India | Tax & Regulatory | < > January 2015

Regulatory Alert
Tracking change

SEBI (Share Based Employee Benefits) Regulations 2014

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In this issue:

Background

- SEBI notified SEBI (Share Based Employee Benefits) Regulations 2014 (Regulations). The Regulations are effective from 28 October 2014. With the enactment of the Regulations, the SEBI (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999 (ESOP Guidelines) are repealed.
- The Regulations have now given recognition to the concepts of Stock Appreciation Rights, General Employee Benefit and Retirement Benefit with a view to align this with global trends in employee compensation practices. Accordingly, the provisions of the Regulation are applicable to the following:
  - Employee Stock Option Scheme (ESOS)
  - Employee Stock Purchase Schemes (ESPS)
  - Stock Appreciation Rights Scheme (SARS)
  - General Employee Benefits Scheme (GEBS)
  - Retirement Benefits Scheme (RBS)

The key features of the Regulations are summarized below.

Applicability

- The provisions of the Regulations are applicable to any company whose *shares* are listed on a recognised stock exchange in India, and has a scheme:
  - for direct or indirect benefit of *employees;* and
  - involving dealing in or subscribing to or purchasing securities of the company, directly or indirectly; and
  - satisfying, directly or indirectly, any one of the following conditions:
    - the scheme is set up by the company or any other company in its group;
    - the scheme is funded or guaranteed by the company or any other company in its group;
    - the scheme is controlled or managed by the company or any other company in its group.

For the purpose of the Regulations, the terms ‘employee’, ‘group’ and ‘share’ are defined as under:

- “Employee means, —
  - a permanent employee of the company who has been working in India or outside India; or
  - a director of the company, whether a whole time director or not but excluding an independent director; or
  - an employee as defined in above clauses of a subsidiary, in India or outside India, or of a holding company of the company or of an associate company but does not include —
    - an employee who is a promoter or a person belonging to the promoter group; or
    - a director who either himself or through his relative or through anybody corporate, directly or indirectly, holds more than ten percent of the outstanding equity shares of the company.
- Group means 2 or more companies which, directly or indirectly, are in a position to, —
  - exercise 26% or more of the voting rights in the other company; or
  - appoint more than 50% of the members of the board of directors in the other company; or
  - control the management or affairs of the other company;
- Share means equity shares and securities convertible into equity shares and shall include American Depository Receipts (ADRs), Global Depository Receipts (GDRs) or other depository receipts representing underlying equity shares or securities convertible into equity shares.”

Implementation of schemes through trust

- A company may implement schemes either directly by setting up an irrevocable trust (to be decided upfront). If the scheme involves secondary acquisition or gift or both, then it is mandatory for the company to implement such scheme through a trust.

- A company may implement several schemes, as permitted under the Regulations, through a single trust, provided it maintains proper books of accounts for each scheme to give at any point of time the financial position of each scheme and to give a true and fair view of the state of affairs of each scheme.
- SEBI may specify minimum provisions to be included in the trust deed. The trust deed has to be filed with the stock exchange in India where the shares of the company are listed.
- A director, key managerial personnel or promoter of the company or its holding, subsidiary or associate company or any relative of such person; or a person who beneficially holds 10% or more of the paid-up share capital of the company cannot be appointed as a trustee.
- The trustees of a trust shall not vote in respect of shares held by such trust in order to avoid any misuse arising out of exercising such voting rights.
- The trustee should ensure that appropriate approval from the shareholders has been obtained by the company in order to enable the trust to implement the scheme and undertake secondary acquisition.
- The Trust shall not deal in derivatives, and shall undertake only delivery based transactions for the purposes of secondary acquisition.
- The company may lend money to the trust (subject to requirements of the Companies Act) on appropriate terms and conditions to acquire the shares either through new issue or secondary acquisition.
- The shareholding of the trust shall be shown as ‘non-promoter and non-public shareholding’ for the purpose of disclosure to the stock exchange. However, such holding shall not be considered as ‘Public Shareholding’ which needs to be maintained at the minimum of 25% of the total equity capital of the company.
- The trust shall not become a mechanism for trading in shares and shall not sell the shares in secondary market except under certain specified circumstances.
- The trust shall be required to make disclosures and comply with the other requirements applicable to insiders or promoters under the SEBI (Prohibition of Insider Trading) Regulations, 1992.

Other key highlights

- An employee shall be eligible to participate in the schemes of the company as determined by the Compensation Committee.
- To align it with 2013 Act, independent directors have been excluded from the category of eligible employees to whom share based employee benefits can be granted. Further, a permanent employee or Director of an Associate Company has been covered in addition to those of the Company, its Subsidiary and Holding Company as an employee to participate in schemes.
- The Compensation Committee shall be constituted as provided under the Companies Act, 2013 (2013 Act). The Compensation Committee shall formulate detailed policy and administer the policies and procedures for the implementation of schemes.
- A company shall have the freedom to implement cash settled or equity settled SAR Scheme. In case of equity settled SAR Scheme, if the settlement results in fractional shares, then the consideration for fractional shares should be settled in cash. No scheme shall be offered to employees of the company unless approved by shareholders by passing a special resolution in the general meeting of the company. SEBI will prescribe details of disclosure to be made in the explanatory statement. Approval of shareholders through separate resolution in the general meeting to be obtained in case of:
  - Secondary acquisition for implementation of the schemes;
  - Secondary acquisition by the trust in case the share capital expands due to capital expansion undertaken by the company;

Transition period

- All listed entities having existing schemes are required to comply with Regulations within a period 1 year.
- A longer transition period of 5 years is provided for the following:
  - For the purpose of employee benefits schemes, to bring down the holding of trust in the shares within the prescribed limits;

- For GEBS / RBS, to decrease the holding of shares by trust upto 10% of total value of total assets of the trust;
- Re-classifying shareholding of existing employee benefit schemes separately from 'promoter' and 'public' category.

Conclusion

The Regulations provides flexibility to corporates to structure employee benefits similar to those offered by multinational companies in developed economies. This would facilitate companies to attract and retain talent which is likely to be an issue as the Indian economy is poised for re-bound.

Source: SEBI (Share Based Employee Benefits) Regulations 2014 dated 28 October 2014.

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Contacts

Ahmedabad
Heritage, 3rd Floor,
Near Gujarat Vidyapith,
Off Ashram Road,
Ahmedabad – 380 014.
Tel: + 91 (079) 2758 2542
Fax: + 91 (079) 2758 2551

Bangalore
Deloitte Centre, Anchorage II,
100/2, Richmond Road,
Bangalore 560 025.
Tel: +91 (080) 6627 6000
Fax: +91 (080) 6627 6010

Chennai
No.52, Venkatanarayana Road,
7th Floor, ASV N Ramana Tower,
T-Nagar,
Chennai 600 017.
Tel: +91 (044) 6688 5000
Fax: +91 (044) 6688 5050

Coimbatore
Shanmugha Manram
41, Race Course,
Coimbatore
Tamil Nadu - 641018
Tel: + 91 (0422) 439 2801
Fax: +91 (0422) 222 3615

Delhi/Gurgaon
Building 10,
Tower B, 7th Floor,
DLF Cyber City,
Gurgaon 122 002
Tel : +91 (0124) 679 2000
Fax : + 91 (0124) 679 2012

Hyderabad
1-8-384 and 385, 3rd Floor,
Gowra Grand S.P.Road,
Begumpet,
Secunderabad – 500 003.
Tel: +91 (040) 6603 2600
Fax:+91 (040) 6603 2714

Kolkata
Bengal Intelligent Park Building Alpha,
1st floor, Block EP and GP Sector V,
Salt Lake Electronics Complex,
Kolkata - 700 091.
Tel : + 91 (033) 6612 1000
Fax : + 91 (033) 6612 1001

Mumbai
Indiabulls Finance Centre,
Tower 3, 28th Floor,
Elphinstone Mill Compound,
Senapati Bapat Marg, Elphinstone (W),
Mumbai – 400013
Tel: + 91 (022) 6185 4000
Fax: + 91 (022) 6185 4101

Pune
106, B-Wing, 7th Floor,
ICC Trade Tower,
Senapati Bapat Road,
Pune – 411 016.
Tel: + 91 (020) 6624 4600
Fax: +91 (020) 6624 4605

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