
REVISITING SEBI'S LEGITIMATE PURPOSE EXCEPTION: IMPLICATIONS OF 2024 AND 2025 AMENDMENTS OF SEBI (PROHIBITION OF INSIDER TRADING) REGULATIONS, 2018 ON CROSS-BORDER M&A AND PRIVATE EQUITY

Shrestha Saha, B.Com. LL.B. (Hons.), St. Xavier's University, Kolkata

ABSTRACT

Insider trading is a significant threat to the integrity of the securities market. The Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015 ['PIT Regulations'] was enacted to curb insider trading by prohibiting sharing of undisclosed information and penalising profiting off such communication or knowledge of such information. The 'legitimate purpose' exception ['the exception'] however enables sharing of such information for legitimate business deals. The recent amendments have made transactions and communication in the securities market more stringent, making it difficult for market participants to take advantage of the exception. This paper aims to provide an understanding of the exception along with the changes brought by the recent amendments of the PIT Regulations and analysing their application in Cross-border Mergers and Acquisition ['M&A'] and Private Equity deals is. It argues that though the recent amendments have brought complex yet necessary changes in the PIT Regulations, it stands as a barrier for the globalisation of Indian market. Thus, rigorous internal control, meticulous vigilance and unambiguous regulatory guidance are essential for its effective application.

Keywords: PIT Regulations, the exception, Cross-border M&A and Private Equity deals.

Introduction

Insider trading, a white-collar crime, is an offence of profiting from communicating, providing, or allowing access to any unpublished information which has the capability of impacting the price of a Company's listed securities on getting so published by an insider, any person who is in possession of such knowledge, and/or connected person. In simple words, Insider trading is an unfair trade practice where insider and/or connected persons and those to whom such unpublished information are communicated profits and the misfortunate investors incur loss. An insider or connected person of a Company in due course attains knowledge about the Company's financial results and activities which will have great impact on the value of their listed shares. Such information is not generally available to the public.

Law-makers understood the need of regulations as a necessity to have a levelled playing field for all market participants. Several Committees were formed namely- The Sachar Committee in 1979 and The Abid Hussain Committee in 1989. The Committees were fixated to penalise insider trading. Securities and Exchange Board of India [SEBI] Act, 1992 imposed heavy fine on a guilty insider. The PIT Regulations stop the insiders from benefiting against the disclosure of UPSI. However, these laws and regulations have plenty of loopholes through which gainers of insider trading slip out from their punishment. One of the major loopholes is the exception introduced in The PIT Regulations as per which communication of unpublished price sensitive information ['UPSI'] by an insider will not be penalised. The 2018 Amendment Regulation adds Regulation 3(2A) where the Board of Directors of Company are given the power whether to make a policy for determination of "legitimate purposes" as a part of "Codes of Fair Disclosure and Conduct". The availability of this exception has been proved to be crucial for Cross-Border M&A and Private Equity deals as it enabled the investor/acquirer form a proper and true image of the concerned company and make sound decision. This exception was introduced with the view of removing any confusion as to which communication of UPSI constituted insider trading. The recent amendments of 2024 and 2025 have made it challenging for defaulters to claim this exception when trading on UPSI. This paper analyses the impact of the recent amendments of the exception and the application of this exception in Cross-border Merger and Acquisition and Private Equity deals.

Research Methodology

The present research study is done analysing the statutory provisions and regulatory guidelines

of Companies Act 2013 and primarily SEBI. For better understanding the private equity fund the study also evaluates and interprets relevant article. The paper employs doctrinal and analytical legal research methodology.

Understanding Insider Trading and UPSI prior the recent Amendments

For analysing the impact of recent amendments, it is necessary to understand provisions of The PIT Regulations defining the essential terms.

Regulation 2(g) and 2(d) defines Insider as –

- a. connected persons, who is or has been during the 6 months prior to the concerned act has been associated with the concerned listed Company or whose securities are to be listed, directly or indirectly, in any capacity- by reason of communication with the Company's officers, or being in a fiduciary or employment relationship or by being director, officer or an employee of the Company or holds a professional or business relationship between himself and the Company (permanent or temporary), having possession of UPSI as well as an immediate relative of a connected person, or
- b. person in possession of or having access to UPSI.

In the Regulation 3(2B) any person holding UPSI pursuant to 'legitimate purpose' is deemed to be an insider.

The Regulation 2(n) defines UPSI as-

any information, relating to a company or its securities, directly or indirectly, that is not generally available which upon becoming generally available, is likely to materially affect the price of the securities and shall, ordinarily including but not restricted to, information relating to the following: –

- i. financial results;
- ii. dividends;
- iii. change in capital structure;

- iv. mergers, de-mergers, acquisitions, de-listings, disposals and expansion of business and such other transactions;
- v. changes in key managerial personnel.

The 'Legitimate Purpose' Exception

The Regulation 3(2A), inserted by The PIT (Amendment) Regulations, 2018, empowers the Board of Directors of a listed company to make a policy for determination of 'legitimate purposes' as a part of 'Codes of Fair Disclosure and Conduct' formulated under Regulation 8. It also provides an explanation defining 'legitimate purpose' - as sharing of UPSI in the ordinary course of business by an insider with partners, collaborators, lender, customers, suppliers, merchant bankers, legal advisors, auditors, insolvency professionals or other advisors or consultants. However, the regulation contains a proviso excluding such sharing which has been done to by-pass the prohibitions of the PIT Regulations. Such insider, under Regulation 2B, are bound to maintain confidentiality of the UPSI.

The Regulation 3(3), however, does not penalise communication or procurement of or access to UPSI to potential investors in cases of takeover, mergers and acquisitions involving securities trading and change of control, or to involved parties for assessing the substantial transaction's feasibility, provided the board of directors of the listed company is of the opinion that the sharing of UPSI is in the best interest of the company.

The exception can, therefore, be used as a shield and not as a sword. Insiders can use this exception to carry out their duties or for substantial transactions, while having best interest for the company. This exception was introduced to ensure that essential corporate functions are not hampered by the strict regulations.

Key Requirements for Invoking the Exception

The exception is not a blanket exemption. Its invocation is subject to certain requirements which are outlined in Schedule C of Code of Conduct for Intermediaries and Fiduciaries to Regulate, Monitor and Report Trading by Designated Persons, Regulation 3(2A) and 3(5) of The PIT (Amendment) Regulations, 2018.

The board of directors or the head(s) of the organisation of every person required to handle

unpublished price sensitive information ensures that a structured digital database [‘SDD’] is maintained, internally, containing the nature of UPSI and the names of those who have shared or to whom it has been shared as well as the Permanent Account Number (‘PAN’) or any other identifier recognised by law, in case PAN is unavailable.¹ Such database must be preserved for eight years or more after the relevant transaction is concluded, or till the conclusion of investigation or enforcement proceedings, if any.²

Changes brought by the 2024 and 2025 Amendments

The PIT (Third Amendment) Regulations, 2024 [‘the 2024 Amendment’] expanded the scope of the definition of ‘connected person’ in Regulation 2(1)(d). The definition now includes any person who has a connection with the listed company or does not have any position in the company but are in regular touch with the company as well its officers, thereby allowing them to directly or indirectly have access to UPSI. The Amendment even substituted ‘an immediate relative’ of connected person with ‘a relative’ of connected person, thereby expanding the ambit of the definition from only close relations to distant relations as well. The definition now includes a person sharing household or residence with a connected person.

The PIT (Amendment) Regulations, 2025 [‘the 2025 Amendment’] made additions, expanding the ambit of ‘UPSI’ under Regulation 2(1)(n). UPSI after the enactment of the amended PIT Regulation mainly includes information relating to-

- i. award or termination of order/contracts not in the normal course of business;
- ii. change in rating(s), besides ESG rating(s);
- iii. fund raising decisions;
- iv. any agreement affecting the company’s management;
- v. fraud or default by the company or its management, or arrest of key managerial personnel, promoter, or director of the company, whether occurred within India or abroad, whereby ‘default’ has the same meaning as in SEBI (Listing Obligations and

¹ The SEBI (Prohibition of Insider Trading) (Amendment) Regulations, 2018, Regulation 3(5)

² The SEBI (Prohibition of Insider Trading) (Amendment) Regulations, 2018, Regulation 3(6)

Disclosure Requirements) Regulations, 2015 ['LODR'];

- vi. resolution plan/restructuring or one time settlement relating to borrowings from financial institutions; filing of winding-up petition and admission of application filed for initiation of corporate insolvency resolution process against the company as a corporate debtor by the Tribunal, approval or rejection of resolution plan under Insolvency and Bankruptcy Code, 2016;
- vii. initiation of forensic audit for detecting financial mis-statement, misappropriation of funds and final forensic audit report;
- viii. giving of guarantees or indemnity or becoming a surety for any third party, not in the ordinary course of business;
- ix. granting, withdrawal, surrender, cancellation or suspension of key licenses.

These changes have made the scope of evading the liabilities of insider trading narrower.

Impact of the exception and the recent amendments in Cross-Border M&A and Private Equity Deals

Competition Act, 2013 ['The Act'] along with the SEBI Regulations governs cross-border M&A and private equity deals.

Section 234 of The Act states that any M&A between companies registered under this Act and companies incorporated in the jurisdiction of those countries which have been notified by the Central Government shall be regulated by the provisions of Chapter XV (sections 230-240) of this Act. The SEBI (Substantial Acquisition of Shares and Takeovers) Regulations 2011 ['SAST'] primarily deals with cross-border M&A. It aims at fair, efficient and transparent acquisition of shares, protecting the interest of minority shareholders of a listed company, i.e. target company. Under SAST Regulation 2011, an acquirer is required to make public announcement of an open offer if they acquire 25% or more of the voting rights of the target company.³ Such an open offer is considered as an UPSI before it is made public.

³ The SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, Regulation 3

The SEBI (Alternative Investment Funds) Regulations 2012 ['AIF'] governs private equity deals. Private equity fund or an alternate investment fund is a privately pooled investment vehicle whereby Indian or foreign investors deposits fund to invest into companies which are generally not listed on any stock exchange.⁴ Private equity firms registered under the AIF Regulations can also acquire control over of a public company and make it private.⁵

An acquirer or investor needs access to UPSI to make sound decisions. The target company's value can be understood by learning it unpublished financial records, future projects, undisclosed liabilities or assets, etc. Due diligence, whereby acquirer or investigates the target company's true position in the market, is necessary to avoid risks. The exception simply provides a breathing space for the acquirer or investor to get informed of such undisclosed information without attracting the complexities of PIT Regulations.

The expansion of the term 'connected person' and including 'a relative' have increased the scope of person to be brought under the PIT Regulations. The definition of 'UPSI' as per the 2025 Amendment is now aligned with the disclosure requirements under Regulation 30 of LODR. These recent Amendments by expanding the definition and ambit of 'connected person' and 'UPSI' has tightened the exchange of non-public information in cross-border M&A and private equity deals by bringing a vast array of people and material information under its regulation. Even the acquirer or private equity fund firms once in possession of any such information relating the target company falling under the scope of the 'UPSI' definition or when the target company or any the 'connected person' gets knowledge of the open offer acquirer is proposing, becomes subject to the PIT Regulations. Thus, along with the digital firewall these amendments has given acquirer or investor, as well as the target company, assurance of a fair and transparent process of M&A or investment.

Conclusion

The exception along with the aforesaid recent amendments creates a balanced environment safeguarding undisclosed material information while facilitating legitimate business transactions such as the cross-border M&A and private equity deals. However, for the smooth

⁴ The SEBI (Alternative Investment Funds) REGULATIONS, 2012, Regulation 2(b)

⁵ Troy Segal, *Understanding Private Equity*, Investopedia, 30 April 2025 (accessed 31 July 2025), [https://www.investopedia.com/articles/financial-careers/09/private-equity.asp#:~:text=Private%20equity%20\(PE\)%20refers%20to,company%20and%20take%20it%20private.](https://www.investopedia.com/articles/financial-careers/09/private-equity.asp#:~:text=Private%20equity%20(PE)%20refers%20to,company%20and%20take%20it%20private.)

and proper application of the exception a robust compliance framework including meticulous maintenance of SDD.

SEBI's digital-based enforcement, though efficient, puts onus on company to determine the 'legitimate purpose' for sharing UPSI, thereby creating loopholes and potential risks of misuse of the exception. For avoiding such risks SEBI has enhanced the ambit of 'connected person' and 'USPI' through its aforesaid amendments.

Besides differing legal provisions of different jurisdictions governing insider trading and acquisition or investment of shares, these amendments have increased compliance burdens which can adversely affect globalisation of Indian market. The inclusion of a person sharing household or residence with a 'connected person' has invited ambiguities.

Additionally, the vast list of information under the definition of UPSI has made any undisclosed information relating to a company or its securities as 'UPSI' if on getting to the knowledge of the public it "*likely*" materially affects the price.⁶ This creates challenges for market participants in differentiating information which can be shared without triggering the PIT Regulations especially during cross-border M&A and private equity deals.

Efficient regulatory guidelines, cross-border cooperation and effective internal compliance measures are crucial for achieving the objective of the recent amendments.

⁶ The SEBI (PIT (Amendment)) Regulations, 2025, Regulation 2(1)