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SECURITIES AND EXCHANGE BOARD OF INDIA

NOTIFICATION

the 24 September, 2002

SECURITIES AND EXCHANGE BOARD OF INDIA (ISSUE OF SWEAT EQUITY) REGULATONS, 2002

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S.O. No.1031 (E) In exercise of the powers conferred by Section 30 of the Securities and Exchange Board of India, 1992 read with Clause (d) of sub sections (1) of Section 79A as inserted by the Companies (Amendment) Act, 1998 (1 of 1999), the Board, hereby makes the following regulations, namely:-

CHAPTER – I

PRELIMINARY

Short title and commencement.

1 (a) These regulations shall be called the Securities and Exchange Board of India (Issue of Sweat Equity) Regulations, 2002.

(b) These regulations shall come into force on the date of their publication in the Official Gazette.

Definitions.

2. (1) In these regulations, unless the context otherwise requires: -

(a) 'Act' means the Securities and Exchange Board of India Act, 1992;

(b) 'associate' includes a person,

(i) who directly or indirectly by himself or in combination with relatives, exercise control over the company; or,

(ii) whose employee, officer or director is also a director, officer or employee of the company;

(c) 'Board' means the Board as defined in clause (a) of sub section (1) of section 2 of the Act;

(d) 'control' shall include the right to appoint majority of the directors or to control the management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders or voting agreements or in any other manner;

(e) 'company' means a company as defined in Companies Act, 1956;

(f) 'director' means, a director as defined in sub-section (13) of section 2 of the Companies Act, 1956;

(g) 'employee' means,

(i) a permanent employee of the company working in India or abroad; or

(ii) a director of the company whether a whole time director or not;

(h) 'ESOS' means an Employee Stock Option Scheme as defined in Securities and Exchange Board of India (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999;

(i) 'insider' means an insider as defined in clause (e) of regulation 2 of Securities and Exchange Board of India (Insider Trading) Regulations, 1992;

(j) 'merchant banker' means a merchant banker registered under Section 12 of the Act;

(k) 'promoter' means promoter as defined in clause (h) of sub regulation (1) of regulation 2 of the Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997;

(l) 'registrar' means a registrar to an issue and includes a share transfer agent registered under Section 12 of the Act;

(m) 'securities' means securities as defined in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956);

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(n) 'statutory auditor' means an auditor appointed by a company under Section 224 of the Companies Act 1956 (1 of 1956);

(o) 'Recognised Stock Exchange' means a stock exchange which has been granted recognition under Section 4 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956);

(p) 'sweat equity shares' means sweat equity shares as defined in Explanation II of sub section (1) of Section 79A of the Companies Act, 1956;

(q) 'Schedule' means a schedule to these regulations.

(r) 'valuer' means a Chartered Accountant or a merchant banker appointed to determine the value of the intellectual property rights or other value addition.

(2) Words and expressions not defined in these regulations shall have the same meaning as have been assigned to them under the Act or the Securities Contracts (Regulation) Act, 1956 or the Companies Act, 1956 or any statutory modification or re-enactment thereof, as the case may be.

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Applicability.

3. Nothing contained in these regulations shall apply to an unlisted company;

Provided the unlisted company coming out with initial public offering and seeking listing of its securities on the stock exchange, pursuant to issue of sweat equity shares, shall comply with the Securities and Exchange Board of India (Disclosure and Investor Protection) Guidelines, 2000.

CHAPTER II

ISSUE OF SWEAT EQUITY BY A LISTED COMPANY

Sweat equity shares may be issued to employee, promoter.

4. A company whose equity shares are listed on a recognized stock exchange may issue sweat equity shares in accordance with Section 79A of Companies Act, 1956 and these Regulations to its –

(a) Employees

(b) Directors

Special Resolution.

5. (1) For the purposes of passing a special resolution under clause (a) of sub section (1) of Section 79A of the Companies Act, 1956 the explanatory statement to be annexed to the notice for the general meeting pursuant to section 173 of the Companies Act, 1956 shall contain disclosures as specified in the Schedule.

(2) The issue of sweat equity shares to promoters shall be subject to the requirements specified in Regulation 6 of these Regulations.

Issue of Sweat Equity Shares to Promoters.

6. (1) In case of Issue of sweat equity shares to promoters, the same shall also be approved by simple majority of the shareholders in General Meeting;

Provided that for passing such resolution, voting through postal ballot as specified under Companies (Passing of the resolution by Postal Ballot) Rules, 2001 shall also be adopted;

Provided further that the promoters to whom such Sweat Equity Shares are proposed to be issued shall not participate in such resolution.

(2) Each transaction of issue of Sweat Equity shall be voted by a separate resolution.

(3) The resolution for issue of Sweat Equity shall be valid for a period of not more than twelve months from the date of passing of the resolution.

(3) For the purposes of passing the resolution, the explanatory statement shall contain the disclosures as specified in the Schedule.

Pricing of Sweat Equity Shares.

7. (1) The price of sweat equity shares shall not be less than the higher of the following:

(a) the average of the weekly high and low of the closing prices of the related equity shares during last six months preceding the relevant date; or

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(b) the average of the weekly high and low of the closing prices of the related equity shares during the two weeks preceding the relevant date.

Explanation: "Relevant date" for this purpose means the date which is thirty days prior to the date on which the meeting of the General Body of the shareholders is convened, in terms of clause (a) of sub section (1) of section 79A of the Companies Act.

(2) If the shares are listed on more than one stock exchange, but quoted only on one stock exchange on given date, then the price on the stock exchange shall be considered.

(3) If the share price is quoted on more than one stock exchange, then the stock exchange where there is highest trading volume during that date shall be considered.

(4) If the shares are not quoted on the given date, then the share price on the next trading day shall be considered.

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Valuation of intellectual Property.

8. (1) The valuation of the intellectual property rights or of the know how provided or other value addition mentioned in Explanation II of sub section (1) of Section 79A of the Companies Act, 1956 shall be carried out by a merchant banker.

(2) The merchant banker may consult such experts and valuers, as he may deem fit having regard to the nature of the industry and the nature of the property or other value addition.

(3) The merchant banker shall obtain a certificate from an independent Chartered Accountant that the valuation of the intellectual property or other value addition is in accordance with the relevant accounting standards.

Accounting Treatment.

9. (1) 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 Auditors Before Annual General Meeting.

10. In the General meeting subsequent to the issue of sweat equity, the Board of Directors shall place before the shareholders, a certificate from the auditors of the company that the issue of sweat equity shares has been made in accordance with the Regulations and in accordance with the resolution passed by the company authorizing the issue of such Sweat Equity Shares.

Ceiling on Managerial Remuneration.

11. The amount of Sweat Equity shares issued shall be treated as part of managerial remuneration for the purpose of sections 198, 309, 310, 311 and 387 of the Companies Act, 1956, if the following conditions are fulfilled:

(i) the Sweat Equity shares are issued to any director or manager; and

(ii) they 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.

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Lock-in of sweat equity shares.

12. (1) The Sweat Equity shares shall be locked in for a period of three years from the date of allotment.

(2) The Securities and Exchange Board of India (Disclosures and Investor Protection) Guidelines, 2000 on 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 after it has issued sweat equity.

Listing.

13. The Sweat Equity issued by a listed company shall be eligible for listing only if such issues are in accordance with these regulations.

Applicability of Takeover.

14. Any acquisition of Sweat Equity Shares shall be subject to the provision of Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 1997.

CHAPTER III

GENERAL OBLIGATIONS

Obligations of the Company

15. (1) The company shall ensure that -

(a) The explanatory statement to the notice for general meeting shall contain disclosures as are specified under clause (b) of sub section (1) of Section 79A and sub regulation (1) of Regulation 5.

(b) The Auditor's certificate as required under Regulation 10 shall be placed in the general meeting of shareholders.

(c) The company shall within seven days of the issue of sweat equity, issue or send statement to the exchange, disclosing:

(i) number of sweat equity shares;

(ii) price at which the sweat equity shares are issued;

(iii) total amount invested in sweat equity shares;

(iv) details of the persons to whom sweat equity shares are issued; and

(v) the consequent changes in the capital structure and the shareholding pattern after and before the issues of sweat equity.

Action against intermediaries.

16. The Board may, on failure of the merchant banker to comply with the obligations under these regulations or failing to observe due diligence in respect of valuation of intellectual property or value addition, initiate action against merchant banker in terms of Securities and Exchange Board of India (Merchant Bankers) Regulations, 1992.

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CHAPTER IV

PENALTIES AND PROCEDURE

Power of the Board to order inspection or investigation.

17. (1) The Board may, *suo-motu* or upon information received by it, cause an inspection to be made of the books of account or other books and papers of any company or an investigation to be made in respect of the conduct and affairs of any person associated with the process of sweat equity, by appointing an officer of the Board [1][not below the rank of Assistant General Manager for the purpose of conducting inspection and not below the rank of Division Chief for the purpose of conducting an investigation]:

Provided that no such inspection or investigation shall be made except for the purpose specified in sub-regulation (2).

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2) The purpose referred to in sub-regulation (1) are the following, namely:-
   (a) to ascertain whether there are any circumstances which would render any person guilty of having contravened any of these regulations or any directions issued thereunder;
   (b) to investigate into any complaint of any contravention of the regulation, received from any investor, or any other person;
3) An order passed under the sub regulation (1) shall be sufficient authority for Inspecting or Investigating Officer to undertake the inspection or investigation as the case may be and on production of an authenticated copy of the order, the person concerned shall be bound to carry out the duty imposed in Regulation 18.

Duty to produce records etc.

18. (1) It shall be the duty of every person in respect of whom an inspection or investigation has been ordered under Regulation 17, to produce before the inspecting or the investigating officer such book, accounts and other documents in his custody or control and furnish him with such statements and

[1] Inserted by the SEBI (Issue of Sweat Equity) (Amendment) Regulations, 2003, w.e.f. 27-8-2003.s

information as the said officer may require from the purposes of the inspection or investigation.

(2) Without prejudice to the generality of the provisions of sub-regulation (1) such person shall -

(a) extend to the Inspecting or Investigating Officer reasonable facilities for examining any books, accounts and other documents in his custody or control (whether kept manually or in computer or in any other form) reasonably required for the purposes of the inspection or investigation;

(b) to provide such inspecting or investigating officer copies of such books, accounts and records which, in opinion of the Officer, are relevant to the inspection or investigation or, as the case may be, allow him to take out computer printouts thereof.

(c) to provide such assistance and co-operation as may be required in connection with the inspection or investigation and to furnish information relevant to such inspection or investigation as may be sought by such officer.

(3) The Inspecting or Investigating Officer shall for the purpose of inspection or investigation, have the full powers;

Submission of Report to the Board.

19. (1) The Inspecting or Investigating Officer shall, on completion of the inspection or Investigation after taking into account all relevant facts and circumstances, submit a report to the Board.

(2) On the receipt of report under sub-regulation (1), the Board may initiate such action as it may be deemed fit to do in the interests of investors and the securities market.

Power of the Board to Issue directions.

20. The Board may in the interests of the securities market and without prejudice to its rights to initiate action, including criminal prosecution under Section 24 of the Act or Section 621 of Companies Act give such directions as it deems fit including:-

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(a) directing the person concerned not to further deal in securities in any particular manner;

(b) directing the person concerned to sell or divest the sweat equity shares acquired in violation of the provisions of these Regulations or any other law or regulations;

(c) prohibiting the persons concerned, from accessing the securities market;

(d) directing the disgorgement of any ill-gotten gains or profits or avoidance of loss;

(e) restraining the company from making a further offer for sweat equity.

SCHEDULE

SECURITIES AND EXCHANGE BOARD OF INDIA

(ISSUE OF SWEAT EQUITY) Regulations, 2002

[Under Regulation 6(4)]

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The explanatory statement to the notice and the resolution proposed to be passed in the general meeting for approving the issuance of sweat equity shall, inter alia, contain the following information:

a) The total number of shares to be issued as sweat equity.

b) The current market price of the shares of the company.

c) The value of the intellectual property rights or technical know how or other value addition to be received from the employee or director along with the valuation report / basis of valuation.

d) The names of the employees or directors or promoters to whom the sweat equity shares shall be issued and their relationship with the company.

e) The consideration to be paid for the sweat equity.

f) The price at which the sweat equity shares shall be issued.

g) Ceiling on managerial remuneration, if any, which will be affected by issuance of such sweat equity.

h) A statement to the effect that he company shall conform to the accounting policies as specified by the Board.

i) Diluted Earning Per Share pursuant to the issue of securities to be calculated in accordance with International Accounting Standards / standards specified by the Institute of Chartered Accountants of India.

Notification: No. SO 1031 (E), dated 24-9-2002.

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