingdom, emphasising the need for SEBI to assume a leadership role in India's crypto market regulation.

Keywords: *Cryptoassets; Distributed Ledger Technology; Decentralisation; Securities; Howey Test.*

I. INTRODUCTION

In the dynamic landscape of global financial markets, the emergence of crypto-assets has triggered regulatory responses from advanced economies. Notably, the Securities and Exchange Board of India ("**SEBI**") has adopted a circumspect approach, refraining from active oversight of this burgeoning sector. This cautious stance stems from pivotal factors that delineate the complex relationship between SEBI and the decentralised realm of crypto-assets. Primarily, SEBI's regulatory mandate, inherently tailored for centralised securities, encounters challenges when applied to the decentralised nature of crypto-assets. The divergence in definitions between Indian legislation and global benchmarks, such as the Howey Test in the United States ("**US**"), further accentuates the limited scope of SEBI's authority over these assets. Additionally, SEBI's scepticism, shared with the Indian government, revolves around

[*] Student, National Law University, Odisha. Corresponding author's Email: 21bba019@nluo.ac.in.
[**] Student, National Law University, Odisha. Corresponding author's Email: anshupalsingh1@gmail.com.

the perceived association of cryptocurrencies with Ponzi schemes, exacerbating the regulatory dilemma.

The operational intricacies of crypto-assets on decentralised blockchain networks pose formidable challenges to SEBI's traditional regulatory approaches. The anonymity inherent in distributed ledger technology, coupled with cross-border complexities, amplifies the difficulties in effective oversight and tracing of illicit activities. As the crypto-asset market matures into a trillion-dollar behemoth, SEBI's reluctance to intervene carries potential legal vulnerabilities and undermines global efforts to mitigate financial risks. In this article, the authors examine the implications of India's hesitancy towards regulating crypto-assets, considering the imperative for regulatory frameworks, the potential risks of inaction, and the pivotal role SEBI could play in shaping a comprehensive and consistent regulatory framework for the evolving crypto market.

II. SEBI'S CAUTION: THE SCEPTICISM SURROUNDING CRYPTO-ASSET REGULATION

As advanced economies across the globe embark on regulating the crypto-asset market,[1] the SEBI has refrained from actively engaging in oversight of this burgeoning sector. This stance is primarily driven by these key factors.

First, SEBI's regulatory mandate primarily encompasses securities, and it has consistently maintained that crypto-assets do not fall under the ambit of "securities" as defined under Section 2(h) of the Securities Contracts (Regulation) Act of 1956.[2] Further, in India, the provisions limit its scope to incorporated companies or bodies corporate, unlike the broader definition adopted in the Howey Test[3] of the United States, which focuses on "common enterprises". This limited scope of SEBI's regulatory authority over crypto-assets is a significant factor in its decision not to regulate them.

Second, SEBI and the Indian government have viewed cryptocurrencies sceptically, often associating them with the potential for Ponzi schemes.[4] While India's legal system lacks a specific definition of a Ponzi scheme, the Securities Exchange Commission ("**SEC**") defines[5]

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[1] Coryanne Hicks, 'Cryptocurrency Regulations around the World' (*Forbes*, 3 April 2023) <https://www.forbes.com/advisor/investing/cryptocurrency/cryptocurrency-regulations-around-the-world/> accessed 22 November 2023.

[2] The Securities Contracts (Regulation) Act of 1956, sec 2(h).

[3] *SEC v WJ Howey Co* [1946] 328 US 293.

[4] 'Crypto Currency Is "Ponzi Scheme", Should Be Banned in India: Govt Official' (*Business Standard*, 26 April 2019) <https://www.business-standard.com/article/pti-stories/crypto-currency-is-ponzi-scheme-should-be-banned-in-india-govt-official-119042600794_1.html> accessed 25 November 2023.

[5] 'Investor Alert Ponzi Schemes Using Virtual Currencies' (*Security Exchange Commission*) <https://www.sec.gov/files/ia_virtualcurrencies.pdf> accessed 03 December 2023.

it as an investment fraud where returns to existing investors are generated from funds contributed by new investors rather than from legitimate business activities.

Moreover, Crypto-assets operate on a decentralised blockchain network, also known as distributed ledger technology ("**DLT**"). This decentralised structure poses significant challenges for traditional regulatory approaches, primarily designed for centralised markets like banks or exchanges. SEBI's regulatory authority primarily lies in overseeing centralised securities markets, and the decentralisation of DLT transactions presents a significant hurdle. Furthermore, SEBI has highlighted the anonymity inherent in DLT transactions, where records are stored on dispersed computer nodes across various jurisdictions.[6] This cross-border aspect of DLT transactions further complicates regulatory oversight and the tracing of illegal activities.

III. THE IMPLICATION OF KEEPING IT UNREGULATED

Amid the transformative impact of crypto-assets on the financial landscape, regulatory bodies face the exigent task of crafting effective frameworks. India's continued silence towards crypto-assets, however, presents potential legal vulnerabilities, as discussed below, and hinders the global effort to mitigate financial risks.

First, the crypto-asset market's explosive growth, from the unregulated periphery to a trillion-dollar behemoth, necessitates SEBI intervention. While early regulatory forays, like the SEC's 2000 action against SG Ltd.'s[7] "virtual exchange," encountered minimal resistance due to the market's nascent stage, the current landscape's complexity and size demand a comprehensive regulatory framework. Inaction risks investor detriment, market instability, and potential legal challenges, potentially outweighing concerns about resistance.

Second, a blanket ban on crypto-assets, often cited as a solution to concerns about money laundering and criminal activity, is demonstrably ineffective due to the technology's inherent decentralisation and global reach. The ease of transferring crypto assets through public keys and the distributed nature of blockchain technology, replicated across millions of computers, renders control measures technically infeasible. Consequently, SEBI regulation, rather than prohibition, emerges as the only viable option to mitigate these risks and safeguard investor interests within the burgeoning crypto market.

[6] Sriram Srinivasan, 'Explained: What Are SEBI's Concerns Around Crypto Assets? ' (*The Hindu*, 13 June 2022) <https://www.thehindu.com/business/Economy/explained-what-are-sebis-concerns-around-crypto-assets/article65517621.ece#:~:text=SEBI%20has%20essentially%20flagged%20the,%2C%20Ether)%20as%20also%20non%2D> accessed 17 November 2023.

[7] *SEC v SG Ltd* [2001] 265 F 3d 42.

Third, India's crypto boom saw BitConnect,[8] a Bitcoin Ponzi scheme, soar before crashing, leaving investors with worthless tokens and promoters enriched by a staggering INR 220 billion. This debacle exposes the dire need for SEBI regulation. Clear disclosure rules, investor awareness campaigns, and robust education initiatives are crucial to protect Indian investors from such predatory schemes in the booming, yet unregulated, crypto market.

Moreover, the IMF-FSB paper[9] highlights the near impossibility of unilateral crypto bans, emphasising the global imperative for minimum regulatory standards. Consequently, India's inaction in crypto regulation carries potential legal ramifications and undermines the collective effort to address financial risks.

IV. SEBI: THE CORRECT REGULATOR FOR CRYPTO-ASSET

The booming crypto-asset market has reached a critical juncture, demanding immediate regulatory intervention. With this imperative established, the crucial question arises: which regulatory body is best equipped to assume this responsibility? This section will delve into the compelling arguments for SEBI's leadership in this domain.

First, the government's anti-crypto stance often cites money laundering and criminal activity as justifications, yet evidence suggests this concern is overstated. In 2020, only 0.34%[10] of global crypto transactions were criminal, representing USD 10.0 billion. Moreover, India's current KYC/AML regulations solely bind entities regulated by the Reserve Bank of India ("**RBI**") or SEBI. Should SEBI assume regulatory authority over crypto, these businesses would fall under the purview of these essential safeguards, potentially mitigating unlawful activities to a significant degree.

Second, SEBI has demonstrably shown a willingness to understand cryptocurrencies. Notably, in 2018, it dispatched officials on 'study tours'[11] to the financial regulatory hubs of Japan, the UK, and Switzerland. This initiative facilitated engagement with global financial agencies and fostered a deeper comprehension of regulatory approaches to cryptocurrencies and Initial Coin Offerings (ICOs).

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[8] Parth Shastri, 'Bitcoin Fraud: How Investors Lost Rs 22,000 Crore' (*The Times of India*, 14 August 2018) <https://timesofindia.indiatimes.com/business/india-business/bitcoin-fraud-how-investors-lost-rs-22000-crore/articleshow/65393687.cms> accessed 15 December 2023.

[9] International Monetary Fund and Financial Stability Board, IMF-FSB Synthesis Paper: Policies for Crypto-Assets (IMF and FSB, 2023) <https://www.fsb.org/2023/09/imf-fsb-synthesis-paper-policies-for-crypto-assets/>.

[10] 'The Chainalysis 2023 Crypto Crime Report' (*Chainalysis*, 2021) <https://go.chainalysis.com/2023-crypto-crime-report.html> accessed 10 November 2023.

[11] 'SEBI Sends Officials Overseas to Study Cryptocurrencies, Initial Coin Offering' (*The Economic Times*, 6 September 2018) <https://economictimes.indiatimes.com/markets/stocks/news/sebi-sends-officials-overseas-to-study-cryptocurrencies-initial-coin-offering/articleshow/65708126.cms> accessed 12 December 2023.

Third, SEBI's core mandate is to regulate and develop the Indian securities market. Crypto-assets, particularly those with characteristics similar to securities such as security tokens and tokenized securities, fall within SEBI's existing expertise and regulatory framework. This expertise can be readily applied to crypto-assets, ensuring effective oversight and investor protection.

Fourth, while SEBI and RBI have historically engaged in a regulatory tug-of-war regarding crypto-assets, assigning this responsibility to RBI risks fragmented and inconsistent regulation. Such an approach could create confusion, hinder market development, and ultimately prove detrimental to the nascent crypto ecosystem. Conversely, SEBI's centralised approach, leveraging its established expertise in securities regulation and investor protection, can ensure a streamlined and consistent framework, fostering responsible innovation and safeguarding investor interests.

Additionally, Crypto exchanges have urged[12] the government to designate SEBI as the primary regulator for crypto-assets, citing their closer resemblance to securities like Bitcoin and Ethereum than traditional currencies, which fall under RBI's purview. This aligns with SEBI's existing expertise in securities regulation and investor protection, ensuring a more comprehensive and consistent regulatory framework for the burgeoning crypto market.

V. APPROACH OF DIFFERENT JURISDICTIONS TOWARDS CRYPTO-ASSETS

The once-nascent crypto market, initially met with regulatory scepticism, has matured into a behemoth demanding global attention. As concerns over investor protection, financial stability, and illicit activity rise, jurisdictions worldwide are stepping in to tame the digital frontier. This section delves into the evolving regulatory landscape, focusing on prominent advanced economies wielding their securities exchange boards as the primary instruments of control.

The European Union's historic Market in Crypto Assets Regulation (“**MiCA**”),[13] adopted in June 2023, marks a pivotal step in crypto-asset market regulation. It defines crypto-assets as digital representations of value or rights, transferable electronically via DLT. This regulation is designed to oversee various aspects of crypto-assets, with a particular emphasis on stablecoins, which are crypto-assets that pledge a stable value against official currencies or benchmarks. Here, the European Securities and Markets Authority (ESMA) will assume a key role, issuing

[12] Dave, ‘Crypto Exchanges Want SEBI or a New Entity as Regulator, Not RBI’ (*The Economic Times*) <https://economictimes.indiatimes.com/markets/cryptocurrency/crypto-exchanges-want-sebi-or-a-new-entity-as-regulator-not-rbi/articleshow/82718907.cms> accessed 01 December 2023.

[13] The Market in Crypto Assets Regulation (EU) 2023/1114.

guidelines within 18 months to establish criteria for classifying digital assets within or outside MiCA's scope, addressing potential regulatory ambiguity in this evolving domain.

In the US, the SEC has established itself as the primary crypto-asset regulator. Its 2019 framework,[14] leveraging the 'investment contract' analysis, provides clarity on classifying digital assets as securities. This approach hinges on the 1946 Howey Test,[15] established by the Supreme Court, which determines whether a scheme falls under the Securities Act based on (a) investment of money, (b) in a common enterprise, (c) expectation of profits, and (d) solely from the efforts of others. This framework serves as a valuable precedent for other jurisdictions contemplating crypto-asset regulation.

The United Kingdom ("**UK**"), in 2016, established a pioneering FinTech regulatory sandbox[16] under the Financial Conduct Authority (FCA), fostering innovation within a controlled environment. In June 2023, the landmark Financial Services and Markets Act ("**FSMA**")[17] was enacted, comprehensively revising the 2000 FSMA. This legislation replaces and modernises European Union law, empowering regulators and introducing dedicated chapters on crypto-assets. Notably, the FSMA aims to ensure compliance with anti-money laundering and counterterrorism legislation by crypto-asset firms operating within the UK's financial system.

VI. CONCLUSION

In conclusion, the SEBI has maintained a cautious stance on regulating the crypto-asset market, primarily due to its limited statutory authority over decentralised transactions. SEBI's regulatory mandate is confined to centralised securities markets, and the decentralised nature of blockchain technology poses significant challenges for traditional oversight methods. The Indian government's scepticism and association of cryptocurrencies with potential Ponzi schemes further contribute to SEBI's reluctance. However, the exponential growth of the crypto-asset market, the imperative for a comprehensive regulatory framework, and the need to protect investors necessitate SEBI's intervention. A blanket ban is deemed ineffective, and SEBI's expertise in securities regulation aligns with the characteristics of certain crypto-assets. Considering the global trend of regulatory frameworks led by securities exchange boards,

[14] Security Exchange Commission, 'Framework for "Investment Contract" Analysis of Digital Assets' (*SEC Emblem*, 3 April 2019) <https://www.sec.gov/corpfin/framework-investment-contract-analysis-digital-assets> accessed 13 December 2023.

[15] Seward, 'Sec, Framework for "Investment Contract" Analysis of Digital Assets (2019)' (*Harvard Law Review*, 24 March 2023) <https://harvardlawreview.org/print/vol-132/sec-framework-for-investment-contract-analysis-of-digital-assets-2019/> accessed 01 December 2023.

[16] 'Regulatory Sandbox' (*FCA*, 1 August 2023) <https://www.fca.org.uk/firms/innovation/regulatory-sandbox> accessed 18 November 2023.

[17] The Financial Services and Markets Act 2023 87.

SEBI's proactive engagement becomes imperative to address legal vulnerabilities, financial risks, and align India with international efforts in regulating the evolving crypto landscape.

NAVIGATING THE MAZE OF MARKET MANIPULATION - CREATING EFFECTIVE INSIDER TRADING PLANS

—*Aditya Hiremath*[*] & *Ishwaryah Manikandan*[**]

Abstract

The mechanism of insider trading plans was introduced in India via the 2015 Prohibition on Insider Trading regulations as a means to allow corporate insiders the freedom to legitimately trade in company stock owned by them. The lack of popularity of this mechanism amongst insiders coupled with growing issues of insider trading violations have attracted the attention of the SEBI which has proposed an array of recommendations to restructure the mechanism to make it an attractive option to insiders. The authors of this blog provide an appraisal of the current mechanism of trading plans, followed by details on the shortcomings of the mechanism, a cross jurisdictional analysis of the use of trading plans, and finally suggestions to make trading plans a more attractive choice for insiders.

Keywords: *Insider Trading, Trading Plans, Range-Specific Determinations, Prohibition of Insider Trading Regulations (PIT), Shareholder Interests, Insider's Interests, Market Integrity.*

I. INTRODUCTION

Regulatory studies have long focused on capital markets and the regulations thereof from two angles- one, concerning protecting the rights of stakeholders that are involved in transactions that take place in these markets and two, to the effect one's action within the confines of the market, has on every other stakeholder so involved.[1] In this blog, the authors explore insider trading regulations in India with a special focus on a cross-jurisdictional analysis of the recent consultation paper (henceforth, 'the Consultation Paper') released by SEBI pertaining to the relaxation of the existing regulatory framework.[2]

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[*] Student, Hidayatullah National Law University, Raipur. Corresponding author's Email: aditya.212422@hnlu.ac.in.

[**] Student, Hidayatullah National Law University, Raipur. Corresponding author's Email: mishwaryah.222768@hnlu.ac.in.

[1] Shantanu Dey, 'Insider Trading Regime in India: Learning Lessons from the US and UK Regulatory Experience' (2016) 37 Business Law Review <https://kluwerlawonline.com/journalarticle/Business+Law+Review/37.1/BULA2016004> accessed 13 December 2023.

[2] 'SEBI | Consultation Paper on Providing Flexibility in Provisions Relating to "Trading Plans" under the SEBI (Prohibition of Insider Trading) Regulations, 2015' <https://www.sebi.gov.in/reports-and-statistics/reports/nov-2023/consultation-paper-on-providing-flexibility-in-provisions-relating-to-trading-

I. AN APPRAISAL OF THE CURRENT STATE OF INSIDERS' INFLUENCE ON MARKET BEHAVIOUR

The key piece of regulation concerning insider trading in India is the Prohibition of Insider Trading Regulations ("PIT") of 2015.[3] Alongside countries such as the US and the UK that have implemented the concept of 'trading plans' – India too accommodates such a practice under Regulation 5 of the PIT[4]. However, trading plans have not been well received by insiders in India. A meagre average of about thirty trading plans[5] have been adopted every year in the past five years- a number which is indicative of two things - one, regulatory burden[6] of complying with the strict conditions that these trading plans come with, and two, circumvention of insider trading regulations by way of trading in peer stocks.[7] Now, it follows a logical trail to assume that a policy that is too hard on the people is bound to fail or worse, yet, have people circumvent it.[8] The authors recognise that preserving market integrity and protecting the general public from volatility and adverse selection are vital objectives of these regulations, yet, a circumvention of the same by spurious means such as informed trading in peer stocks by way of the UPSI being fungible[9] ultimately brings about the defeat of this objective.[10] This only underscores the importance of regulations that are not only workable on paper but cognizant of implementational constraints and are made in such a way as to incentivise compliance.[11]

Trading plans, by the strict conditions imposed, may hamper the legitimate dealing of securities by corporate insiders to meet exigencies. In the current framework,[12] trading plans are subject to a slew of regulatory requisites such as 12 months of the minimum coverage period, months of cool-off period, a mandatory blackout period and exemption from the general contra trade restrictions applicable on trade in securities. It is well-acknowledged that the framework is suffocative[13] of insider's interests- a realisation that prompted SEBI to release

plans-under-the-sebi-prohibition-of-insider-trading-regulations-2015_79317.html> accessed 15 December 2023.

3 Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015, Regulation 5.

4 Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015, Regulation 5.

5 Guest, 'Flexible Trading Plans: SEBI's Consultation Paper on Insider Trading Regulations' (*IndiaCorpLaw*, 28 November 2023) <https://indiacorplaw.in/2023/11/flexible-trading-plans-sebis-consultation-paper-on-insider-trading-regulations.html> accessed 15 December 2023.

6 Donald C Langevoort, 'Theories, Assumptions, and Securities Regulation: Market Efficiency Revisited' (1992) 140 University of Pennsylvania Law Review 851.

7 Prachi Deuskar, Aditi Khatri and Jayanthi Sunder, 'Insider Trading Restrictions and Informed Trading in Peer Stocks' (20 June 2023) <https://papers.ssrn.com/abstract=4210203> accessed 13 December 2023.

8 Langevoort (n 5).

9 Deuskar, Khatri and Sunder (n 6).

10 Langevoort (n 6).

11 Park (n 1).

12 'SEBI | Consultation Paper on Providing Flexibility in Provisions Relating to "Trading Plans" under the SEBI (Prohibition of Insider Trading) Regulations, 2015' (n 3).

13 Taxmann, '[Analysis] Insider Trading Reforms | Balancing Regulations with Operational Realities for Effective Implementation' (*Taxmann Blog*, 27 November 2023) <https://www.taxmann.com/post/blog/analysis-insider-trading-reforms-balancing-regulations-with-operational-realities-for-effective-implementation/> accessed 14 December 2023.

the Consultation Paper. Now, the authors of this blog argue that the Consultation Paper itself is not comprehensive in remedying the flaws of Prohibition of Insider Trading Regulations.

II. CROSS JURISDICTIONAL COMPARISON OF THE PROHIBITION OF INSIDER TRADING REGULATIONS

Laws prevailing in the US

In the United States, insider trading regulations permit the exception of trading plans under Rule 10b5-1.[14] These plans give corporate insiders an "affirmative defence to insider trading" by allowing them to carry out trades under trading plans made in advance whilst not in possession of "material non-public information.[15] The defence has been included to strike a balance between restricting injustices on account of information asymmetry and retaining a securities market that is free. Unlike in the Indian context, trading plans have been popular amongst insiders in the USA with the Securities Exchange Commission's 2021 report stating that around 5,800 executives and board members from 1,600 firms engaged in trading activities governed by Rule 10b5-1 plans. Pfizer CEO Albert Bourla previously had his trading plan altered (making for a very profitable transaction for him) a day before positive news of his company's development of the COVID-19 mRNA vaccine was declared.[16] The trade was deemed suspicious on account of its timing. This is an example of how allowing excessive flexibility in trading plans defeats the very purpose of its formulation.

The 2023 amendments to Rule 10b5-1 plans were brought in to correct individual excesses on the part of corporate insiders who had been utilising this mechanism to amass personal gains at the cost of the integrity of the stock market and shareholders' interests.[17] This must be contrasted with the SEBI's intent on amending Regulation 5[18] to encourage trading plan formulation, adoption, and implementation to benefit corporate insiders by removing the excesses of the current regulations – particularly the length of the minimum coverage period of the trading plan, the six months long cooling off period, and the existence of blackout periods. While the US and India may have implemented trading plans as a concept, the legislative intent is fundamentally different between the two;[19] and is reflective of the larger differences in the economic ideology of the two countries. Advocating for a single trading plan mandate, and

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[14] Securities Exchange Act of 1934 § 10(b)5-1, 15 U.S.C. § 78j (2000).
[15] Stephen L Lenkey, 'Cancellable Insider Trading Plans: An Analysis of SEC Rule 10b5-1' (2019) 32 The Review of Financial Studies 4947.
[16] 'Pfizer CEO Sold Millions in Stock After Coronavirus Vaccine News, Raising Questions' (11 November 2020) <https://www.wbur.org/npr/933957580/pfizer-ceo-sold-millions-in-stock-after-coronavirus-vaccine-news-raising-questio> accessed 15 December 2023.
[17] C. Alex Bahn, Alan J. Wilson, 'SEC Adopts Amendments to Rule 10b5-1' (*WilmerHale*, 15 December 2022) < https://www.wilmerhale.com/en/insights/blogs/focus-on-audit-committees-accounting-and-the-law/20221215-sec-adopts-amendments-to-rule-10b5-1> accessed 13 December 2023.
[18] Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015, Regulation 5.
[19] Pranav Saraswat, 'Elements of Effective Insider Trading Regulations: A Comparative Analysis of India and USA' (2020) 10 Nirma ULJ 81.

limits on the quantum of securities are measures that would face stark opposition in the US but were readily accepted in the Indian context.[20]

Insider trading in China

China, on the other hand, takes an iron-hand approach[21] concerning insider trading by absolutely restricting directors and senior management personnel[22] from selling their shareholding in the company whilst they continue to have such office.[23] Although this provision may have the effect of encouraging long-term growth prioritisation and helping in the alignment of managerial interests with that of shareholders' interests, there is no doubt that this provision is highly restrictive and counts as regulatory overreach.

III. BRINGING IN REFORMS: A CRITIQUE ON SEBI'S CONSULTATION PAPER

The SEBI's Consultation Paper[24] is a good place to begin a discourse on the regulatory framework of insider trading in India. The following section pinpoints the points of reforms as suggested by the SEBI and attempts to understand the rationale behind these pointers.

1. Evaluating the Jurisprudence behind Reducing the Cool-off Period

The basis of a cooling-off period in insider trading regulations across the globe is quite simple- the rationale behind the outlawing of insider trading is to protect the general public from adverse selection in the market- now, such adverse selection ceases to exist upon the UPSI becoming publicly available. In essence, the cooling-off period foresees the release of such UPSI to the general public within this statutory window to level the playing field for the general public vis-à-vis the insider. It is unclear as to how a four-month window as opposed to a six-month window would serve better in allowing for public disclosures. Perhaps, the regulator has intended to favour insiders' right to trade in securities. Such a recommendation is welcome as the cooling-off period may symbolically exist to provide an opportunity for the publicization of the UPSI but in essence, the very deferral of the trading plan's implementation serves the purpose of lessening its impact on market dynamics and simultaneously being considerate of the insider's position.

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[20] Dey (n 2).
[21] Company Law, Art 147.
[22] NPC, 'Company Law of the People's Republic of China' (NPC) <http://www.npc.gov.cn/zgrdw/englishnpc/Law/2007-12/12/content_1383787.htm> accessed 15 December 2023.
[23] (Robin) Hui Huang, 'The Regulation of Insider Trading in China: A Critical Review and Proposals for Reform' (9 July 2005) <https://papers.ssrn.com/abstract=753745> accessed 15 December 2023.
[24] Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015, Regulation 5.

2. Altering Durations of Trading Plans to Suit Insiders' Interests

The minimum coverage period, that is, the duration in which the trading plan is to be fully implemented is currently 12 months under the PIT Regulations. The Consultation Paper[25] rightly acknowledges that 12 months as a window of disbursal of funds to the insider is rather stretched and recommends the watering down of this period to 4 months. This is in light of remedying the insider of the otherwise inflexible nature of the insider trading plan under the Regulation that disallows any alteration, modification or complete novation of the trading plan. In essence, making the trading plan an irrevocable commitment- but such reduction of the minimum coverage period does bring the insider much-needed respite as to the immediacy of funds disbursal from the plan.

IV. SUGGESTIONS FOR POLICY CHANGES TO INSIDER TRADING REGULATIONS IN INDIA

Let us suppose that the recommendations of the Consultation Paper are implemented, for example, a corporate insider may make a plan with a cool-off period of four months. However, soon after she makes the plan, she may become aware of her son's sudden critical illness – requiring urgent funds to pay off his medical bills. High-level executives are, by convention, paid heavily by transfer of stock options- and she is no exception. She may sell these securities to fund her son's medical treatment but the trading plan would not only restrict her from making immediate sales to finance such an exigency but also the quantum of shares that she may be able to sell – since she would only be allowed to sell the quantum as disclosed in the trading plan. Such instances leave much to be pondered about the position of the insider concerning these trading plans not improving by much even if the Consultation Paper's recommendations are implemented in toto.

1. Allowing for Selective Trading Plan alterations in Emergency Situations

It is in the authors' opinion, that this situation be remedied by allowing for emergency alterations of trading plans in the interest of justice – upon an application by the insider to the compliance officer and a subsequent inspection and approval. The compliance officer has been endowed with judicial discretion concerning matters related to insider trading throughout the PIT Regulations[26]. The authors suggest that the same office be used to streamline such applications by those in such levels of the corporation that receive a sizable proportion of their income by way of securities. Upon the approval of the same, the application may be forwarded to the stock exchange akin to the disclosure under Regulation 5- after which, the necessary changes are made and the insider is allowed to disburse funds from his shares for his emergency.

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[25] 'SEBI | Consultation Paper on Providing Flexibility in Provisions Relating to "Trading Plans" under the SEBI (Prohibition of Insider Trading) Regulations, 2015' (n 3).

[26] Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015, Regulation 5.

2. Implementing Volume-Specific Application of Trading Plans

A possible course of action to make trading plans more effective could be the establishment of threshold limits on the total size of shareholding of the insiders for the application of trading plans. For example, only 80% of insiders' quantum of shareholding be subject to the application of trading plans. This would ensure that a certain sum be allowed to be freely traded as per changing market requirements – making the trading plan more attractive to insiders while simultaneously ensuring that market integrity is not sacrificed by an infliction of adverse selection. Such a proportion is to be worked out considering the level at which the insider is in within the organisation, shares distributed to him as against his cost-to-company salary and a macroeconomic analysis of the impact of his activity of buying or selling the permissible quantum of shares.

3. Allow for Range-specific determinations of the Quantum of Shares to be traded in Trading Plans

Much like the recommendation 4.4 of the SEBI consultation paper[27] allowing for a price limit to protect insiders from significant adverse price fluctuation, another possible addition to make the trading plan option more attractive is to allow for the creation of trading plans with estimated volume ranges for trades as opposed to specific monetary figures. For example, the trading plan would mention that trades of shares between 40,000 and 50,000 shares would be made on August 1st 2024, followed by a trade of 20,000 to 30,000 shares on 15th September 2024. This would allow a greater deal of flexibility to insiders in their formulation of trading plans.

V. THE WAY FORWARD

Insider trading regulations in India necessitate an approach that is not top-heavy to burden the insider with lofty rules that negate his right to trade in securities but at the same time must cater to the general public's principle right to not be subjected to adverse selection by way of such insiders exploiting their access to UPSI. Unlike the US, the Indian economic set-up cannot be expected to give the insiders complete free rein over their alterations and revocability of insider trading plans as such an approach would endanger shareholder interests. Similarly, the Chinese approach of complete suppression of the insiders' right to trade in securities granted to them is not workable in the Indian context where stock options have become popular. The way forward necessitates a mix of the two and innovations in terms of accommodating these competing interests by way of evolving regulations that fit the Indian context.

[27] 'SEBI | Consultation Paper on Providing Flexibility in Provisions Relating to "Trading Plans" under the SEBI (Prohibition of Insider Trading) Regulations, 2015' (n 3).