New insider norms: Sebi to clear air on Esops soon

The Securities and Exchange Board of India (Sebi) might soon clear the air over exercising employee stock ownership plans (Esops) in light of the insider trading regulations that came into effect last month. The new rules on insider trading prohibit an employee from buying and selling ashare within a period of six months. This has raised doubts over dealing (buying or selling) in shares pursuant to six months of Esops, known as contra trade.

The stock market regulator plans to allow such trades with the pre- clearance of a companyappointed compliance offer. “A compliance officer can clear a trade after Esops are exercised. The employee, however, will have to give a written application mentioning the reasons,” said a source.

The Insider Trading Regulations 1992, following a clarification in 2009, allows contra trades only in personal emergencies. The concerns on the treatment of Esops arose when the new insider- trading regulations did not specifically exempt Esops from the ambit of insider trading. “ Restriction in Clause 4.2 of insider trading is intended for transactions in the secondary market and is not applicable to the exercise of Esops and sale of these shares,” Sebi clarified in 2009.

The Clause allowed employees to subscribe to the ESOPs even if they had sold shares during the previous six months. However, restrictions were applicable on buying for the next six months upon selling of exercise Esops.

Lawyers and companies had been approaching the regulator for a clarification on Esops.

“The new regulations do not provide any such exemption and consequently, the regulations will apply both at the time of exercise of options and on the sale of those shares. As a result, an employee will not be able to do a contra trade within six months from the date when shares were issued upon exercise of option,” said Lalit Kumar, partner, J Sagar Associates.

However, Sebi sources say there is enough clarity in the present regulations that could define treatment of Esops. “ If market needs more clarity, we will issue a note regarding the same,” said a source.

Some legal experts say in the absence of a clarification from the regulator, one could take cues from the previous clarification. “ The provisions pertaining to treatment of Esops were separately clarified by Sebi under the previous insider trading regulations.

The current set of regulations do not specify the treatment of Esops. However, taking some guidance from clarifications provided by Sebi earlier, the employee should be able to subscribe to Esops even if such employee has sold shares during the previous six months and the same should not be tantamount to a contra trade.

However, once shares acquired through Esops are sold in the market, the restriction on buying should become applicable for next six months,” said Tejesh Chitlangi, partner, IC Legal.

Similarly, while exercising Esops, the code of conduct framed by the company and the regulations must be complied with.

Experts say allowing ‘ contra trade’ with prior approvals of a compliance offer will only bring partial relief. “ It will only be a partial exemption and not a complete exemption as the employee will have to seek preclearance at the time of exercise of the options and then again at the time of sale. This will limit the ability of employees to exercise Esops freely,” said Kumar. India Inc, too, is said to have approved Sebi citing difficulties in appointing compliance officers. “ A lot of feedback is about putting too much onus on the compliance officer. But, this is the intent of regulations that companies should be the first- level check on insider trading,” said a source.

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