



SEBI (Share Based Employee Benefits and Sweat Equity) Regulation 2021

By:-

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CHAPTER

7

SEBI (SHARE BASED EMPLOYEE BENEFITS AND SWEAT EQUITY) REGULATIONS, 2021

Covering-

- Applicability
- Non Applicability
- Important Definitions
- Highlights of the regulations
- Requirements specified under the Regulations
- Schemes - Implementation and Process
- Variation of terms of the schemes
- Winding up of the Schemes
- Employee Stock Option Scheme
- Employee Stock Purchase Scheme (ESPS)
- Stock Appreciation Rights Scheme (SARS)
- General Employee Benefits Scheme
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- Sweat Equity Shares
- Chapter IV of SEBI Regulations, 2021

**EXPECTED
MARKS COVERAGE
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SEBI (SHARE BASED EMPLOYEE BENEFITS AND SWEAT EQUITY) REGULATIONS, 2021

APPLICABILITY

A. The provisions of these regulations shall apply to any **company whose shares are listed** on a **recognised stock exchange in India, and has a scheme:**

(i) for **direct or indirect benefit of employees**; and

(ii) involving **dealing in or subscribing to or purchasing securities** of the company, directly or indirectly; and

(iii) **satisfying, directly or indirectly, any one of the following conditions:**

(a) the scheme is **set up** by the company or any other company in its group;

(b) the scheme is **funded or guaranteed** by the company or any other company in its group;

(c) the scheme is **controlled or managed** by the company or any other company in its group.

B. The provisions of these regulations shall apply to following:-

(I) **EMPLOYEE STOCK OPTION SCHEMES;(ESOS)**

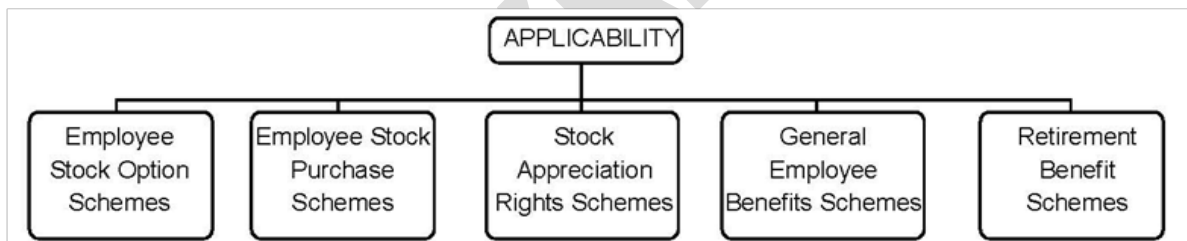
(II) **EMPLOYEE STOCK PURCHASE SCHEMES; (ESOP)**

(III) **STOCK APPRECIATION RIGHTS SCHEMES; (SAR)**

(IV) **GENERAL EMPLOYEE BENEFITS SCHEMES; (GEBS)**

(V) **RETIREMENT BENEFIT SCHEMES. ; (RBS)**

(VI) **SWEAT EQUITY SHARES (SES)**



NON APPLICABILITY

the provisions pertaining to **preferential allotment** as specified in the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 **shall not be applicable** *in case of a company issuing new shares* in pursuance and **compliance of these regulations** except wherever specifically provided for in these regulations.

IMPORTANT DEFINITIONS

ESOSs means a scheme under which a company **grants option to employee** directly or through a trust.

According to Section 2(37) of Companies Act 2013, **“employees’ stock option”** means the option given to the directors, officers or employees of a company or of its holding company or subsidiary company or companies, if any, which gives such directors, officers or employees, the benefit or right to purchase, or to subscribe for, the shares of the company at a future date at a pre-determined price.

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ESPSs means a scheme under which the **company offers shares to employee as part of a public issue** or through a trust.

“STOCK APPRECIATION RIGHT OR SAR” means a right given to a SAR grantee entitling him to receive appreciation for a specified number of shares of the company where the settlement of such appreciation may be made by way of cash payment or shares of the company.

“GENERAL EMPLOYEE BENEFITS SCHEME OR GEBS” means any scheme of a company framed in accordance with these regulations, dealing in shares of the company or the shares of its listed holding company, for the purpose of employee welfare including healthcare benefits, hospital care or benefits, or benefits in the event of sickness, accident, disability, death or scholarship funds, or such other benefit as specified by such company.

“RETIREMENT BENEFIT SCHEME OR RBS” means a scheme of a company framed in accordance with these regulations, dealing in shares of the company or the shares of its listed holding company, for providing retirement benefits to the employees subject to compliance with existing rules and regulations as applicable under laws relevant to retirement benefits in India.

“SWEAT EQUITY SHARES” means sweat equity shares as defined in sub-section (88) of section 2 of the Companies Act, 2013 (18 of 2013).

SECRETARIAL AUDITOR

“Secretarial auditor” means a **company secretary in practice** appointed by a company under **Rule 8** of the Companies (Meetings of Board and its Powers) Rules, 2014 to conduct secretarial audit pursuant to **Regulation 24A** of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015.

HIGHLIGHTS OF THE REGULATIONS

The highlights of the regulations are as follows:-

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| (a) Company can implement schemes either directly or by setting up an irrevocable trust(s) . |
| (b) No scheme shall be offered to employees of a company unless the shareholders of the company approve it by passing a special resolution in the general meeting. |
| (c) Companies having employee stock option programmes are allowed to buy their own company shares subject to certain conditions. |
| (d) Company shall constitute a compensation committee for administration and superintendence of the schemes. |
| (e) Secondary acquisition in a financial year by the trust shall not exceed two per cent of the paid up equity capital as at the end of the previous financial year. |
| (f) For undertaking secondary market acquisitions companies are required to take shareholders' approval through special resolution ; |
| (g) The trust shall be required to hold the shares acquired through secondary acquisition for a minimum period of six months . |
| (h) Option, SAR (stock appreciation rights schemes) or any other benefit granted to an employee under the regulations shall not be transferable to any person . |
| (i) The employee shall not have right to receive any dividend or to vote or in any manner enjoy the benefits of a shareholder in respect of option granted to him, till shares are issued upon exercise of option . |
| (j) The amount payable by the employee , if any, at the time of grant of option, may be forfeited by the company if the option is not exercised by the employee within the exercise period; <u>OR</u>
may be refunded to the employee if the options are not vested due to non-fulfillment of conditions relating to vesting of option as per the ESOS. |

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REQUIREMENTS SPECIFIED UNDER THE REGULATIONS

1. MINIMUM PROVISIONS IN A TRUST DEED

The SEBI requires certain provisions to be incorporated in the Trust Deed:-

1. Details of the Trust- its name, object, source of funds, its usage and details of scheme, settler, trustees;
2. Powers and Duties of trustee(s);
3. Provisions on dissolution of the Trust;
4. Provisions specifying that the trustee shall not act in any manner that would be detrimental to the interests of the beneficiaries;
5. Other clauses to safeguard the interests of the beneficiaries

2. COMPENSATION COMMITTEE

The compensation committee shall be a committee of **such members of the Board of Directors** of the company as provided under **regulation 19 of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015**, as amended from time to time.

Provided that a company **may also opt to designate its nomination and remuneration committee** as the compensation committee for the purposes of these regulations.

As per the regulation, the **committee is required to formulate detailed terms and conditions regarding:-**

(a) Quantum of the benefit
(b) Kind of benefits;
(c) Conditions to avail the benefits;
(d) Period within which the employee shall exercise the option;
(e) Exercise period of the option in the event of termination or resignation of an employee;
(f) Right of an employee to exercise all options at one time or at various points of time;

The compensation committee **shall frame suitable policies and procedures** to ensure that **there is no violation of securities laws** including the SEBI (Prohibition of Insider Trading) Regulations, 2015 and the SEBI (Prohibition of Fraudulent and Unfair Trade Practices Relating to the Securities Market) Regulations, 2003, as amended from time to time, by the trust, the company and its employees, as may be applicable.

3. SHAREHOLDERS' APPROVAL

As per the provisions of regulations, no scheme shall be offered to the employees of a company unless the shareholders of the company approve it by passing a **special resolution**. The **explanatory statement** to the notice shall include the information as **specified by SEBI** in this regard.

Approval of shareholders by way of separate resolution in the general meeting shall be obtained by the **company in case of:**

(a) Secondary acquisition for implementation of the schemes. Such approval shall mention the percentage of secondary acquisition (subject to limits specified under these regulations) that could be undertaken;
(b) Secondary acquisition by the trust in case the share capital expands due to capital expansion undertaken by the company including preferential allotment of shares or qualified institutions placement, to maintain the five percent cap as prescribed in these regulations of such increased capital of the company;
(c) Grant of option, SAR, shares or other benefits, as the case may be, to employees of subsidiary or holding company;
(d) Grant of option, SAR, shares or benefits, as the case may be, to identified employees, during any one year, equal to or exceeding one per cent. of the issued capital (excluding outstanding warrants and conversions) of the company at the time of grant of option, SAR, shares or incentive, as the case may be.

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4. LISTING REQUIREMENT

In case new issue of shares is made under the scheme, **it has to be listed immediately** on the stock exchange. A statement has to be filed by the company and **obtain an in-principle approval** from the stock exchange. Such statement shall include the description of the schemes in detail.

The company shall **also notify the concerned stock exchange** as and when **an exercise of option/SAR** is made.

5. DISCLOSURES BY BOARD OF DIRECTORS

The Board of Directors in their report shall disclose any material change in the scheme(s) and whether the scheme(s) is/are in compliance with the regulations.

The following details shall be disclosed on the **company's website** and a **web-link** thereto shall be provided in the report of board of directors:

(a) Relevant disclosures relating to the accounting standards;
(b) Diluted EPS on issue of shares pursuant to all the schemes;
(c) Details related to ESOS;
(d) Details related to ESPS;
(e) Details related to SAR;
(f) Details related to General Employee Benefit Scheme/Retirement Benefit Scheme (GEBS/ RBS);
(g) Details related to Trust;

6. MANDATORY DISCLOSURES

No ESOS/SAR shall be offered unless the disclosures, as specified by the SEBI in this regard, are made by the company to the prospective option/SAR grantees. The disclosure documents specified are:

(a) Statement of Risks;
(b) Information about the company;
(c) Salient features of the scheme.

7. SECRETARIAL AUDITOR

The secretarial auditor of the company shall certify compliance of the provisions of this regulations.

SCHEMES - IMPLEMENTATION AND PROCESS

A company may implement schemes either :-

(a) directly or
(b) by setting up an irrevocable trust(s).

Direct Route for ESOP's

(a) Company forms an Compensation committee and define the eligibility of ESOPs
(b) Issue fresh shares for ESOPs.
(c) After vesting period employees can exercise the option.
(d) On exercise of an option Company issue the shares to the employees.

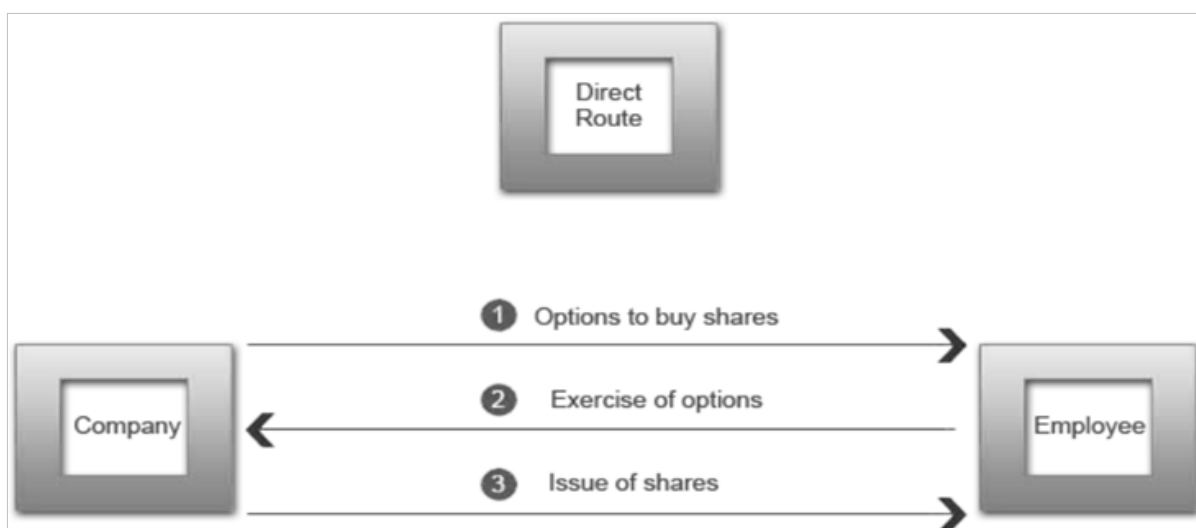
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Trust Route for ESOP's

(a) Company forms an Employee Welfare Trust .
(b) Company grants Loan to the trust for subscribing shares .
(c) Company issue fresh shares to the Trust and options to the Employees .
(d) Employees exercises the option .
(e) Trust Transfers the Shares to the employee upon receipt of exercise price.
(f) Trust repays the loan to the Company .

IMPLEMENTATION OF SCHEMES THROUGH TRUST

1. If a company has implemented the scheme through a trust and the same **has to be decided upfront at the time of taking approval of the shareholders** for setting up the schemes.

However, if the scheme involves **secondary acquisition or gift or both, then it is mandatory** for the company to implement such scheme(s) through a **trust(s)**.

2. A company may implement **several schemes** as permitted under these regulations **through a single trust**.

However, such single trust shall keep and maintain-

(a) proper books of account,
(b) records and documents,

for each such scheme so as to explain its transactions and to disclose at any point of time the financial position of each scheme and in particular give a true and fair view of the state of affairs of each scheme.

3. A person **shall not be appointed as a trustee, if he-**

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| (i) is a director, key managerial personnel or promoter of the company or its holding, subsidiary or associate company or any relative of such director, key managerial personnel or promoter; or |
| (ii) beneficially holds ten percent or more of the paid-up share capital of the company; |

However, **where individuals or 'one person companies'** as defined under the Companies Act, 2013 are appointed as trustees, there shall be a minimum of **two such trustees**, and in case a **corporate entity is appointed as a trustee, then it may be the sole trustee**.

4. The **trustees of a trust**, which is governed under these regulations, **shall not vote in respect of the shares** held by such trust, so as to avoid any misuse arising out of exercising such voting rights.

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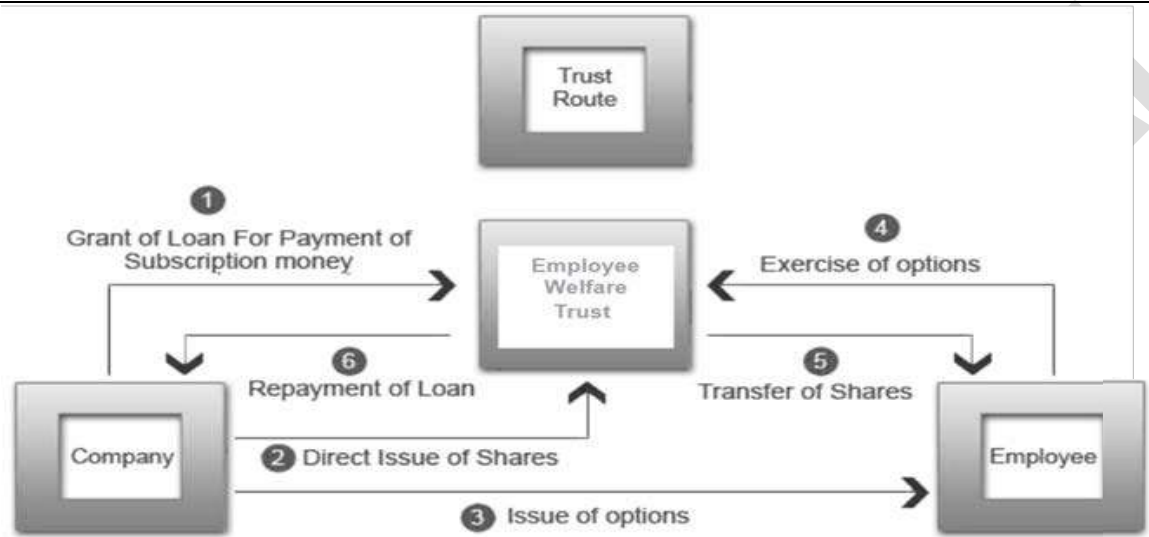
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5. **The trustee** should ensure that **appropriate approval from the shareholders has been obtained** by the company in order to enable the trust to implement the scheme(s) and **undertake secondary acquisition for the purposes of the scheme(s)**.
6. The company **may lend monies to the trust** on appropriate terms and conditions to acquire the shares either **through new issue or secondary acquisition**, for the purposes of implementation of the scheme(s).
7. For the purposes of disclosures to the stock exchange, the shareholding of the trust shall be shown as **'non-promoter and non-public' shareholding**.
8. Secondary acquisition in a financial year by the trust shall not exceed two percent of the paid up equity capital as at the end of the previous financial year.



VARIATION OF TERMS OF THE SCHEMES

The Company **shall not vary the terms** of the schemes unless **special resolution** is to be passed in the General Meeting provided that **such variation is not prejudicial to the interests** of the

Notice for passing special resolution for variation of terms of the schemes **shall disclose full details** of the variation, the rationale therefore, and the details of the employees who are beneficiaries of such variation;

Variation may be **includes reprice the options, SAR or shares**, as the case may be which are not exercised, whether or not they have been vested if the **schemes were rendered unattractive due to fall in the price of the shares in the stock market**; and

The company shall ensures that **such repricing shall not be detrimental to the interest of the employees** and approval of the shareholders in general meeting has been obtained for such repricing.

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WINDING UP OF THE SCHEMES

In case of winding up of the schemes being implemented by a company through trust, *the excess monies or shares remaining with the trust after meeting all the obligations*, if any, shall be utilised for repayment of loan or by way of distribution to employees as recommended by the compensation committee.

1. EMPLOYEE STOCK OPTION SCHEME

Procedure for issuing ESOP by a Listed Company

(a) Hold a Board Meeting to consider and approve ESOP and formation of Compensation Committee ;
(b) Compensation committee shall plan draft the scheme of ESOP;
(c) Hold Board meeting to adopt the final scheme , appoint the Merchant banker and approve the notice of the General meeting for shareholders approval ;
(d) Hold General Meeting for approval of shareholders ;
(e) Make an application to the stock exchange for obtaining in-principal approval of the stock exchange;
(f) Issue of letter of grant of option to the eligible employees along with the letter of acceptance of option;
(g) On receipt of letter of acceptance of option along with upfront payment (if any) , from the employee, issue the option certificates ;
(h) After expiry of vesting period, not less than one year the options shall vest in the employee . At that time, the Company shall issue a letter of vesting along with the letter of exercise of options;
(i) Receipt of letter of exercise from the employee;
(j) Hold a Board Meeting at the suitable Interval during the exercise period for allotment of shares on options exercised by the options ;
(k) Dispatch of letter of allotment along with the share certificates or credit the shares so allotted with the Depositories;
(l) Make an application to the Stock exchange for listing of the Shares so allotted ; and
(m) Receipt of Listing of the shares from the Stock exchange.

2. EMPLOYEE STOCK PURCHASE SCHEME (ESPS)

Pricing and Lock-In

The company may determine the price of shares to be issued under an ESPS, provided they conform to the provisions of **accounting policies** under these regulation. Shares issued under an **ESPS shall be locked-in for a minimum period of one year from the date of allotment**.

However, in case where shares are allotted by a company under an ESPS in lieu of shares acquired by the same person under an ESPS in another company **which has merged or amalgamated with the first mentioned company**, the **lock-in period already undergone** in respect of shares of the transferor company shall be **adjusted against** the lock-in period.

If ESPS is **part of a public issue** and the **shares are issued to employees at the same price** as in the public issue, the shares issued to employees pursuant to **ESPS shall not be subject to lock-in**.

3. STOCK APPRECIATION RIGHTS SCHEME (SARS)

“*Stock Appreciation Right*” means a **right given to a SAR grantee entitling him to receive appreciation for a specified number of shares** of the company where the settlement of such appreciation may be made by way of **cash payment or shares** of the company.

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Explanation – An SAR settled by way of shares of the company shall be referred to as **equity settled SAR**. “**Stock Appreciation Right Scheme**” means a scheme under which a company grants SAR to employees.

Administration and Implementation

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| (a) The SAR scheme shall contain the details of the manner in which the scheme will be implemented and operated; |
| (b) A company shall have the freedom to implement cash settled or equity settled SAR scheme ; |
| (c) No SAR shall be offered unless the disclosures, as specified by Board in this regard, are made by the company to the prospective SAR grantees . |

Vesting

There shall be a minimum vesting period of **one year** in case of SAR scheme.

Rights of the SAR holder

The employee **shall not have right to receive dividend or to vote** or in any manner enjoy the benefits of a shareholder in respect of SAR granted to him.

4. GENERAL EMPLOYEE BENEFITS SCHEME

“**General Employee Benefits Scheme**” means any scheme of a company framed in accordance with these regulations, **dealing in shares of the company or the shares of its listed holding company, for the purpose of employee welfare** including healthcare benefits, hospital care or benefits, or benefits in the event of sickness, accident, disability, death or scholarship funds, or such other benefit as specified by such company.

Administration and Implementation

GEBS shall contain the **details of the scheme and the manner in which the scheme shall be implemented** and operated.

At no point in time, **the shares of the company or shares of its listed holding company shall exceed ten percent of the book value or market value or fair value of the total assets of the scheme, whichever is lower**, as appearing in its latest balance sheet for the purposes of GEBS.

The secretarial auditor of the company shall certify compliance of the above.

5. RETIREMENT BENEFIT SCHEME

“**Retirement Benefit Scheme**” means a scheme of a company, framed in accordance with these regulations, **dealing in shares of the company or the shares of its listed holding company, for providing retirement benefits** to the employees subject to compliance with existing rules and regulations as applicable under laws relevant to retirement benefits in India.

Administration and Implementation

Retirement benefit scheme may be implemented by a company provided it is in compliance with these regulations, and provisions of any other law in force in relation to retirement benefits. The retirement benefit scheme **shall contain the details of the benefits** under the scheme and the manner in which the scheme shall be implemented and operated.

At no point in time, **the shares of the company or shares of its listed holding company shall exceed ten per cent of the book value or market value or fair value of the total assets of the scheme, whichever is lower**, as appearing in its latest balance sheet for the purposes of RBS.

The secretarial auditor of the company shall certify compliance of the above.

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6. SWEAT EQUITY SHARES

SWEAT EQUITY SHARES – DEFINITION

According to section 2(88), sweat equity shares mean *equity shares issued by a company to its directors or employees at a discount or for consideration, other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.*

Chapter IV of SEBI (SHARE BASED EMPLOYEE BENEFITS AND SWEAT EQUITY) REGULATIONS, 2021

APPLICABILITY

Nothing contained in this chapter shall apply to an **unlisted company**:

Provided that an **unlisted company coming out with initial public offer and seeking listing** of its securities on the recognized stock exchange, pursuant to issue of sweat equity shares, **shall comply with the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirement) Regulations, 2018.**

EMPLOYEE

The term 'employee' means,

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| (i) an employee of the company working in India or abroad ; or |
| (ii) a director of the company whether a whole time director or not. |

ISSUE OF SWEAT EQUITY SHARES TO EMPLOYEES

A company whose equity shares are listed on a recognised stock exchange may issue sweat equity shares in accordance with **section 54 of the Companies Act, 2013 and these regulations** to its employees for their providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.

MAXIMUM QUANTUM OF SWEAT EQUITY SHARES

A company shall not issue sweat equity shares for more than fifteen percent of the existing paid up equity share capital in a year. However, the issuance of sweat equity shares in the company shall not exceed twenty five percent of the paid up equity share capital of the company at any time.
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Further, a company listed on Innovators Growth Platform shall be permitted to issue not more than fifteen percent of the paid up equity share capital in a financial year subject to overall limit not exceeding fifty percent of the paid up equity share capital of the company, up to ten years from the date of its incorporation or registration.

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SPECIAL RESOLUTION

- (1) For the purposes of passing a special resolution under clause (a) of sub-section (1) of section 54 of the Companies Act, 2013), the **explanatory statement to be annexed to the notice** for the general meeting pursuant to section 102 of the Companies Act, 2013 **shall contain disclosures as specified in the Schedule – II of these regulations.**
- (2) The issue of sweat equity shares to employees **who belong to promoter or promoter group** shall be approved by way of a **resolution passed by a simple majority** of the shareholders in general meeting. However, for passing such a resolution, **voting through postal ballot and/or e-voting** as specified under Companies (Management and Administration) Rules, 2014 **shall also be adopted.** Further, provided that the *promoters/promoter group shall not participate in such resolution.*
- (3) Each issue of sweat equity shares shall be voted by a **separate resolution.**
- (4) The resolution for issue of sweat equity shares shall be valid for a period of **not more than twelve months from the date of passing of the resolution.**

PRICING OF SWEAT EQUITY SHARES

The price of sweat equity shares shall be determined in accordance with the **pricing requirements stipulated for a preferential issue** to a person other than a qualified institutional buyer under the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018.

VALUATION

- (1) The valuation of the **know-how or intellectual property rights or value addition** shall be carried out by a **merchant banker.**
- (2) The merchant banker may consult **such experts and valuers**, as it may deem fit, having regard to the nature of the industry and the nature of the valuation of know-how or intellectual property rights or value addition.
- (3) The merchant banker **shall obtain a certificate from an independent chartered accountant** certifying that the valuation of the know-how or intellectual property rights or value addition is in accordance with the relevant **accounting standards.**

ACCOUNTING TREATMENT

Where the sweat equity shares are issued for a **non-cash consideration**, such non-cash consideration shall be **treated in the following manner** in the books of account of the company:-

- (a) where the non-cash consideration takes the form of a **depreciable or amortizable asset**, it shall be carried to the **balance sheet** of the company in accordance with the relevant accounting standards; or
- (b) where **clause (a) is not applicable**, it shall be **expensed** as provided in the relevant accounting standards.

PLACING OF AUDITOR'S CERTIFICATE BEFORE ANNUAL GENERAL MEETING

In the general meeting subsequent to the issue of sweat equity shares, the Board of Directors shall place before the shareholders, a certificate from the **secretarial auditor** of the company **that the**

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issue of sweat equity shares has been made in accordance with these regulations and

in accordance with the resolution passed by the company authorizing the issue of such sweat equity shares.

CEILING ON MANAGERIAL REMUNERATION

The amount of sweat equity shares issued **shall be treated as part of managerial remuneration** for the purpose of sections 196, 197 and other applicable provisions of the Companies Act, 2013, **if the following conditions are fulfilled:**

(a) the sweat equity shares are issued to any **director or manager**; and

(ii) the sweat equity shares are issued for non-cash consideration, **which does not take the form of an asset** which can be carried to the balance sheet of the company in accordance with the relevant accounting standards.

LOCK-IN OF SWEAT EQUITY SHARES

(1) The sweat equity shares shall be locked in for such period of time as specified in relation to a **preferential issue** under the **Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018**, as amended from time to time.

(2) The provisions of the Securities and Exchange Board of India (Issue of Capital and Disclosures Requirements) Regulations, 2018 in respect of public issue in terms of **lock-in** and **computation of promoters' contribution** shall apply if a company makes a public issue after it has issued sweat equity shares.

LISTING

The sweat equity shares issued by a listed company **shall be eligible for listing** subject to their issuance being in accordance with these regulations.

APPLICABILITY OF THE SEBI (SUBSTANTIAL ACQUISITION OF SHARES AND TAKEOVERS) REGULATIONS, 2011.

Any acquisition of sweat equity shares **shall be subject to** the provisions of the Securities and Exchange Board of India (substantial acquisition of shares and takeovers) Regulations, 2011.

GENERAL OBLIGATIONS

The company shall ensure that –

(a) the **explanatory statement** to the notice for general meeting contains the disclosures specified under clause (b) of sub-section (1) of section 54 of the Companies Act, 2013 and sub-regulation (1) of regulation 32 of these regulations.

(b) the **secretarial auditor's certificate** required under regulation 36 is placed in the general meeting of the shareholders.

(c) the company, within **seven days** of the issue of sweat equity shares, sends a **statement to the recognised stock exchange, disclosing:**

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(i) number of sweat equity shares issued;
(ii) szz price at which the sweat equity shares are issued;
(iii) total amount received towards sweat equity shares;
(iv) details of the persons to whom sweat equity shares have been issued; and
(v) the consequent changes in the capital structure and the shareholding pattern <i>before and after</i> the issue of sweat equity shares.

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Answers to be analysed in Classroom

Q. 1.

Answer to Question No. 1:-

Lined area for writing the answer to Question No. 1.

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