



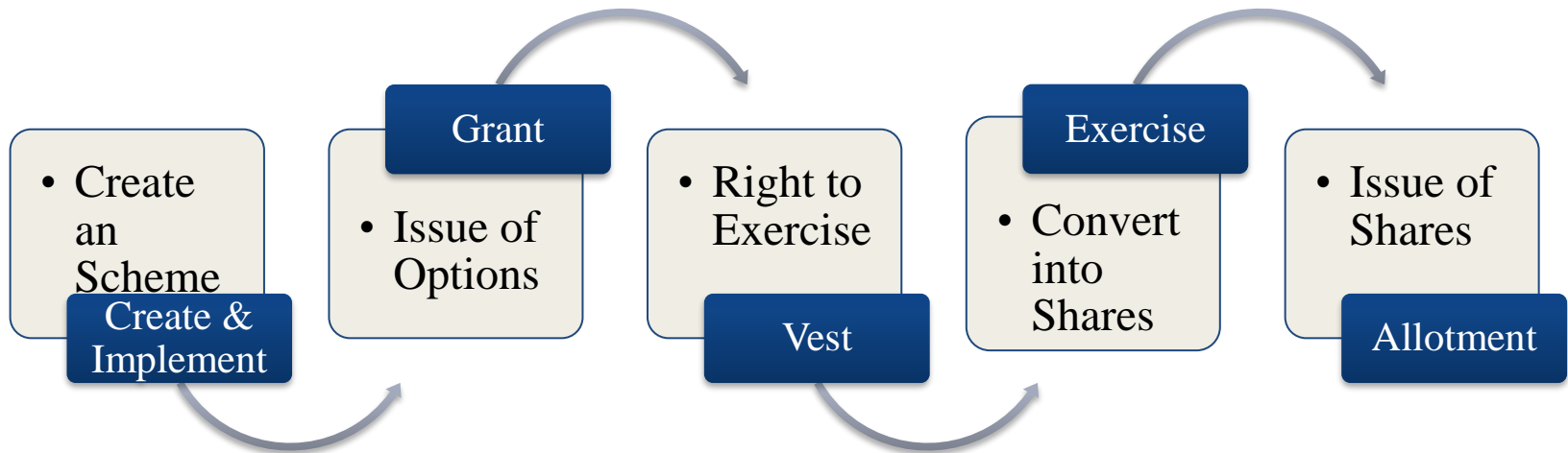
LEGAL FRAMEWORK ON ESOPs



● What are Employee Stock Benefit Schemes

Employee Stock Benefit Schemes give the employees an **ownership interest** by participating in the Stock /Shares of the Company.

Life cycle of ESOP



- Employee Stock Option Schemes are the most commonly used form for employee ownership in more than 70% organizations.

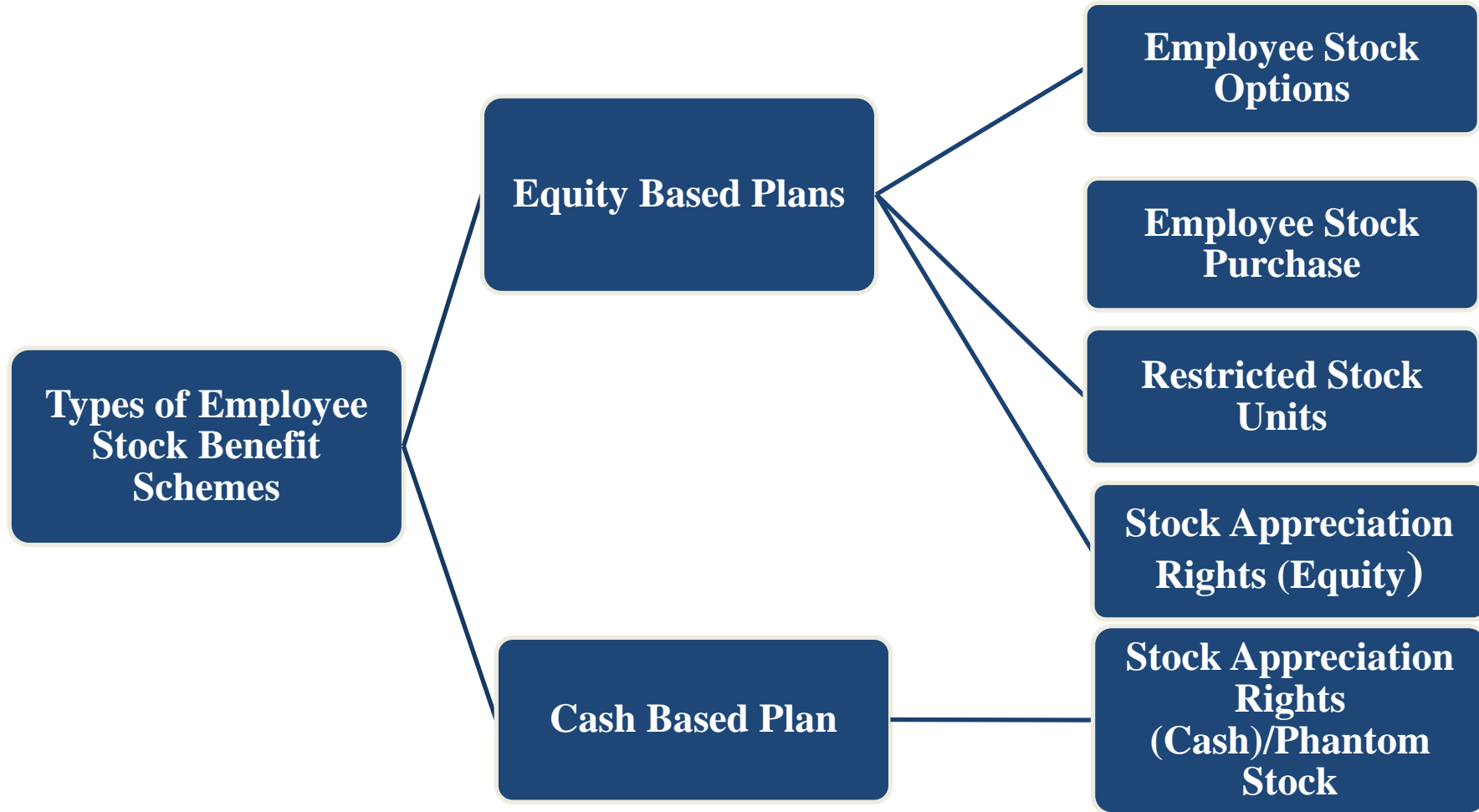


● Objective of Employee Stock Benefit Schemes

- To **motivate** the employees to contribute to the growth and profitability of the Company.
- To **retain** the key employees and reduce the attrition rate of the Company.
- To **achieve sustained growth** and the **creation of shareholder value** by aligning the interests of the employees with the long-term interests of the Company.
- To **create a sense of ownership and participation** amongst the employees to share the value they create for the Company in the years to come, and
- To provide **additional deferred rewards** to employees.
- Company gets dual benefit of **cash saving along with tax benefit.**
- ESOP is **cost effective tool** for retention & rewards.



● Types of Employee Stock Benefit Schemes



Employee Stock Option Plan (ESOP)

Employee Stock Option Plan is a type of Equity ownership plan, where in;

- ✓ Options are issued to employee
- ✓ Creating a right to subscribe shares of the Company
- ✓ At a pre determined price
- ✓ Over a fixed period of time
- ✓ Upon fulfilment of certain conditions



- It is one of the most traditional mode used **to incentivize** the employees.
- ESOP provides **flexibility** to decide the terms, exercise price, vesting period at the time of grant.



Employee Stock Purchase Plan(ESPS)

Employee Stock Purchase Plan is a type of Equity ownership plan, where in

- ✓ Shares are issued to employee
- ✓ Creating a right to subscribe shares of the Company
- ✓ At a discounted price
- ✓ Over a fixed period of time.



- In compared to ESOP, Employees get "**Shares**" of the company instead of options.
- It is a reward plan used **to appraise and incentivize** the employees.
- Under ESPS , the shares are allotted immediately so the benefit received is well ascertained.



Restricted Stock Unit Plan (RSU)

Restricted Stock Unit Plan is another type of Equity ownership plan, where in

- ✓ Units are issued to employee
- ✓ Creating a right to subscribe shares of the Company
- ✓ Over a fixed period of time
- ✓ Upon achieving certain conditions

- **Based on vesting ,types of RSU:**

- **Loyalty Based RSU**
- **Performance Based RSU**

- Generally, RSU can be issued at zero price, but in India it is read with context of ESOP.
- Unlike ESOP's, the exercise price of RSU's is near **the par value of shares.**



Stock Appreciation Rights Plan (SAR)

Stock Appreciation Plan is type of Equity ownership plan, where in

- ✓ Units are issued to employee
- ✓ Employee receives Appreciation Value
- ✓ Settlement of appreciation is made in either in Equity or in Cash



- “**Appreciation**” is difference between the Exercise Date price & Grant Date price of the Company.
- Based on settlement, SAR can be categorized as:
 - Settled in Equity: **Appreciation is converted into Equity shares** which are then allotted the employee.
 - Settled in Cash: **Appreciation is directly transferred to the bank** account of an employee.



Types of Employee Stock Benefit Schemes

Law Recognised Schemes

SEBI (Share based Employee Benefits and Sweat Equity) Regulations, 2021

ESOP

- Employee Stock Option Schemes

ESPS

- Employee stock Purchases Schemes

SAR

- Stock Appreciation Rights schemes

RSU

- Restricted Stock Units Schemes

GBES

- General Employee Benefits Schemes

RBS

- Retirement Benefit Schemes



Coverage of Employees

Law



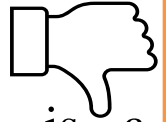
Who is an Employee?

Covered



- ✓ Employees designated by company.
- ✓ Directors of the Company.
- ✓ Employees of Subsidiary Company
- ✓ Employees of Holding Company
- ✓ Employees of Associate Company.
- ✓ Employees of Group Company.
- ✓ Foreign Employees.

Not covered



- Employees who is a promoter or belonging to promoter group.
- Director holding directly or indirectly more than 10 % of outstanding equity shares of the Company.
- Independent Directors.
- *Consultants, Like Doctors, Gig workers Contractual Employees

*Not yet covered under definition of Employee, but clarity on there coverage is still under discussion.

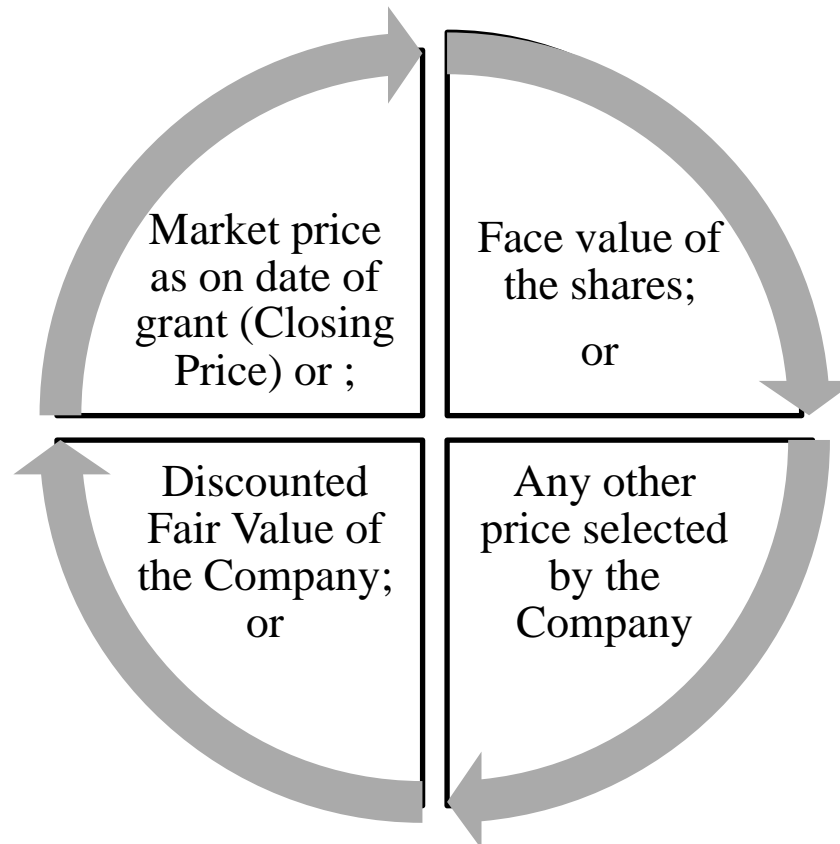


● Pricing Criteria for Exercise Price

Law

- ✓ Companies are free **to decide the Exercise price;**
- ✓ Issue at discount / premium;
- ✓ Price shall not go below the Par Value of Shares.

Pricing Formula

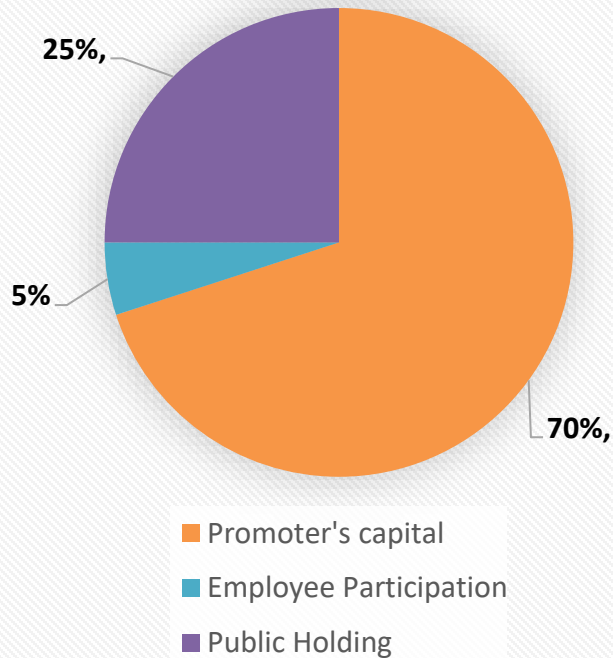


● Pool of the Scheme

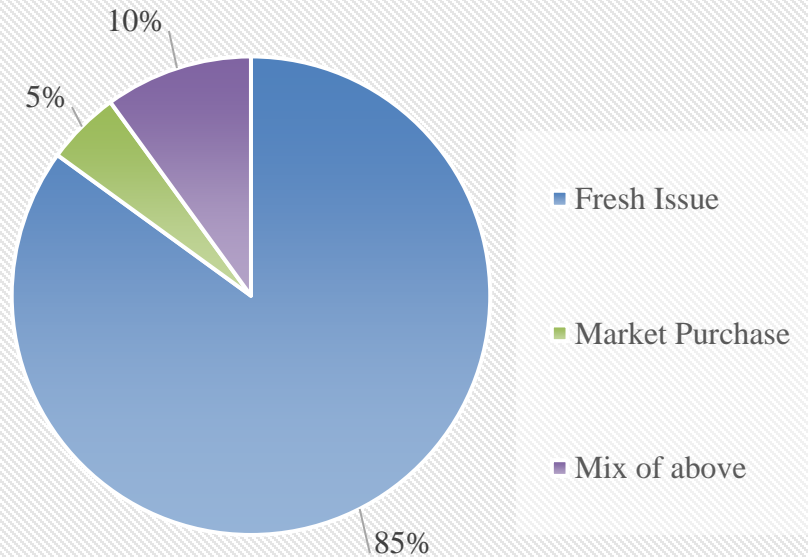
Law

- ✓ Companies are **free to decide** the number of shares to be reserved for ESOP Pool.

SHARE POOL

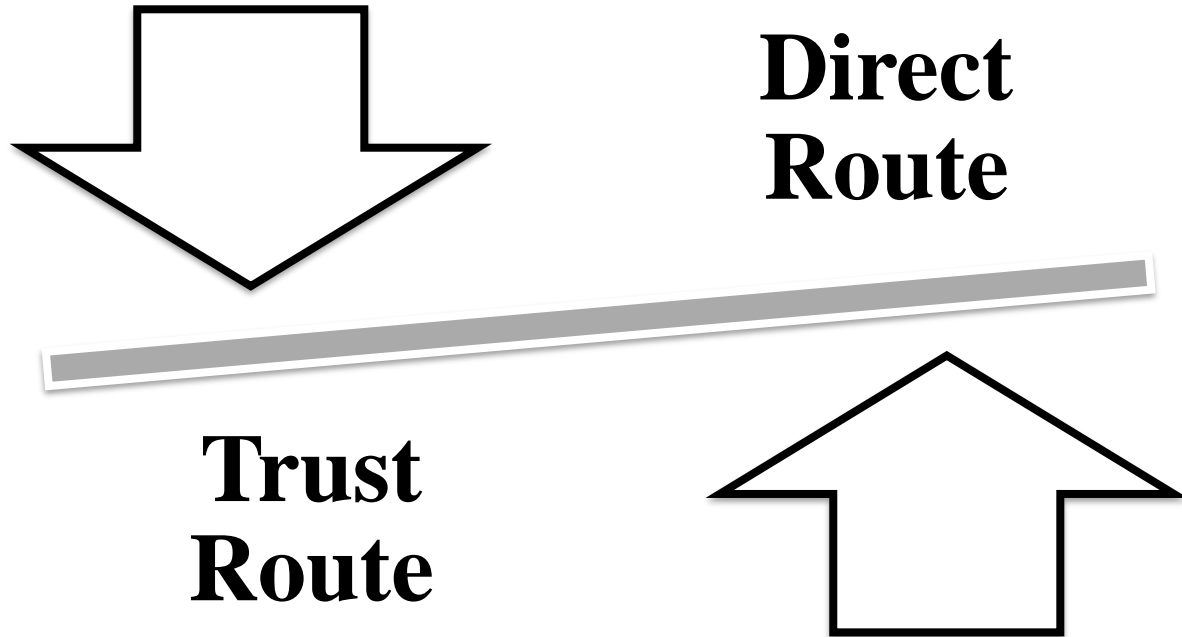


SOURCE OF POOL



● Route of the Scheme

Law

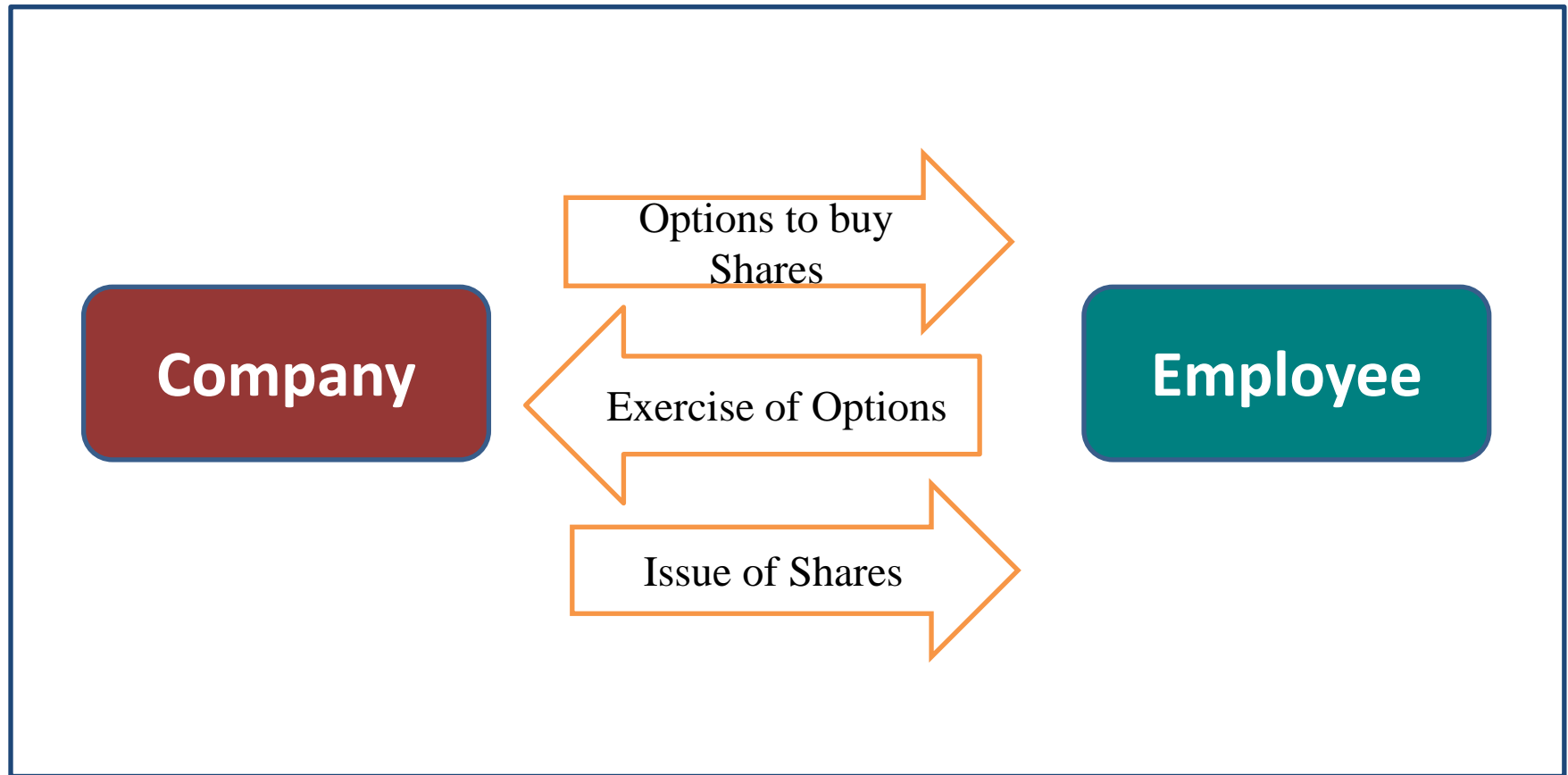


Companies can make changes in the route of the Scheme (i.e., Direct Route to Trust Route or Vice-Versa) subject to the Shareholders approval.



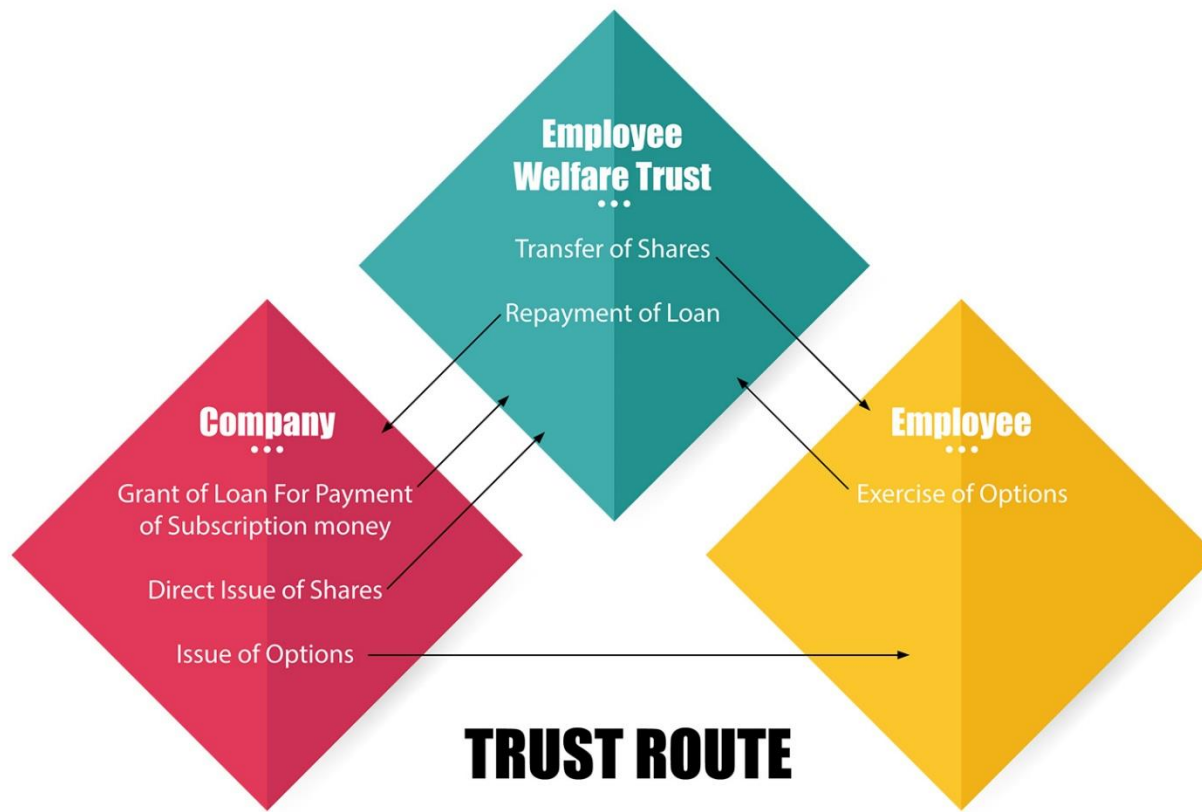
Direct Route

Law



Trust Route

Law



Acquisition of Shares by the Trust

Law

Trust can acquire shares by:

Secondary Market Acquisition

Fresh Subscription

From Stock Exchanges

Directly from the Company

Limit-
2 % of the paid-up equity capital in a F.Y.

Overall Limit-
Max. 5 % of the paid-up equity capital at any time.



Trust Route-Who can be a Trustee?

Law

✓ **Any person can be appointed as a trustee of the trust;**

Except



- Director, key managerial personnel or promoter of the company;
- Any relative of such director, key managerial personnel or promoter;
- Director of Holding Company;
- Director of Subsidiary company;
- Director of Associate Company;

or

- Beneficiary holding ten percent or more of the paid-up share capital or the voting rights of the company;



Trust Route-Who can be a Trustee?

Law

Minimum Number of Trustee?



Individual(s) or “one person company”

Minimum 2
Trustee required

Corporate Entity

Can be a Sole
Trustee



● Listed entities having worldwide presence

Law

✓ Granting ESOP's to Foreign Employees:

- **Yes**, the companies can grant ESOP also to its foreign employees in compliance to the various regulatory aspects.
- In context of FEMA regulations, the investment received from the foreign employee **is treated as FDI**;
- Any investment made by a foreign employee shall be **subject to the entry routes, sectoral caps , the investment limits, pricing guidelines**;



Listed entities having worldwide presence

Law

✓ Company may grant ESOP via **two entry routes;**

Automatic Route



“Automatic route” means the entry route through which investment by a person resident outside India **does not require the prior approval of Government.**

Approval Route



“Government route” means the entry route through which investment by a person resident outside India **requires prior Government approval***.

** If the grants are made to the citizens of land sharing border countries with India such as citizen **Bangladesh; or Pakistan; China and other countries.***



● ESOP to form a part of Managerial Remuneration

Law

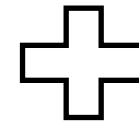
- MR provisions shall be subject to section 197, 198 of the Companies Act, 2013.



If a Director are given ESOP;s



Perquisite value arising in his hands(at the time of exercise)



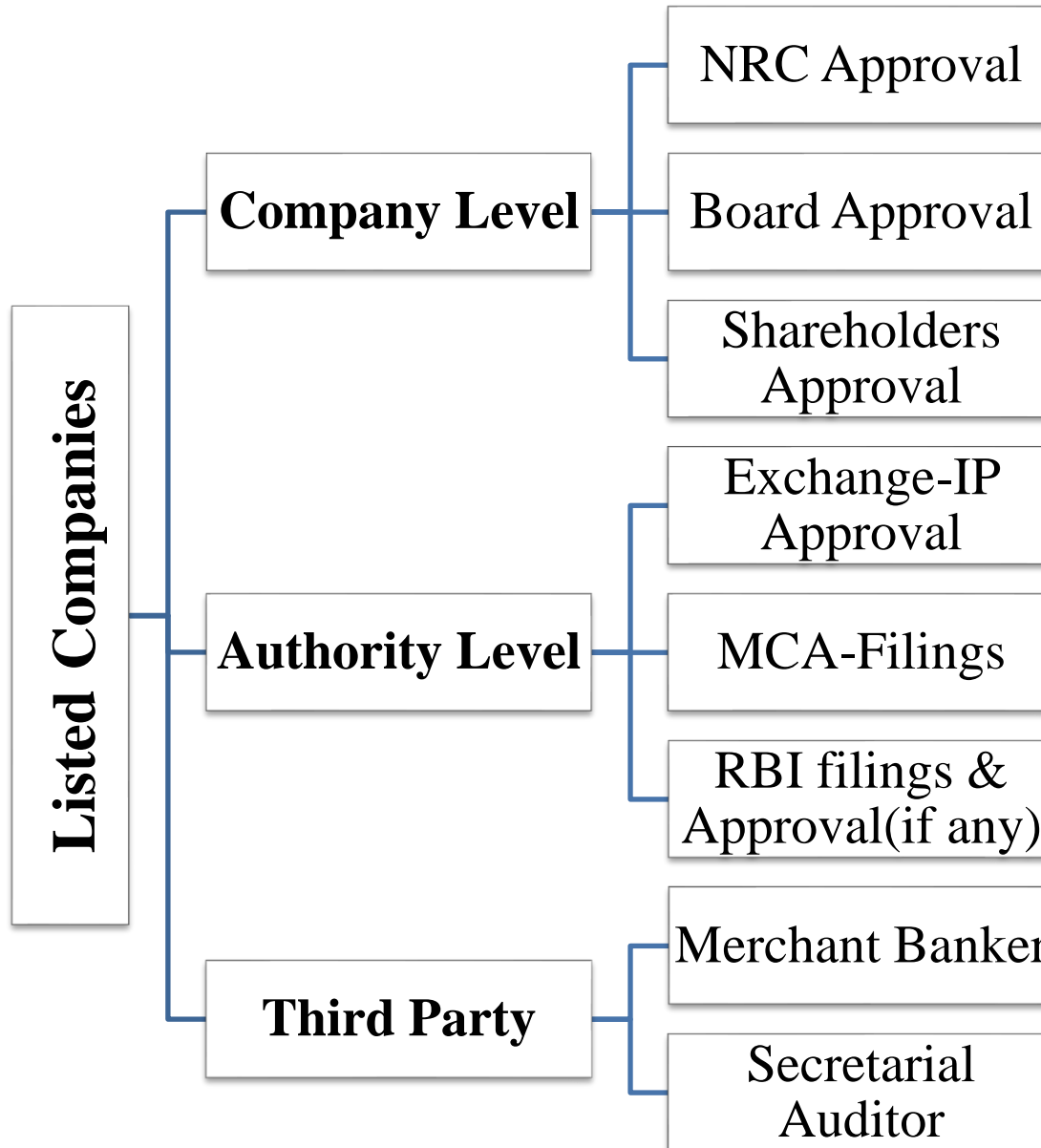
Shall form a part of the MR, in that financial year in which the perquisite arises.



Company shall take the necessary approvals, pursuant to the increase in the limits of remuneration.



Procedure for Issuance by Listed Company



● Companies going for listing (Pre-Post IPO)

Law

SEBI (Share based Employee Benefits and Sweat Equity) Regulations, 2021

Prior to IPO Grant



- IP approval required from stock exchanges, for the grants made in the schemes.
- Exercise & allotment allowed.

Post IPO Grants



- Ratification by Shareholders.
- Before making any fresh grants, IP approval required from stock exchanges,.



● Disclosure Requirements

Law

✓ Disclosures in the Board Report

- Material Changes in the scheme
- Relevant disclosures in terms of the accounting standards
- Diluted EPS on issue of shares
- Total number of options approved under ESOS
- Details of Vesting, Exercise price ,source of shares.
- Method used to value-Intrinsic or fair value
- Option movement during the year (For each ESOS) & other details.



● Disclosure Requirements

Law

✓ Other Requirements

Certificate from auditors

Board shall Place
Certificate from
Secretarial
Auditors

Each AGM

Accounting policies.

Disclosure as per
A/S

Guidance Note on
Accounting



● PIT Regulations on Exercise of options

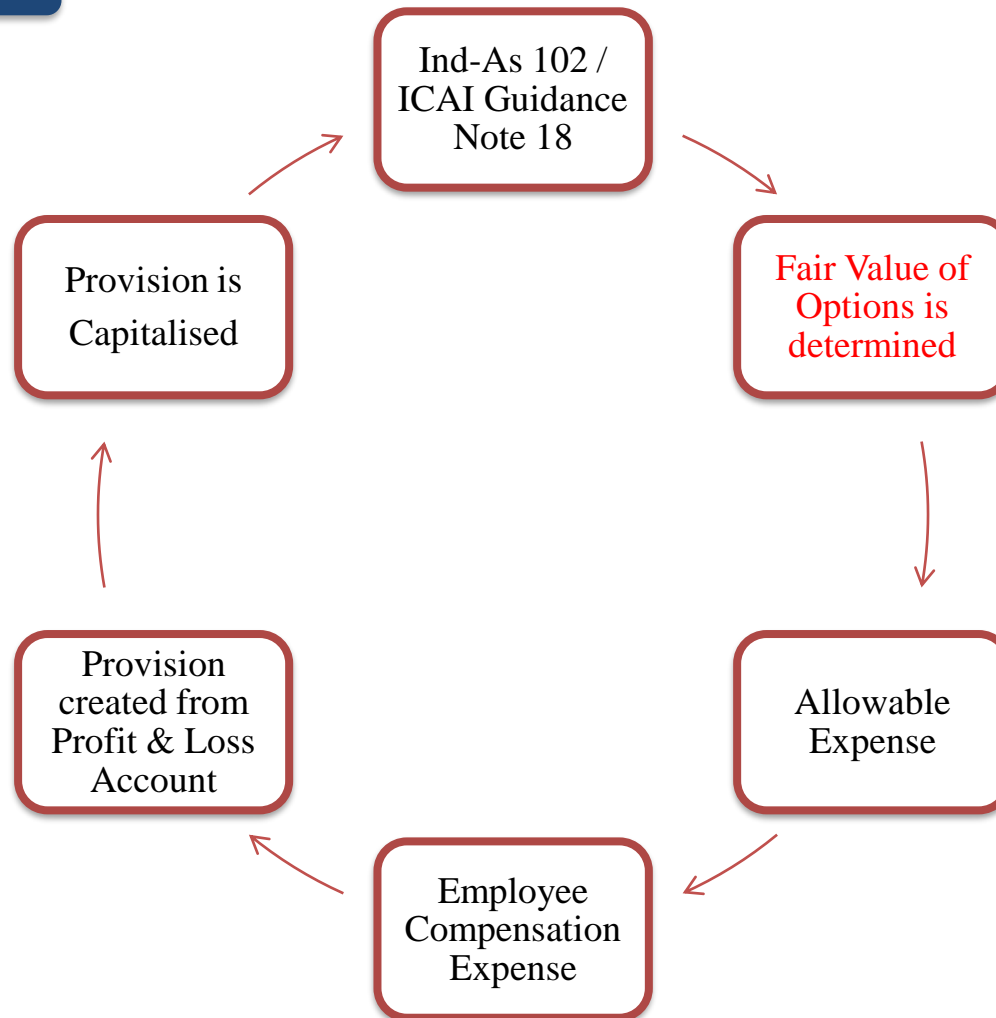
Law

- ✓ Exercise of options shall not be considered to be “trading.”
- ✓ Sale of shares acquired through exercising ESOP will be considered Open market trade.
- ✓ The Designated Persons **can only sell their ESOP** securities if they have not earlier acquired the Company securities **prior to six months** of such selling, **(except via exercising the ESOP shares)**,
- ✓ Sale of ESOP Shares cannot be done when the Trading window is closed.



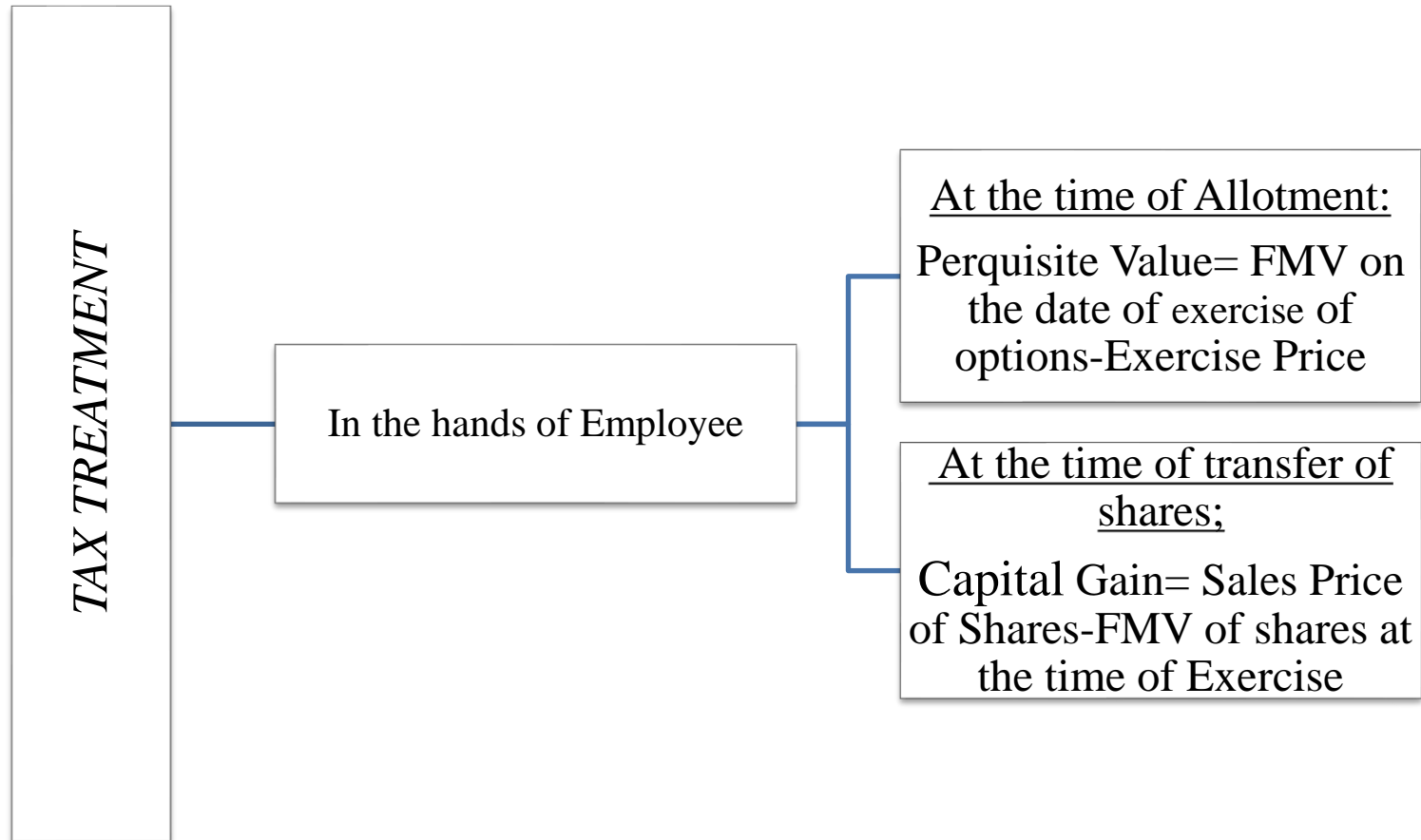
Accounting Treatment in Esop's

Law



● Tax Treatment in Esop's

Law



● ESOP Gain Analysis: E.g.

Description	Employee A
No. of Options granted	10,000
Date of grant	1-Apr-23
FMV (as on date of grant) (in Rs.) (per option) (A)	150
Exercise Price (in Rs.) (deeming no discount) (per option) (B)	150
Income Tax Bracket of Employee (in %)	30
Vesting Period (Single Vesting in 1 year)	1
Exercise period (year)	1



● ESOP Gain Analysis: E.g.

Description	Employee A
No. of Options Vested (100% vested)	10,000
No. of Options Exercised (D)	10,000
Date of Exercise (one year)	02-Apr-24
FMV (as on date of exercise) (in Rs.) (deeming 100% growth) (E)	200
Perquisite value per Option (FMV - exercise price i.e $200 - 150 = 50$) (in Rs.) (E-B) = (F)	50
Total Perquisite value (Notional Gain) $(10000 * 50)$ (D * F) = (G)	50,0000
Perquisite Tax per Option (in Rs.) (Assuming 30% slab rate) $(F * 30\%) = (H)$	15



● ESOP Gain Analysis: E.g.

Description	Employee A
Total Perquisite Tax $(15 * 10000) (H * D) = (I)$	15,0000
Date of Selling of Shares (1 years)	02-Apr-25
FMV (as on date of Sell off) (in Rs.) (J)	300
Cost of Acquisition of shares sold off [i.e. FMV as on date of Exercise (E)] (K)	200
Gain on selling of shares (In Rs.) per share (L)	100
Total Gain on Selling $(D * L(10000 * 100)) = (M)$	10,00,000



ESOP Gain Analysis: E.g.

Description	Employee A
LTCG Tax (Assuming Rate 10%) (In Rs.) per share (N)	10
Total Tax at the time of selling of shares ($D*N$) = $(10000*10)$ (O)	100,000
Total Amount payable by Employee to Company $(10000*150)$ (B*D) = (P)	1,50,0000
Total Tax Payable by Employee (Total Perquisite Tax+ Tax on Sale of shares)(I+O) = (Q)	25,0000

Actual Gain to Employee

Description	Employee A(in Rs.)
Amount receive after selling of Shares ($J*D$)	30,00,000
Less: Amount payable by Employee to Company (i.e. (P))	15,00,000
Less: Total Tax paid by the Employee (i.e.(Q))	3,00,000
Actual Gain	12,00,000



**THANK
YOU**

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