Contemplation Of Legal and Ethical Aspects of Insider Trading

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Abstract:
On insider trading, policymakers are ambivalent. An insider trade is the act of trading shares of a publicly-traded company based on factual, nonpublic information about the company. The Securities and Exchange Commission in the United States has declared insider trading damaging to the financial sector and has regulated it since 1934. Communicating insider trading fraudulent conduct is questionable. In most countries, laws and rules are enacted without considering the harmful and beneficial aspects. Insider trading is illegal since it undermines the public's trust in the capital markets and provides insiders with an unfair advantage/enrichment. A lack of fair play makes illegal insider trading detrimental to small investors and markets. By delivering more informed equilibrium pricing, insider trading contributes to the economy's overall welfare. Despite being a source of consternation for investors, insider trading can sometimes serve as a 'leading indicator.' The criminal justice system has several provisions for dealing with fraudulent transactions. This study analyzes the need for statutory provisions regarding insider trading and examines whether or not an insider trading law is redundant.
Keywords: morality, ethics, insider trading, law, cases,

Introduction

Insider trading is not illegal in all cases and cannot be deemed unlawful. Economic policies cannot go beyond utilitarian ethics. For three centuries, the philosophy and economic theories derived from utilitarianism and morality have been followed. How far utilitarianism ethics influence insider trading policies (Riley, 2016). The Securities and Exchange Commission has banned insider trading since 1934, declaring it harmful to the economy. Most countries do not analyze the negative and positive aspects before making laws and policies. The government should be concerned if an individual takes property from another person without their consent, but what if the adult individuals receive free support? In such non-fraudulent transfers, governmental interference is contentious. If the aggrieved party seeks justice, they are entitled to remedies under contract, tort, and criminal law. Existing civil and criminal laws deal with fraudulent behavior, breach of contract, and property crimes. There is no need for statutes governing insider trading. Proclaiming insider trading as fraudulent activity is dubious.

Insights into the ethical implications

In the trading world, insider training is acquiring or selling stock based on confidential information about a company, enabling the trader to profit or avoid the loss for the trader's benefit (Kennon, 2020). An ethical system or structure is one in which what is right and wrong is delineated. There are often ethical issues in business because of the actions of managers or finance staff. A fiduciary is a term used to describe someone who represents the interests of another party for a fee. (Finance for Managers, 2012). Insider trading is characterized by fraud, unfairness, and unethical business practices, and, as a result, the insiders lack ethical principles and values. The information era has advanced significantly, yet unethical information leakage has been rampant (Gallaugher, 2015). Most ethical breaches occur as a result of unauthorized access to nonpublic information. (Insider Trading and Business Ethics, 2018, and Insider Trading, n.d). It could be argued that insider trading could be divided into legal and illegal categories. To engage in legal insider trading, a company must routinely report to the Security and Exchange Commission regarding its trading activities.

Traders define illicit trading insider as buying or selling stock outside the trust and confidence of a company. It is considered illegal trading when an employee uses or gives confidential company information to family and friends to make financial decisions before the information is made public. If the company manager buys or sells stock based on information provided by the company to the SEC and reports the transaction to the SEC, it will be considered legal. (Insider Trading, n.d). Ethical violations can occur at all levels of a business organization, at the professional level, and at the individual level (Business Ethics, n.d., and Insider Trading, n.d.).

Insinuation on the legal front

Trading in a public company's stock or other securities based on material, nonpublic information about the company can result in undue profits or avoid losses. (Jagolinzer, 2009). If convicted of insider trading, a person could be imprisoned for 20 years or fined up to $5,000,000. Organizations convicted of the same offense could be fined up to $25,000,000. Additionally, individuals and organizations are potentially subject to forfeiture of earned income and penalties that will be nearly three times the amount of profit made or loss avoided. If they fail to do so, insider traders will face a maximum fine of $1,000,000, and 3rd parties will sue them for causing them losses. Several sources describe insider trading in more detail (Insider Trading and Business Ethics, 2018). Those who provide the SEC with information about insider trading can be rewarded with a bonus, thus prosecuting insider traders. Violators may be charged with banking fraud, wire fraud, mail fraud, computer fraud, securities fraud, false statements, obstruction of justice, racketeering, and money laundering. (Jagolinzer, 2009). Insider trading is prohibited because it hurts the public's confidence in the capital markets, enriches insider traders unfairly, and pulls the economy downward. (Business Ethics, n.d).

Implications for socio-economic development

Individuals and entities may suffer non-punitive collateral consequences, such as the revocation of professional licenses. The possibility of disciplinary proceedings by a state licensing board, leading to a suspension or revocation of the request. Legal proceedings like these can impact the overall market conditions and the families of investors. Small investors and the markets lose a great deal when insider trading is illegal because there is no fair play and there is no reasonable demand and supply for stocks, thereby adversely affecting the functioning of the capital markets and the confidence in their health. (Clark, n.d).

The act of committing fraud or stealing securities is known as insider trading. When certain parties in the market are trading on insider information that isn't available to the rest of the market, the broader market becomes skewed, and the prices of securities become skewed. Illegal insider trading adversely affects a healthy relationship between shareholders and businesses. Many publicly traded companies rely heavily on the people who buy their stock. The people mentioned above may stop investing because of ethical and legal scandals, i.e., insider trading. This, in turn, harms the socio-economic development of any country. (Clark, n.d). The Securities and Exchange Commission (SEC) Regulations render insider trading a backdoor activity. There shouldn't be any abstract rules. Instead, they should emerge spontaneously as a product of the embedded economy. Commitment to social good prevents traders from engaging in illegal trading in an informed manner. According to some researchers, there is a link between CSR and insider trading. It shows that corporate social responsibility is directly linked to insider trading. Insider trading is provocative for investors, and it can also be viewed as a 'leading indicator.' Insider trading contributes to the economy's overall welfare by providing a more informative equilibrium price. Information-based trades have primary cross-sectional implications for the broader market.

According to the study, corporate social responsibility (CSR) is positively related to legal insider trading. Many U.S. companies with high CSR ratings do not engage in illegal or unethical insider trading (Cui, Jo, and Li, 2014). In the current state of the market, insider trading represents an unpresidential favorable result compared to the state of the market in the past. These abnormal returns attract the other participants (HOGAN, 2005). According to research, there is a tiny amount of evidence to imply that insider trading may affect the well-being of ignorant stakeholders in the study. At the same time, however, it also contributes to the overall well-being of the economy (Hatchondo, 2002). This is because preannounced prize announcements impact the relative market shares as well. Corporate insiders, employees, tippees, and analysts are all considered informed traders (TOOKES, 2008). According to the SEC's rules 10b5-1, the social negotiation on insider trading regulation provides an affirmative defense against illegal insider trading. This paper analyzes the latent impact of the Securities and Exchange Commission's (SEC) law of insider trading Rule 10b5-1 adversely affective regulation (Bozanic, Dirsmith, & Huddart, 2012).

Case Study on Tyco's Leadership Failure and White Collar Crime

More than $170 million in misappropriated property is at issue in this case. Denis Kolwoski, the CEO, and Mark Schwartz, the CFO, were accused of stealing the property and security funds through insider trading, embezzlement of company funds, conflict of interest, and accounting fraud. Aud. Their theft amounted to approximately $430 million. Since this case is the most significant representation case attempted in a state court, several legitimate investigators have been monitoring closely to see if state judges will follow the lead of government courts, which have imposed severe penalties on corporate officials accused of white-collar crimes (Kemmerer & Shawver, 2007). This case examines Tyco International's embarrassment in 2002, when the national television channel of the United States depicted one of its most notable CEOs, Dennis Kozlowski, in cuffs after he was caught misusing the company's cash to conceal information about top managers and investors (Cracking down on white-collar crime, n.d.).

The organization's leaders were involved in the corruption cases, and the top management abused its power. Leaders of the company and senior management are expected to make ethical decisions. Their decisions should be in the interest of the company as a whole. They misused their power for their benefit rather than for the company's use. Mark Schwartz. Denis Kolwoski and Mark Schwartz stole the money from the company and paid high commissions to finalize the deal. In addition to wasteful spending for their benefits and inappropriate discharge of employees, they have also wasted much money for their help and Engaged in wasting much money for their benefits.

The whole situation amounts to corruption committed by the CEO, Denis Kolwoski, and Mark Schwartz's CFO.
Both leaders were engaged in controversial essential employee loan and loan forgiveness programs ('Tyco international scandal: Case analysis, n.d.) ('Cracking down on white-collar crime,' n.d.). It is expected that the leaders will engage in high moral activities. The decisions and actions of the leaders of an organization have a direct impact on its operations and functioning. Those leaders who have the power to be involved in unlawful and unethical activities are those leaders to whom decision-makers have access. Leaders are expected to be paragons for their employees because they strive to imitate their behavior ('Ex-Tyco CEO Kozlowski, jailed in $100M fraud scheme, loses bid for new New York parole hearing', 2015). A response to unethical behavior on the part of the CEO has forced the company to change its chief executive officer. A decision was made that the company would appoint a new CEO with good ethical values so that the other employees would also be inclined to follow him. The company then developed its moral codes and guidelines for employee conduct. This ethical policy and procedure are available in many languages to make it easier for everyone to understand and act by the new guidelines, regardless of their cultural background. To understand the ethical values among top managers, the company conducted a study on its own. The former Tyco executive Dennis Kozlowski and two former employees have been prosecuted in a Manhattan court. It is expected that the use of the federal court system to deal with the bad corporate behavior of American corporations will energize those in search of a solution. Although, this is only the commencement of a long battle that will last long ('The corner,' n.d.).

Insider trading and the Indian judicial system

Satyam has been involved in a scam that is well known to everyone. A significant part of the Satyam Scam involves corporate governance issues and suspicions that there is a cooperation between auditors and chartered accountants in committing fraudulent auditing procedures at Satyam. This resulted in fabricated financial statements delivered to all company stakeholders, including the board of directors, stock exchanges, regulators, and investors.
The scam involves fabricating financial information about a company to deceive both the market and other stakeholders of that company. By overstating basic figures such as sales, operating profit, interest liabilities, and cash balances to create the impression that the company was healthy, it was possible to deceive the public into thinking that the company was in good shape. Despite this, it is tough to manipulate such data without the cooperation of the auditors and certain members of the executive board. According to some reports, independent directors have been unaware of the company's books of accounts (Satyam Scam, 2015). A stock market regulator ruled that T A N Murti, the head of investor relations at Satyam Computer Services Ltd (SCSL), fell foul of anti-insider trading rules following his appointment as head of investor relations. The Sebi investigation revealed that Murti traded SCSL shares despite knowing unpublished pricing sensitive information (UPSI) ('Satyam Computer Services Case,' 2020).
The 2015 Regulations clarified the definition of an insider in significant ways. Currently, an insider is defined as someone related to another individual or who possesses or has access to undisclosed price-sensitive information. Since 2015, an insider is no longer required to meet the 1992 Regulations' second requirement; they must be a linked person as defined in the 1992 Regulations. They compare the term used in the 1992 Regulations with the disjunctive r in the 2015 Regulations. Therefore, the first half of the 1992 Regulations' Regulation 2(e)(i) cannot be upheld.

Furthermore, under Regulation 2(e)(i), it must be reasonably anticipated that the linked person will be able to access price-sensitive information that has not been published. It is not sufficient to use "reasonably expected." by itself. It must be demonstrated that such an individual can access undisclosed price-sensitive information. The decision adequately specifies the function of the term as it is defined in Regulation 2(e) (i). Additionally, the decision correctly recognized the terminology change between the previous version of Regulation 3 and the amended one of 2002 and compared the statement derived from the phrase "while in possession."

Moreover, the minority ruling refers to and relies on the findings of the SFIO, which proved that B. B. Ramalinga Raju and his collaborators manipulated financial statements and had them hidden by the company's board of directors, among which the Appellant is included as a member. On the assumption that the falsification of the financial figures (which constitute the UPSI in this instance) was concealed from Satyam's Board of Directors, it would be difficult to conclude that the Appellant owned UPSI let alone traded on it. The Appellant, as a director, must be found in violation of the PFUTP Regulations if he was aware of the falsification of financial statements. In the Appellate Court's Impugned Order, the WTM dismisses the accusation of a PFUTP violation for lack of evidence. This proves unequivocally that the Appellant CSR never possessed UPSI. The WTM's conclusion that the Appellant broke PIT Regulations during this period is determined to be unsustainable legally.

The Appellant cannot be classified as a promoter based on his signature on the annual reports as a director, which did not indicate that he was a promoter. The Appellant's name was mentioned behind his back because B. Ramalinga Raju and B. Rama Raju referred to him as a promoter merely in letters addressed to various stock exchanges without the Appellant's knowledge or approval. It is also implied in the minority decision that the Appellant's shares were not subject to a lock-in period during the merger of SES and SCSL, as is required by law for promoters. The Appellant was one of the individuals misled by B. Ramalinga Raju and his brother B. Rama Raju. Unfortunately, I became a victim of the former Chairman of SCSL's deception (Chintalapati Srinivasa Raju and Ors. V. Securities and Exchange Board of India, 2018).

Operation of joint ventures and insider trading

Satyam Computer Service Ltd. (SCSL) sent a letter about its financial situation to different stock exchanges and the Securities and Exchange Board of India (SEBI) to demonstrate fake financial positions. In addition to being a brother of Chintalapati Srinivasa Raju, he was also a cousin of Ramalinga Raju. Chintalapati Srinivasa Raju was Satyam enterprise solutions Private Limited (SES). SES was a joint venture between SCSL and Satyam. He stated that SCSL held 80% of the shares and that he owned 20% of the claims. The article says 80% of the shares are owned by SCSL and 20% by Chintalapati Srinivasa Raju. The promoters of the SCSL were B. Ramalinga Raju and B. Rama Raju accused Chintalapati Srinivasa Raju of being oblivious about the books of account of SCSL. A regulation called the SEBI (Prohibition of Insider Trading Regulations), 1992 prohibits insider trading for any personal gain. This means that the connected person cannot engage in insider trading. SCSL's book of accounting, which was fabricated and members had access to that information throughout the process, was untrue. Chintalapati Srinivasa Raju was alleged to be an insider who sold the shares of SCSL. The denial of being an inside trader by Chintalapati Srinivasa Raju is most salient because he was not the only promoter but also the co-brother of Ramalinga Raju. The court found complicity based on the accused being a family member. The Supreme Court of India decided against the accused, Chintalapati

Srinivasa Raju (Chintalapati Srinivasa Raju and Ors. v. Securities and Exchange Board of India, 2018).

The regulatory framework in curbing insider trading:
The security exchange board of India proposed a draft to regulate insider trading in December 1991.SEBI keeps working to protect the interest of investors in India. SEBI proposed putting some restrictions on insiders for unpublishing price-sensitive information and prohibiting the dealings for his benefit. The proposed draft became a regulation in 1992 known as the exchange Board of India (insider trading) regulations 1992. The law has three chapters. The first chapter defines the person who is connected and has information. The prohibitions are imposed on that connected person to keep the unpublished information confidential. The second chapter talks about some issues prohibited from dealing with, communicating, or concealing specific matters. The last part gives SEBI power to investigate the cases related to insider trading. In 2015 new regulation was introduced, and many unique aspects were added. Every connected person shall be an insider who has access to or positions on unpublished price-sensitive information. Several new words were introduced in 2015, for instance, board, trading day, promoter, securities, specified, trading, etc. ('Sebi Insider Trading Regulations,' 2015).

Maintaining the integrity of the markets:
In N Narayanan V. Adjudicating Officer Sebi, India's Supreme Court ruled that SEBI must protect investors' interests from companies' leadership. Investor confidence can be maintained by safeguarding investments. A company's administration should maintain transparency and disclosure. Supreme Court issued instructions to monitor investors' confidence in the market in this case. In the said case, the company had severe irregularities in its books of accounts. According to SEBI, the company manipulated its accounts by making false entries, making false disclosures, refusing to cooperate with SEBI, and improperly accessing account books. The Supreme Court dismissed the appeal. Many leaders and directors engage in different insider trading activities, which SEBI has to deal with. The court deemed it a severe crime that could hamper the country's economic growth. It is unfortunate that the real honors of the company, i.e., investors and subscribers, are not respected. Regardless of what the community considers about the company, the management keeps hold of it. Electronic and print media should ensure that people know of misleading and fraudulent claims. In the case of N Narayanan v. Adjudicating Officer Sebi, the wrong prediction about the company by the media people was regarded as an abuse of the market.

Supreme Court of the United States on Insider Trading
In the United States and other Subordinate courts, insider trading has been developed based on the theory of fiduciary duties to protect shareholders' interests. There are many ways courts have developed arguments against insider trading prohibition. Section 10(b) of the Securities Exchange Act 1934 and Rule 10b-5 of the Securities Exchange Act 1934 are interpreted in other legal contexts to analyze insider trading as fraud.
Accessing privileged information puts the permit holder in a fiduciary obligation not to disclose or use that information. In terms of the security markets, a common saying goes, "Knowledge is money." A challenge can be filed against the coat if nonpublic information is used to gain an unfair advantage. On the issue of when unique and valuable knowledge becomes an unfair advantage, there are many competing arguments. If the disclosure will

not harm the corporation, disclosing information before a transaction is consummated in certain jurisdictions is unnecessary. Dissenting opinions exist on this point.

Absence of Pre-Existing Fiduciary Obligations: Chiarella Case of United States

In the case at hand, the United States Supreme Court acquitted the defendant Chiarella of all felony charges of insider trading. Chiarella received little information about being a journalist in the Pansick Press in New York. According to the accused, Chiarella conducted extensive research to deduce the company's name and made several transactions. Over 14 months, Chiarella made around $30,000. He had been condemned for the crime in the lower courts, but the Supreme Court overturned that conviction.

It cannot be contended that there is a rule such as 'equal information for all, so there cannot be criminal liability based on a lack of equivalent knowledge. A recent case involving Chiarella has led Justice Powell to argue that Chiarella is not required to disclose his knowledge-based information to other trading partners. The common law supports the processor of superior information against any criminal liability where the others have scant information.

Chiarella had no obligation to disclose the information to the shareholders. He did not give any misrepresentation or information; instead, he remained silent. Chiarella was saddened by the duty he had to perform toward Paddick. Pick never accuses Chiarella of failing to fulfill his duty. Due to the lack of a pre-existing fiduciary relationship between Chiarella and the other traders, he was acquitted of the charges.

Strong v. Rapid is a case where the Supreme Court explained the dissenting opinion based on the case's specific facts. In his view, Justice Blackmun believed that if any particular piece of information is received due to a unique position, this asymmetric information creates particular points. In this case, the information passed through the site where Chiarella worked. Therefore, this scope of the fiduciary relationship should be interpreted in light of the specific facts.

Raymond Dirk was exonerated from all insider trading charges by the United States Supreme Court. The subject of fraud in equity funding was brought to Raymond Dirk's attention as he worked in a broker-dealer firm in New York City. Specifically, he received information about the matter from Roland Secrist, a former equity funding officer.

The information is something that Darks used in the market before making it public. The company has charged Darks for insider trading. Darks was not directly involved in any of the stock transactions. Nevertheless, according to the judgment of Supreme Court Justice Powell, it is clear that there is no existence of any fiduciary relationship between Dirks and stakeholders. Raymond Dirks was simply doing an analysis that any other analyst would do. He was given some insider information to assist him in the study.

Conclusion

Insider trading is the act of trading securities based on material, nonpublic information, which results in undue profits or avoidance of losses. Unethical behavior disregards the rules of business, laws, and principles of securities trading. Economics-Socio misbehavior provides benefits to perpetrators or avoids losses to the perpetrators. Economic-Socio misconduct undermines public confidence, faith, and trust in the capital markets. Insider trading consequences are penalties, imprisonment, disgorgement of profits, and cancellation of licenses.

As of now, data indicates that insider trading benefits the market while causing no harm to any individuals or groups. Therefore, this law will likely decrease the efficiency of the market. There is a need for insider trading prohibition in those countries, not just in India, the U.K., or the United States. The lack of a definition of "insider trading" has been the most vocal complaint about U.S. law. As a result of the courts defining "crime" on their own, this significant omission has increased litigation. Congress is to be blamed for this omission to be given due credit. It is now illegal to carry out insider trading, but no one knows it. It is expected that many genuine transactions will be avoided due to the new insider trading regulation and that the market will likely react negatively. Thousands, perhaps even hundreds of people and brokerage firms will undoubtedly be prosecuted for things that, Years later, following tens of thousands, maybe even millions, of dollars have been spent on legal fees, the courts will determine that these people and firms were completely innocent. In the last few years, the international financial markets have grown and developed significantly regarding how securities are traded and the range of assets sold. A country's economy depends on the integrity of its securities market, and the regulator must implement laws that prevent market abuse to ensure the integrity of the market. As a result of this development, markets are becoming truly global, thereby enabling traders to trade almost instantly through various items and on several markets all across the globe.

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