

TAX FLASH NEWS

SEBI issues Circular on disclosure and process requirements for ESOPs for listed companies

Background

The Securities Exchange Board of India (SEBI) on 28 October 2014 had notified new regulations¹ for share based employee benefits which had replaced the erstwhile Employee Stock Option Plan (ESOP) guidelines². Under the new regulations, certain details/processes had to be prescribed by SEBI.

SEBI vide Circular dated 16 June 2015 (Circular) has specified the necessary guidelines relating to disclosure and process requirements under the new regulations.

Key guidelines issued in the Circular

Regulation 3(3) - Minimum provisions in trust deed

This regulation mentioned that SEBI may specify the minimum provisions to be included in the trust deed under which the trust is formed, and such trust deed and any modifications thereto shall be mandatorily filed with the stock exchange in India where the shares of the company are listed. Pursuant to the New Regulations, SEBI vide its Circular has now specified the minimum provisions to be mentioned in the trust deed. Following are some of the provisions to be included:

- Details of the trust like name, object, details of settlor, source of funds etc.;

¹ SEBI (Share based employee benefits) Regulations, 2014 notified on 28 October 2014

² SEBI (Employee stock option scheme and employee stock purchase scheme) guidelines, 1999

- Powers and duties of the trustee(s);
- Provisions for dissolution of the trust.
- Trust deed shall provide that it would be the duty of the trustees to act in the interest of employees who are beneficiaries of the trust; and subject to provisions of the regulations, it shall not act in any manner or include any provision in the trust deed that would be detrimental to the interests of the beneficiaries;
- Any other clause for safeguarding the interests of the beneficiaries.

Regulation 5(3) - Terms and Conditions of schemes to be formulated by the Compensation Committee

This regulation provided that the compensation committee shall formulate the detailed terms and conditions of the schemes which shall, inter alia, include the provisions as specified by SEBI. SEBI vide the Circular has now specified such terms and conditions:

- Quantum (per employee and aggregate) of option/Stock Appreciation Rights Scheme (SARs)/share/benefit;
- Kind of benefits to be granted under the General Employee Benefit Scheme (GEBS) and Retirement Benefit Scheme (RBS);
- Conditions of lapsing of the benefit in case of termination of employment for misconduct;
- Exercise period;
- Specified time period for exercising the vested options/SARs in the event of termination or resignation of an employee;
- Right of an employee to exercise all the options or SARs, as the case may be, vested in him at one time or at various points of time within the exercise period;

- Procedure for making a fair and reasonable adjustment to the entitlement including adjustment to the number of options/SARs and to the exercise price in case of corporate actions such as rights issues, bonus issues, merger, sale of division and others;
- Grant, vesting and exercise of shares, options or SARs in case of employees who are on long leave;
- Eligibility to avail benefits under GEBS and RBS in case of employees who are on long leave;
- Procedure for cashless exercise of options/SARs.

Regulation 6(2) - Contents of the explanatory statement to the notice and resolution for shareholders meeting

This regulation specified that the explanatory statement to the notice for calling general meeting and the resolution proposed to be passed by shareholders for the schemes in the general meeting, shall include the information as specified by SEBI in this regard which has now been specified vide Circular. The same have been mentioned hereunder:

- Brief description of the scheme(s);
- Total number of options, SARs, shares or benefits, as the case may be, to be granted;
- Classes of employees entitled to participate in the scheme(s);
- Requirements of vesting and period of vesting;
- Maximum period within which the options/SARs/benefit shall be vested;
- Exercise price, SAR price, purchase price or pricing formula;
- Exercise period and process of exercise;
- Appraisal process for determining the eligibility of employees for the scheme(s);
- Maximum number of options, SARs, shares, as the case may be, to be issued per employee and in aggregate;
- Maximum quantum of benefits to be provided per employee under a scheme(s);
- Whether the scheme(s) is to be implemented and administered directly by the company or through a trust;
- Whether the scheme(s) involves new issue of shares by the company or secondary acquisition by the trust or both;
- Amount of loan to be provided for implementation of the scheme(s) by the company to the trust, its tenure, utilisation, repayment terms, etc.;
- Maximum percentage of secondary acquisition that can be made by the trust for the purposes of the scheme(s);
- Statement to the effect that the company shall conform to the specified accounting policies;

- Method which the company shall use to value its options or SARs;
- Statement confirming disclosures of difference between employee compensation cost using intrinsic value method and the fair value method and its impact on the profits and earning per share of the company, in the director's report (if applicable).

Regulation 10(b) - Information required in the statement to be filed with stock exchange(s)

This regulation mentioned that a statement as specified by SEBI in regards to listing, is filed and the company has obtained an in-principle approval from the stock exchanges. The details to be mentioned in the said statements has been now been specified vide Circular. The same have been mentioned hereunder:

- Authorised share capital of the company;
- Issued share capital of the company as on date of institution of the scheme/amendment of the scheme;
- Date of institution of the scheme/amendment of the scheme;
- Validity period of the scheme;
- Date of notice of Annual General Meeting(AGM)/Extraordinary General Meeting (EGM) for approving the scheme/for amending the scheme/for approving grants under regulation 6(3) of the New Regulations;
- Date of AGM/EGM approving the scheme/amending the scheme/approving grants under the New Regulations;
- Kind of benefit granted under the scheme;
- Identity of classes of persons eligible under the scheme (like permanent employees, permanent employees outside India, permanent employees of subsidiary, whole time directors etc.);
- Total number of shares reserved under the scheme, as applicable;
- Number of shares entitled under the grant;
- Total number of grants to be made;
- Maximum number of shares, options, SARs or benefits to be granted per employee per grant and in aggregate;
- Exercise price or pricing formula;
- Amount payable, if any at the time of grant along with the quantum of such amount;
- Lock-in period, vesting period, exercise period under the scheme;
- Maximum period within which the grant shall be vested;

- Whether employee can exercise all the options or SARs vested at one time?
- Whether employee can exercise vested options or SARs at various points of time within the exercise period?
- Whether scheme provides for the procedure for making a fair and reasonable adjustment to the number of options or SARs and to the exercise price in case of rights issues, bonus issues and other corporate actions? Clause in scheme describing such adjustment;
- Description of the appraisal process for determining the eligibility of employees under the scheme;
- Specified time period within which vested options or SARs are to be exercised in the event of termination or resignation of an employee;
- Specified time period within which options or SARs to be exercised in the event of death of the employee;
- Whether scheme provides for conditions under which options, SARs, or benefits vested in employees may lapse in case of termination of employment for misconduct? Clause in scheme describing such adjustment;
- Whether scheme provides for conditions for the grant, vesting and exercise of options, SARs or benefits in case of employees who are on long leave? Clause in scheme describing such adjustment;
- Whether amount paid/payable by the employee at the time of the grant of the options, SARs or benefits will be forfeited if the employee does not exercise the same within the exercise period? Clause in scheme describing such adjustment;
- Details of approval of shareholders pursuant to specified with respect to:
 - i. Grant to employees of subsidiary or holding or associate company.
 - ii. Grant to identified employees, during any one year, equal to or exceeding one percent of the issued capital (excluding outstanding warrants and conversions) of the company at the time of grant;
- Details of the variation made to the scheme along with the rationale therefor and the details of the employees who are beneficiary of such variation.

The Circular also specifies the documents and the undertakings to be filed along with the the registration statement to the stock exchange(s).

Regulation 10(c) - Format of notification for issue of shares

This regulation mentioned that as and when an exercise is made, the company shall notify the concerned stock exchange as per the statement specified by SEBI in this regard. Format of the same has now been prescribed in the Circular. Following are few points to be included:

- Company name and address of registered office;
- Name of the stock exchanges on which the company's shares are listed;
- Filing date of the statement referred in regulation 10(b) of the SEBI (Share Based Employee Benefits) Regulations, 2014 with stock exchange;
- Filing number, if any;
- Title of the scheme pursuant to which shares are issued, if any;
- Kind of security to be listed issued;
- Par value of the shares;
- Date of issue of shares;
- Number of shares issued; etc.

Regulation 14 - Disclosures by the board of directors

This regulation specified that in addition to the information that a company is required to disclose, in relation to employee benefits under the Companies Act, 2013, the board of directors of such a company shall also disclose the details of the scheme(s) being implemented, as specified by SEBI in this regard.

The Circular has now specified the details, to be disclosed in the board of directors report and on the company's website. Further, link of such website is required to be provided in the directors report.

- Relevant disclosures in terms of the 'guidance note on accounting for employee share-based payments' issued by Institute of Chartered Accountants of India (ICAI) or any other relevant accounting standards as prescribed from time to time;
- Diluted earning per share on issue of shares pursuant to all the schemes covered under the regulations shall be disclosed in accordance with 'Accounting Standard 20 - Earnings Per Share' issued by ICAI or any other relevant accounting standards as prescribed from time to time;
- Specified details related to :_
 - ✓ Employee Stock Option Scheme (ESOS);
 - ✓ Employee Stock Purchase Scheme (ESPS) including disclosures in respect of grants made;
 - ✓ SAR;
 - ✓ GEBS/RBS;
 - ✓ Trust including amount of loan disbursed, loan outstanding etc. and brief details of transactions in shares by the trust.

Regulations 16(2) and 23(3) - Disclosure document

As per this regulation, no ESOS or SARs shall be offered unless the disclosures, as specified by SEBI, are made by the company to the prospective option/SAR grantees.

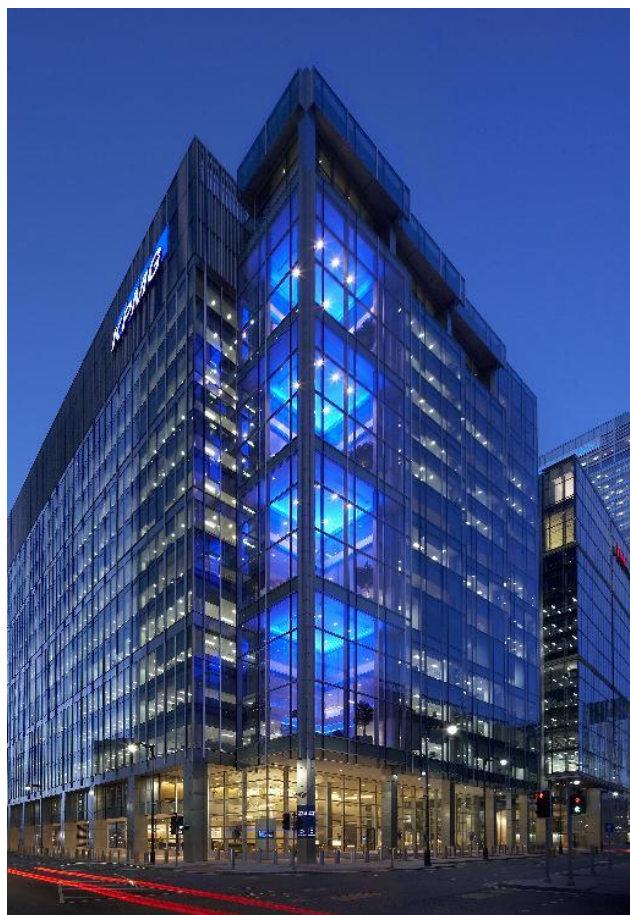
Following disclosure documents have now been prescribed by SEBI in the Circular:

- Part A – Statement of risks elaborating the specified risks related to concentration, leverage, illiquidity, vesting of SARs;
- Part B – Specified information about the company;
- Part C – Salient features of the scheme.

Our comments

Guidelines prescribed in the Circular would assist the companies in complying with the requirements laid down in the SEBI (Share Based Employee Benefits) Regulations, 2014 in relation to Equity Linked Incentives given to the employees. The disclosures in the director's report related to ESOPs has been elaborated.

Guidelines also provide for specific terms and conditions and disclosure requirements for the ESOP trusts. Therefore the listed companies operating ESOP schemes through trusts need to review their current trust deeds and disclosure requirements and comply with the SEBI (Share Based Employee Benefits) Regulations, 2014 by 27 October 2015.



www.kpmg.com/in

Ahmedabad

Commerce House V, 9th Floor,
902 & 903, Near Vodafone House,
Corporate Road,
Prahlad Nagar,
Ahmedabad – 380 051
Tel: +91 79 4040 2200
Fax: +91 79 4040 2244

Bengaluru

Maruthi Info-Tech Centre
11-12/1, Inner Ring Road
Koramangala, Bangalore 560 071
Tel: +91 80 3980 6000
Fax: +91 80 3980 6999

Chandigarh

SCO 22-23 (1st Floor)
Sector 8C, Madhya Marg
Chandigarh 160 009
Tel: +91 172 393 5777/781
Fax: +91 172 393 5780

Chennai

No.10, Mahatma Gandhi Road
Nungambakkam
Chennai 600 034
Tel: +91 44 3914 5000
Fax: +91 44 3914 5999

Delhi

Building No.10, 8th Floor
DLF Cyber City, Phase II
Gurgaon, Haryana 122 002
Tel: +91 124 307 4000
Fax: +91 124 254 9101

Hyderabad

8-2-618/2
Reliance Humsafar, 4th Floor
Road No.11, Banjara Hills
Hyderabad 500 034
Tel: +91 40 3046 5000
Fax: +91 40 3046 5299

Kochi

Syama Business Center
3rd Floor, NH By Pass Road,
Vytilla, Kochi – 682019
Tel: +91 484 302 7000
Fax: +91 484 302 7001

Kolkata

Unit No. 603 – 604,
6th Floor, Tower – 1,
Godrej Waterside,
Sector – V, Salt Lake,
Kolkata 700 091
Tel: +91 33 44034000
Fax: +91 33 44034199

Mumbai

Lodha Excelus, Apollo Mills
N. M. Joshi Marg
Mahalaxmi, Mumbai 400 011
Tel: +91 22 3989 6000
Fax: +91 22 3983 6000

Noida

6th Floor, Tower A
Advant Navis Business Park
Plot No. 07, Sector 142
Noida Express Way
Noida 201 305
Tel: +91 0120 386 8000
Fax: +91 0120 386 8999

Pune

703, Godrej Castlemaine
Bund Garden
Pune 411 001
Tel: +91 20 3050 4000
Fax: +91 20 3050 4010