

# WHATS-UPSI?

## Key Themes from SEBI's Recent Orders on Insider Trading



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### Introduction

*Words have no wings but can fly a thousand words.* This Korean proverb is perhaps exemplified best by electronic and social media: which lend, not wings, but veritable rocket-fuel to a staggering quantum of information. Securities regulators around the world have thus evolved tech-savvier avatars to combat market disruption.

Recently, the Securities and Exchange Board of India (“SEBI”) has followed suit. In two sets of orders, it has opined on the dissemination of unpublished price sensitive information (“UPSI”) through digital and social media. Read together, the orders lend valuable perspective on some keenly debated questions, which we discuss in this article.

### The Orders

**WhatsApp Orders**<sup>1</sup>: In 2017, SEBI conducted an extensive investigation on UPSI leakage through closed WhatsApp groups. This led to a slew of adjudication proceedings. Eventually, SEBI held that individuals who had forwarded one-liners summarizing select financial line-items of 11 listed entities through WhatsApp (“UPSI Transferors”) were liable for communication of UPSI under the SEBI (Prohibition of Insider Trading) Regulations, 2015 (“PIT 2015”). In particular, SEBI held that:

- The financial information circulated was UPSI.
- Since the information was circulated in closed private environs, it did not amount to “*Heard on Street*” estimates.
- Irrespective of the source of the leak, since the UPSI Transferors had received UPSI, they were “deemed insiders” under PIT 2015. Onward circulation through WhatsApp therefore amounted to communication of UPSI.

**Manappuram Orders**<sup>2</sup>: On March 19, 2013, market participants received a research report from a renowned brokerage on the Q4 2013 results of Manappuram Finance Limited (“MFL”). The report was subsequently hosted on Bloomberg and discussed on CNBC TV-18. Some recipients offloaded MFL’s shares later that day on-market. A probe revealed that the report had contained UPSI, i.e., MFL was likely to report losses in Q4 (which MFL formally notified the exchanges on March 20, 2013). While relevant officials of MFL and the brokerage settled these violations, proceedings were also initiated by SEBI against the recipients who had sold MFL’s shares – alleging they traded while in possession of UPSI. In these orders, SEBI held that the sales did not amount to insider trading under the SEBI (Prohibition of Insider Trading) Regulations, 1992 (“PIT 1992”) since:

- By widespread distribution to over 2,000 recipients, hosting on Bloomberg and dissemination on television prior to the trades, the UPSI had been rendered “public”.
- The recipients were “innocent tippees”. Since the report was written by a prominent research house and contained disclaimers stating it was based on public information, the recipients had no reason to believe it contained UPSI.

### Key Themes

Interestingly, both sets of orders discussed at length the Report of the High Level Committee to review PIT 1992 (“**Sodhi Report**”), the underlying framework for PIT 2015. We discuss below some key themes that emerge from the orders.

#### **Research reports: kosher content and “proprietary information” defense**

In the WhatsApp orders, the UPSI Transferors argued that the information circulated by them was speculative market chatter based on broker analyses on Bloomberg. Thus, it was generally available information (“GAI”) and not UPSI.

SEBI disagreed and expounded on what was permissible content (and therefore, not UPSI) in communiqués (by extension, research reports) shared by market participants with their clients.

As a result, SEBI appears to have prescribed some bright-lines on research reports:

- (i) **Content:** Research reports on listed companies must be based on (a) GAI, or (b) analyses or estimates of GAI, conducted either by the analyst itself, or by third parties.
- (ii) **Scope of GAI and non-discriminatory access:** In the Mannapuram orders, while not specifically referring to “GAI”, SEBI examined how and through what media UPSI may be made public. It held that UPSI loses its character of being “unpublished” as soon as it is disseminated on non-discriminatory information channels, such as newspapers, television and electronic media platforms. Stock-exchange dissemination was merely one (and not the only) way through which UPSI may be made public.

SEBI also considered the scope of GAI in the WhatsApp orders, quoting the Sodhi Report which provided illustrations of GAI in the context of research reports. In particular, the report stated that research reports priced for purchase in line with market practice to all clients should be considered non-discriminatory, and therefore, GAI.

- (iii) **Sourcing:** Reports including estimates and analyses by third parties on GAI (such as reports hosted on Bloomberg) must appropriately source this content. Further, the author relying on third-party analyses should corroborate it through a “*demonstrable, verifiable trail of well documented and laid down processes*”. Thus, readers would be informed of all relevant sources, and, through an obligation to maintain and disclose sources, authors would be compelled to rely on analyses in the public domain, and not unsubstantiated scuttlebutt that may be UPSI.
- (iv) **Usage of own estimates not UPSI:** SEBI recognized that it was common for brokerages to formulate “*estimate(s) on results based on several factors including financial modelling, management guidance, global factors, meetings with management of listed companies*”. It opined that such estimates are not to be considered UPSI, even if they match formal announcements made later by the listed companies.

#### **Heard-on-Street (“HOS”): not UPSI if shared uniformly**

In the WhatsApp orders, the UPSI Transferors maintained that the circulated information was not UPSI, but HOS. They averred that HOS is a well-recognized practice in the brokerage community whereby analysts publish speculative (sometimes unsubstantiated) forecasts on their coverage companies, often prior to results announcements. SEBI agreed that HOS by itself would not constitute UPSI if released uniformly and without disparity in access. Information received on limited WhatsApp groups would not constitute legitimate HOS activity.

#### **UPSI remains UPSI even if its source/ “leak” is unidentified or unknown**

In the WhatsApp orders, the UPSI Transferors argued that they were merely conduits of information. The original tipper remained unidentified. Accordingly, the UPSI Transferors claimed that the impugned information could not be classified as UPSI. SEBI disagreed, opining that UPSI derived its character by what it was (i.e. information capable of materially affecting the price of securities when made generally available), not who spilled the beans. SEBI maintained that tipper-zero’s identity would, at best, have bolstered (and not negated) the fact that the financial information circulated was UPSI.

#### **Innocent tippees are not liable if they traded in possession of UPSI**

A globally recognized concept, an “innocent tippee” unknowingly receives (without soliciting) UPSI and, without discernible reasons to suspect taint, trades on its basis. The Sodhi Report had advocated including an innocent tippee defense in PIT 2015. However, given underlying complexities in detecting and proving insider trading, this defense was not included.

SEBI noted that whilst adopting PIT 2015, the SEBI board had observed that the determination of innocence of a trader would be on individual facts and circumstances. In the Manappuram orders, SEBI held that the research report recipients had adequately demonstrated their innocence, since the report (a) was authored by a reputed broking entity, and (b) contained a disclaimer stating that it was based on publicly available information (therefore, GAI).

Similarly, in the WhatsApp orders, the UPSI Transferors claimed they were unaware that the messages received by them contained UPSI. However, SEBI held that since the UPSI Transferors were seasoned market participants, they could not feign ignorance of the sensitivity of the information they had received.

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### **Information becomes UPSI much before formal adoption by board/ listed company**

In both sets of orders, SEBI examined when the underlying UPSI came into existence. While the noticees argued that the UPSI had been created only when it was adopted by the board prior to notification to the stock exchanges, SEBI held that the underlying UPSI had come into existence before—when initial versions of the information had been prepared for review by company officials.

Interestingly, similar findings have been recorded by SEBI in its recent orders on [Ricoch India](#) and [United Spirits](#). In both, UPSI was held to be generated significantly in advance of its finality. In United Spirits, holding that UPSI (being a proposed tender offer by Diageo for United Spirits) came to life on the day when the transaction team was convened on email, SEBI noted that while determining the nature of UPSI, “*elements of absolute certainty and finality are irrelevant*”.

These findings are of key relevance for capital raising by listed companies, particularly, for deals launched soon after the end of a financial quarter. Deal-teams should keep this in mind while drawing up timelines.

### **Conclusion**

Through these orders, SEBI has shown itself vigilant and capable of tackling UPSI transfer through modern-day tech. It has manifested a mature outlook towards individuals trading on the basis of information in the public domain, while deep-diving into the concept of “public domain” to include newspapers, the television and Bloomberg within its ambit. In the process, some bright-lines for research reports have emerged. HOS has also been recognized as legitimate research activity, although the regulator has cautioned participants against selective circulation. Innocent tippees have also been exonerated from charges of insider trading.

Finally - it is heartening to note the emphasis SEBI places on the Sodhi Report in its deliberations. The street will hope this signals an era of pragmatic interpretation of PIT 2015 in adjudication proceedings.

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<sup>1</sup> Bajaj Auto Limited, Ambuja Cements Limited, Asian Paints Limited, Wipro Limited, Mindtree Limited and Bata Limited.

<sup>2</sup> BNP Paribas Asset Management, IDFC Asset Management Company, SBI Funds Management Private Limited, Aditya Birla Sunlife AMC and Kotak Mahindra Life Insurance.

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