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Prasanna S,

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No. 08, Arul Nagar, Seera Thoppu,

Maudhanda Kurichi, Srirangam,

Tiruchirappalli – 620102

Phone : +91 94896 71437 – info@iledu.in / Chairman@iledu.in



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OVERVIEW OF INSIDER TRADING WITH SPECIAL EMPHASIS ON THE CASE OF HINDUSTAN UNILEVER VS SEBI

AUTHOR – PRIYANJANA BANDOPADHYAY, STUDENT AT AMITY UNIVERSITY, KOLKATA

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Abstract

Insider Trading can be defined as the illegal or unlawful trading of securities from internal sources of the company based on confidential information, which would not be available to the public and hence causing the trader an unfair advantage. Infamous securities market players like Hiten Dala or Harshad Mehta were involved in Insider Trading Activities in the Indian Market, on the other hand, Players like Michael Milken and Dennis Levin were involved in the International Stock market. Insider Trading which is also classified as a white-collar financial crime has been subjected to legislations in India. The Securities Exchange Board of India (SEBI) has framed rules and regulation in the year 1992 and then revised the rules and regulations again in the year 2002. This paper deals with Insider Trading and the insider trading scandal surrounding the merger of Hindustan Unilever Limited and Brook Bond Lipton India Limited.

KEY WORDS: *Investment Law, Stakeholder Protection, Insider Trading, Material Information, SEBI, Unpublished Price Sensitive Information.*

Introduction to Insider Trading

Infamous Scam-stars like Hiten Dalal and Harshad Mehta have played a major role behind the 1992 securities scam and price rigging. During 1997-2000, a number of companies were also involved in fraudulent practices. These incidents exposed the inefficiency of the market regulation and the questioned the effectiveness of securities laws in India to control the scams and curb fraud of the common investors.

Insider Trading can be defined as the practice of purchasing or selling securities of a public company while having possession of confidential information which is not available to the public. Confidential information or material information refers to any information that may result in a substantial impact of the investor's decision regarding buying or selling of security. Inside traders use unpublished information for their own financial benefit and

growth or in order to avoid loss. Once such material or confidential information is out to the public, it affects the share prices of the company in such a way that it would benefit the insider once it is available. One example of an insider can be a government officer who has access to an economic report before it becomes publicly released or available.

The definition and rules or regulations that govern "insider" can differ significantly from country to country. When insiders, eg, an employee of a corporation who has access to any confidential or strategic information about the company and uses the same information for trading in the company's securities or stocks. Insider trading is considered to be unlawful as it is an unfair practice which disadvantages the other stockholders due to lack of important nonpublic insider information. The exception to this scenario lies when information has been made public such that all concerned investors

can have access to it and thus it won't be considered illegal insider trading.

The securities and Exchange Board of India (Prohibition of Insider Trading) Regulation 1992 does not give a direct explanation or definition of the term 'insider trading'. However, it defines the term 'Insider', 'connected person' and 'price sensitive information'

Insider

"It has been defined under Regulation 2(g) of SEBI (Prohibition of Insider Trading) Regulations,

2015 and divides the term into 3 groups -

1. Who are linked to the company or Corporation
2. Who are connected to the Company or Corporation
3. Persons who are thought or believed to be associated with the firm

It further lays down 3 criteria for a person to meet to become an insider -

1. The Individual must be a natural person or Legal Organization
2. The individual should be linked or appear to be connected
3. By Virtue of such a link, unpublished price sensitive information is acquired".⁸⁷⁴

Unpublished Price Sensitive Information

"The definition of UPSI is provided under Regulation 2(n) SEBI (Prohibition of Insider Trading) Regulation, 2015. It defines UPSI as any information, directly or indirectly, relating to any company or its securities which is not available to the public but upon becoming available it is likely to affect the price of the securities or share and shall, ordinarily including but not restricted to, information relating to the following -

1. Financial information

2. Capital Structure Change
3. Dividends
4. Mergers, de-mergers, acquisition and company development, as well as any other transactions
5. Personnel changes in key Managerial positions
6. Important events as defined under the listing agreement".⁸⁷⁵

Connected Person

"Under Regulation 2(d) of SEBI (Prohibition of Insider Trading) Regulation, 2015 defines a connected person as any person who -

1. is a director, as has been defined in clause (13) of section 2 of the Companies Act, 1956 of a company, or is deemed to be the director of the company by virtue of sub-clause (10) of sec 37 of the Act.
2. occupies the position as an employee or officer of the company or holds a position involving a professional or business relationship between himself and the company, whether temporary or permanent and who may reasonably be expected to have access to unpublished, price sensitive information in relation to that company"⁸⁷⁶.

History and Evolution of Insider Trading

Insider Trading had its origin around the year 1792 in the USA. Thus, laws against Insider Trading were formed strictly in order to put a curb in USA. The enactment of the securities Act of 1933 came because of the market Crash in the year 1929 due to prolonged "lack of confidence of investor" in the securities or share market followed by the Great Depression of US Economy.

From the Indian Perspective, The Thomas Committee was established in the year 1948 as an attempt to curb Insider Trading. It helped the

⁸⁷⁴ SEBI (Prohibition of Insider Trading) Regulations, 2015, Reg. 2(g)

⁸⁷⁵ SEBI (Prohibition of Insider Trading) Regulations, 2015, Reg. 2(n)

⁸⁷⁶ SEBI (Prohibition of Insider Trading) Regulations, 2015, Reg. 2(d)

Securities Exchange Act of 1934 in limiting and reducing insider trading. Further, sec 307 and 308 were added to the Companies Act, 1956 and disclosures by officers as well as directors became mandatory and obligatory. The Sachar Committee in the year 1979 felt a need to modify the Companies Act in view of the risk of workers misusing information related to securities or shares of company to influence the stock prices. The Securities Contracts (Regulation) Act, 1956 was modified in 1986 to curb insider trading by the Patel Committee. In 1989, a proposal was made by Abid Hussain Committee that insiders who are engaged in Insider trading shall be punished by civil as well as criminal actions. In 1992, The SEBI (Insider Trading) Regulations Act, 1992 was passed and got renamed as SEBI (Prohibition of Insider Trading) Regulation, 1992.

Penalty for Insider Trading under SEBI – SEC 15G – "if any insider who –

1. Either on his own behalf or on behalf of any other person, deals in securities or shares of a body corporate which is listed on any stock exchange on the basis of any unpublished pricesensitive information,
2. Communicates any unpublished price-sensitive information to any person, with or without his request for such information except as required in the ordinary course of business or under any law, or
3. Counsels, or procures for any other person to deal in any securities of anybody corporate based on unpublished price-sensitive information,

They shall be liable to a penalty which shall be not less than ten lakh rupees, but which may extend to twenty-five crore rupees or three times the amount of profit made from insider trading, which is higher"⁸⁷⁷.

"Sec 24 of SEBI Act, 1992 –

1. Without Prejudice to any award of penalty by the adjudicating officer under this Act, if any person contravenes or attempts to contravene or abets the contravention of the provisions of this Act or of any rules or regulations made there under, he shall be punishable with imprisonment for a term which may extend to ten years, or with fine, which may extend to twenty-five crore rupees or with both.
2. If any person fails to pay the penalty imposed by the adjudicating officer or fails to comply with any of his directions or orders, he shall be punishable with imprisonment for a term which shall not be less than one month but which may extend to ten years, or with fine, which may extend to 25 crores rupees or with both"⁸⁷⁸.

Why should we control Insider Trading?

1. The Manipulation of securities and Shares of market by using insider trading generally causes loss to a corporation and thus it leads to loss for the investors, or it leads to no investor or profit only for the insiders.
2. Whenever a company faces an insider trading, investors tend to lose confidence in the company and tend to stop investing further in the company and sell all the stocks of the company.
3. If any Insider gets a chance or opportunity to get past the laws with even SEBI regulating all the trading, it decreases the confidence of the investor in the stock exchange operations itself.
4. To have a healthy economy is very important keeping in view that Indian Financial Market is still very low in the domestic investment rate and a

⁸⁷⁷ The Securities and Exchange Board of India Act, 1992, No. 15, Acts of Parliament, 1992(India)

⁸⁷⁸ The Securities and Exchange Board of India Act, 1992, No. 15, Acts of Parliament, 1992(India)

proper financial system in place is must and for that confidence in the market is the most important aspect.

pandemic has also introduced several challenges and problems.

Case Analysis of HINDUSTAN UNILEVER VS SEBI

The case of Hindustan Unilever vs SEBI⁸⁷⁹ is one of the most landmark cases of insider trading and several changes or modifications were brought after the decision given on this case. The main issues centered upon HLL buying 8 lakh brook bond shares about 2 weeks ago before the merger was formally disclosed. The transaction took place on 25th March, 1996 which is only 25 days before the merger of HLL-BBLIL was announced on 19th April, 1996. After investigating for nearly 15 months, SEBI issues a show cause notice to all the Executive directors, Chairman as well to the Company Secretary and the then Chairman of HLL. In March 1998, SEBI prosecuted HLL with the offence of Insider Trading and ordered HLL to pay United Trust of India Compensation and the five HLL and BBLIL common Directors were accused with criminal crimes including insider trading. Following the investigations and orders of SEBI, HLL filed an appeal to the appellate board which upheld the judgment of SEBI.

Key changes after the Judgment were seen as SEBI modified the term under Sec 2(k) with SEBI (Insider Trading) Amendment Regulations, 2002 and added a new provision, Sec 2(ha) to the same amended Act which defined "Price Sensitive Information"

Conclusion

Insider trading activities has been always a long standing practice in the corporate sector and every person wishes to make a profit for himself but this might come at the risk of bringing unequal methods. Despite the fact that numerous laws have been enacted and legislations along with adequate regulatory mechanism have been implemented in order to curb insider trading in today's Society, the

⁸⁷⁹ Hindustan Lever Ltd. Vs Securities and Exchange Board of India, A.I.R 1998 (18) SCL 311 (India)