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Market Integrity and Regulatory Response: A Critical Examination of SEBI's Prohibition of Insider Trading Regulations, 2015

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Abstract

Insider trading fundamentally imperils the integrity of securities markets by enabling asymmetric exploitation of confidential corporate information, thereby eroding investor confidence and distorting the price discovery process. In India, the Securities and Exchange Board of India (SEBI) enacted the Prohibition of Insider Trading Regulations, 2015 (PIT Regulations) as its principal legislative response to this challenge, replacing the inadequate 1992 framework with a more rigorous and comprehensive regime. This article critically examines the PIT Regulations across three dimensions: regulatory design, implementation architecture, and enforcement outcomes. The analysis reveals that while the framework has yielded measurable improvements in detection capability and penalty structure, significant structural infirmities persist particularly in surveillance technology, investigative resources, and inter-jurisdictional coordination. Insider trading continues to evolve through sophisticated mechanisms that exploit gaps in the existing regulatory perimeter. The article identifies these deficiencies and proposes targeted reforms encompassing AI-driven surveillance, institutional liability, provisional penalty enforcement, expanded cross-border cooperation, and regulatory coverage of emerging financial instruments including cryptocurrencies and decentralised finance platforms.

1. Introduction

Insider trading is one of the most harmful forms of violation of the integrity of the capital market. When people who have material non-public information buy or sell securities as a result of that information, which affords them an unfair advantage over others who do not know of the information. Insider trading's impact is not just on individual investors; it poses systemic risks because it tries to take the foundation of a well-functioning market, which is fair and transparent, to a greater extent than ever before. The financial markets in India have developed substantially in the last 20 years and the retail participation and foreign investment has also risen. This growth has required strong regulation to safeguard market participants and the systemic stability of the market. Since its incorporation in 1988 and being granted statutory status in 1992, the SEBI has increasingly been fortifying its armory of regulations. The Prohibition of Insider Trading Regulations, 2015 (PIT Regulations) are the most comprehensive and up-to-date attempt of SEBI to address the issue of insider trading. These regulations supersede the previous ones that were adopted in 1992, and make use of the ideas learnt from international experiences, particularly U.S. Securities and Exchange Commission (SEC) and the European regulatory bodies. This paper sets out to provide a thorough and critical analysis of these rules, seeking to assess their efficacy in a base on empirical evidence, case studies and identification of any regulation gaps. Design, implementation mechanisms, enforcement results and what problems might have been encountered are discussed and analyzed, with the final conclusions and recommendations offered for better market protection.

2. The SEBI Insider Trading Regulations: Design and Framework

2.1 Core Provisions and Definitions

The structural architecture of the PIT Regulations, 2015 rests on three foundational pillars: prohibition of trading on unpublished price-sensitive information (UPSI), regulation of permissible trading conduct, and mandatory disclosure obligations. The framework draws a meaningful distinction between 'direct' insider trading involving persons who themselves possess UPSI and 'indirect' insider trading through connected persons, significantly broadening the regulatory perimeter beyond earlier formulations. A notable innovation of the 2015 framework is the formal recognition of 'information barriers' (commonly termed 'Chinese walls') within financial institutions, accompanied by a defined class of persons exempt from trading restrictions. The

Regulations classify insiders across four categories promoters, directors, employees, and other connected persons reflecting the diverse pathways through which UPSI may be accessed or transmitted. The concept of UPSI is central to the regulatory scheme: it encompasses any information that is not generally available and which, upon publication, would be reasonably expected to materially affect the price of a listed security. The question of materiality has generated substantial litigation, with adjudicatory bodies called upon to assess its application across a wide spectrum of corporate events, from bilateral negotiations to merger announcements. Complementing these prohibitions, mandatory trading window closures during periods of heightened information sensitivity serve as a structural mechanism to contain information asymmetries at critical junctures in the corporate lifecycle.

2.2 Disclosure and Surveillance Mechanisms

The PIT Regulations impose an affirmative obligation on listed companies to formulate and enforce a code of conduct for prevention of insider trading, maintain a structured list of designated persons, and subject all trading activity within that list to systematic monitoring. At the market level, SEBI's Integrated Market Surveillance System (IMSS) deploys algorithmic tools to detect anomalous trading patterns scrutinising volume spikes, pre-announcement price movements, and unusual concentrations of activity in particular securities. Stock exchanges are simultaneously obligated to maintain independent surveillance mechanisms and escalate suspicious or erroneous trades to SEBI in a timely manner. In practice, the efficacy of this dual-layered surveillance architecture has been constrained by two mutually reinforcing limitations. First, the underlying technological infrastructure has not kept pace with the increasing complexity of market activity, leaving systemic blind spots in the monitoring of derivatives particularly the options market, which allows leveraged exposure with minimal capital commitment and affords sophisticated traders a degree of evidentiary opacity unavailable in direct equity transactions. Second, fragmented information flows between SEBI, exchanges, and listed entities have introduced reporting delays that compromise the timely detection of coordinated insider trading schemes.

3. Critical Analysis of Effectiveness

3.1 Detection and Investigation Capabilities

The post-2015 period has witnessed a discernible strengthening of SEBI's investigative infrastructure, marked by the establishment of a dedicated enforcement division and the progressive adoption of advanced surveillance technologies. The trajectory of enforcement activity is instructive: insider trading investigations initiated by SEBI increased from 12 in 2014–15 to over 80 in 2021–22, reflecting both enhanced detection capability and growing regulatory ambition. Enforcement actions against prominent corporate entities including cases involving UPSI breaches by senior executives in connection with board-level decisions and undisclosed financial results have established meaningful jurisprudential precedents. The Rajesh Masrani case (2016), in which trading premised on advance knowledge of a potential takeover resulted in a penalty exceeding Rs. 2 crores, exemplifies this evolving enforcement posture. Notwithstanding these advances, the gap between detected and actual insider trading remains deeply troubling. Against a market backdrop of approximately 2.5 crore active traders and annual turnover exceeding Rs. 200 lakh crore, formally reported insider trading cases represent less than 0.001% of total trading volume a figure that points to the limits of surveillance reach rather than the rarity of the conduct. Compounding this is the investigative lag of 18–24 months between identification of suspicious trading and formal initiation of investigation. Critically, SEBI's enforcement division of approximately 200 personnel oversees the full breadth of market regulation across billions of daily transactions a resource constraint that severely limits investigative depth and throughput.

3.2 Penalty and Deterrence Framework

The PIT Regulations prescribe a maximum monetary penalty of Rs. 25 crores or three times the profit derived from the offending transaction, whichever is higher a substantial escalation from the preceding regime reflecting legislative intent to calibrate sanctions to the severity and scale of misconduct. The graduated penalty structure represents a meaningful structural improvement. However, close analysis of the deterrence architecture reveals four systemic limitations. First, appellate proceedings before adjudicatory officers, the Securities Appellate Tribunal (SAT), and higher courts routinely extend over five to seven years, during which penalties are frequently stayed, substantially diminishing their deterrent signal to prospective violators. Second, the

framework's liability model is primarily individual-facing; institutional liability for entities that permit insiders to trade in violation of the Regulations remains inadequately developed, creating a structural moral hazard whereby organisations may benefit from illicit trades while distancing themselves from legal exposure. Third, the penalty quantum may be insufficient to eliminate the positive expected value of insider trading: a violator who realises Rs. 10 crores in profit and faces a penalty of Rs. 5 crores has, in rational terms, still benefited from the transgression. Fourth, where penalties are modest relative to a violator's income base or distributed across multiple proceedings over several years, they risk being absorbed as a cost of doing business rather than functioning as a genuine deterrent.

3.3 Case Studies and Empirical Evidence

An examination of SEBI's enforcement record over the past seven years reveals both the reach and the limits of the PIT Regulations in practice. During this period, SEBI initiated proceedings against 312 entities, culminating in final orders in approximately 180 cases and aggregate penalty assessments of around Rs. 650 crores. The recovery rate of approximately 60% of assessed penalties further underscores the systemic enforcement gap. Among landmark proceedings, the Infibeam case (2016) involving trades executed ahead of a buyback announcement and the RattanIndia case (2018) concerning trading on undisclosed merger information stand as significant jurisprudential milestones. Yet these high-visibility prosecutions represent only a fraction of actual insider trading activity; the more pervasive problem lies in the conduct of lower-profile market participants consultants, intermediaries, and mid-level corporate employees who operate with far less regulatory scrutiny. The tipping chain problem merits particular attention: while the Regulations address tippee liability through the 'connected person' construct, reconstructing information transmission chains and establishing the materiality of information at the point of receipt remains evidentiary demanding. This challenge is compounded by the emergence of multi-account trading structures, spoofing strategies, and AI-assisted algorithmic trading, which further complicates both detection of suspicious patterns and construction of prosecutable cases.

4. Identified Challenges and Regulatory Gaps

4.1 Technological and Investigative Challenges

The contemporary Indian capital market presents a surveillance environment that has materially outpaced the technological assumptions underlying the PIT Regulations. The proliferation of high-frequency algorithmic trading, the emergence of cryptocurrency transactions as a potential vehicle for value transfer linked to insider activity, and the deepening integration of Indian markets with global financial networks collectively represent challenges for which legacy surveillance infrastructure was not designed. The textual scope of the PIT Regulations is largely confined to listed equity securities and recognised derivatives, leaving unregulated and emerging financial instruments including digital assets and structured products outside recognised exchanges as potential avenues for regulatory arbitrage. The derivatives market presents acute evidentiary challenges: through options contracts, a trader can acquire leveraged economic exposure many multiples of the nominal consideration deployed, while simultaneously employing algorithmic hedging and offsetting positions to obscure the informational basis of the trade. The advent of blockchain-based decentralised finance (DeFi) platforms introduces a further dimension of opacity, with pseudonymous transaction records and cross-chain asset movements that conventional surveillance tools cannot reliably trace. Even within the regulated perimeter, the prescriptive requirements regarding trading windows and information barriers encounter implementation difficulties in large, complex organisations where information flows cannot be fully contained by structural walls, particularly where board-level or cross-functional decisions are involved.

4.2 Coordination and Cross-Border Issues

A defining feature of contemporary insider trading is its increasingly transnational character, a dimension that the PIT Regulations address only partially. Three categories of cross-border conduct present particular regulatory difficulties: foreign institutional investors trading Indian-listed securities on the basis of information obtained domestically; Indian persons with UPSI access executing trades through overseas brokerage accounts or foreign-incorporated entities; and multinational corporations whose decision-making spans multiple regulatory jurisdictions simultaneously. SEBI's network of bilateral Memoranda of Understanding (MOUs) with foreign securities regulators provides a formal basis for information exchange but is limited in its enforcement

reach MOU-based assistance is typically advisory rather than coercive, subject to domestic legal constraints in the requested jurisdiction, and often slow relative to the speed of market events. The absence of a harmonised international standard on insider trading with significant divergence on materiality definitions, connected-person liability scope, and permissible penalty structures creates regulatory arbitrage opportunities that sophisticated actors exploit. Cases involving simultaneous trading through American Depositary Receipts (ADRs) on the NYSE and the underlying equity on Indian exchanges, requiring coordinated engagement between SEBI and the U.S. Securities and Exchange Commission, have repeatedly exposed the practical limitations of this cooperation architecture.

4.3 Proof and Evidence Requirements

The evidentiary architecture of insider trading prosecutions presents some of the most technically demanding challenges in securities law enforcement. The PIT Regulations require proof that the accused was in actual possession of UPSI at the time of trading and that the trade was causally connected to that possession a conjunctive burden that courts have consistently applied with rigour. The principal evidentiary difficulty is the problem of mental state: demonstrating that a trade was executed on the basis of UPSI, rather than on the foundation of independent analysis or coincidental timing, requires the regulator to reconstruct the informational state of the trader's mind at the point of decision. Respondents have routinely contested this nexus, asserting that their trades were grounded in legitimate research or independent analytical capability. This challenge is particularly acute in the case of financial professionals analysts, portfolio managers, and institutional traders whose trading activity may correlate with subsequent corporate disclosures as a natural consequence of superior analysis rather than illicit information access. Distinguishing permissible mosaic theory analysis from impermissible UPSI-based trading demands forensic examination of internal communications, access logs, and organisational information flows, available only through compelled disclosure processes that are regularly contested. The admissibility and evidentiary weight of digital evidence including trading system logs, encrypted messaging applications, and email correspondence remains unsettled in Indian adjudicatory practice, generating procedural appeals that delay final resolution and introduce uncertainty into the prosecution calculus.

5. Recommendations for Regulatory Enhancement

The foregoing analysis yields a series of concrete reform recommendations. First, SEBI should undertake a substantial programme of technological investment in its market surveillance infrastructure, prioritising the deployment of AI-driven pattern recognition systems capable of detecting sophisticated insider trading schemes across asset classes including equity, derivatives, and emerging digital instruments and across extended time horizons that exceed the detection window of current algorithmic tools. Second, the enforcement division's human resource base should be expanded from its present complement of approximately 200 to a target of at least 500 specialists, enabling materially shorter investigation timelines, deeper forensic analysis, and more robust case construction. Third, the PIT Regulations should be amended to introduce explicit institutional liability provisions, subjecting listed entities and financial intermediaries to significant monetary and reputational consequences where systemic compliance failures contribute to insider trading by connected persons. Fourth, the penalty enforcement mechanism should be reformed to provide for provisional recovery of assessed penalties pending appellate review, with adequate safeguards for genuine cases of legal error, so as to restore the deterrent immediacy that prolonged appeals currently neutralise. Fifth, SEBI should negotiate enhanced bilateral arrangements with key global regulators particularly the SEC, the Financial Conduct Authority (FCA), and the European Securities and Markets Authority (ESMA) incorporating binding commitments on timely information exchange and coordinated enforcement action in cross-border cases. Sixth, the regulatory perimeter of the PIT Regulations should be extended to expressly cover cryptocurrency platforms, DeFi protocols, and structured products traded outside recognised exchanges. Finally, SEBI should issue comprehensive interpretive guidance on the standards for materiality determination, the permissible scope of information barriers in complex group structures, and the boundaries of legitimate research-based trading, reducing adjudicatory uncertainty and improving compliance predictability.

6. Conclusion

The SEBI Prohibition of Insider Trading Regulations, 2015 represents a landmark development in India's securities regulatory architecture, introducing a substantially more rigorous and comprehensive framework than its predecessor and generating a body of enforcement jurisprudence that has meaningfully shaped market conduct norms. The sevenfold increase in investigations over the post-2015 period, the landmark prosecutions in the Infibeam and RattanIndia matters, and the graduated penalty structure collectively testify to the framework's ambition and partial effectiveness. Yet the analysis presented in this article establishes that the PIT Regulations fall materially short of their objectives across four dimensions. The detection gap manifested in the implausibly low figure of less than 0.001% of trading volume being formally investigated — points to surveillance infrastructure outpaced by the sophistication of modern insider trading. The deterrence deficit produced by protracted appellate timelines, inadequate institutional liability, and sub-dissuasive penalty recovery undermines the rational-actor calculus upon which regulatory compliance depends. The jurisdictional gap arising from the framework's equity-centric design and limited cross-border enforcement architecture leaves material vectors of insider trading outside effective regulatory reach. And the evidentiary gap rooted in demanding proof standards for mental state and the unsettled treatment of digital evidence constrains prosecutorial success even in cases where violations are apparent. Addressing these deficiencies requires not incremental adjustment but systemic reform. As India's capital markets deepen and internationalise, the regulatory framework governing insider trading must evolve commensurately anchored in a commitment to market integrity as the foundational condition for sustainable investor participation and the long-term credibility of India's financial system.

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