

ESOP Direct

A  **QAPITA** Company

EQUITY COMPENSATION

TRENDS IN INDIA AND SOUTH EAST ASIA (SEA) - 2022

AN ESOP DIRECT REPORT

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Dear Readers,

Welcome to the 10th edition of our Survey on Equity Compensation Trends in 2022 in India & South East Asia.

This year, leveraging the synergies of both Qapita and ESOP Direct networks, we have secured a high participation rate and extensive coverage. This survey incorporates inputs from 309 Companies (both Listed and Unlisted in India and Unlisted Companies in South East Asia) spread across 22 different sectors. We thank all participants for sharing their plan designs, insights and experiences with us. We can confidently claim that this survey comprehensively represents Indian and South East Asian corporate trends and practices with respect to equity compensation.

Whilst this is the 10th edition of this survey in India, this is the first time we have added an international segment with South East Asia. Over 85 companies have participated and contributed to this survey from the South East Asia region this year.

Our endeavour is to provide analysis that covers market practices and identifies the relationship between various aspects of plan design and administration. There are some interesting observations in this Survey, which would be helpful in understanding and implementing Equity Compensation Plans, and achieve the outcomes desired by management as well as employees. This year we have also analysed some additional responses, which are relevant to the changes in regulations as well as the overall economic situation.

Few key highlights of this survey are as follows:

- Almost 92% to 97% of companies agree that their ESOP Plans have achieved their stated objectives. Over the last ten years, the trend has always been above 90%.
- Companies are also looking at offering Options at a discount to market price or face value linked to performance vesting conditions.
- In Listed Companies in India – Trust route is getting more popular, and to reduce dilution, Companies are also moving towards secondary acquisition.
- A key trend we have been tracking over the years is coverage and quantum. This year we have observed that Companies have increased their coverage and granted options to more employees (deeper distribution within the organisation).

We hope that this Report helps readers to access and understand the current trends in Equity Compensation plans in India and South East Asia.

We sincerely thank all the participants and invite them for continued participation in the future. We will endeavour to make this Survey more inclusive every year. As always, we welcome suggestions to improve and refine our work. Please send in your comments and suggestions to rahul@esopdirect.com

Warm regards,

Ravi Ravulaparthi,
CEO and Co-Founder, Qapita



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EXECUTIVE SUMMARY

EXECUTIVE SUMMARY

Basic objective of implementing Equity Compensation Plans



Retention and reward continue to be the most significant reasons for granting Equity-based compensation, followed by wealth creation and employee ownership in Listed and Unlisted Companies in India.

For Unlisted Companies in South East Asia (SEA) Retention and attraction of talent continue to be the main factors for granting Equity-based compensation, followed by achievement of performance targets.



Achievement of Objectives

92-97% of the Companies have achieved (fully or partly) the objective of implementing Equity compensation plans in all regions.

Coverage

- 68% of Listed Companies in India grant options to less than 10% of employees.
- 42% of Unlisted Companies in India and SEA covers up to 10% of employees.
- However, we have also seen that around 38% Unlisted Companies in SEA cover more than 50% of their employees.





Selection of Instruments

ESOPs (including discounted ESOPs) continue to be the most popular instrument. RSUs are the next most popular option in Listed/Unlisted Companies in India and Unlisted Companies in SEA

Liquidity for Unlisted Companies

36% of the Unlisted Companies in India have achieved liquidity out of which 37% have cash settled the options and 28% have brought back shares.

13% of Unlisted Companies in SEA have achieved liquidity out of which 33% have cash settled the options and 27% have brought back shares.





Vesting Period

43% of Listed, 50% of Unlisted Companies in India and 72% of Unlisted Companies in SEA have a vesting period of 4 years or more.



Vesting Frequency

77% of Listed, 73% of Unlisted Companies in India and 59% of Unlisted Companies in SEA have an annual vesting schedule.



Exercise Period

91% of Listed Companies in India have an exercise period of up to 6 years.
61% of Unlisted Companies in India and 55% of Unlisted Companies in SEA prefer to allow exercise in connection with a Liquidity Event.



Exercise Price

Listed Companies in India are increasingly moving away from market price grants to grants at face value or at a discount to market price. Unlisted Companies in India are seen shifting from grants at fair market value (FMV) to grants at face value or at a discount to FMV.
Whereas, Unlisted Companies in SEA prefer face value or discount to FMV grants followed by grants at FMV.



Implementation Route

Increasing number of Listed Companies in India are turning to Trust route. Currently, 43% of such Companies follow Trust route as compared to 20% as per the last survey.
90% of Unlisted Companies in India and 92% of Unlisted Companies in SEA have implemented their ESOP Plans directly.

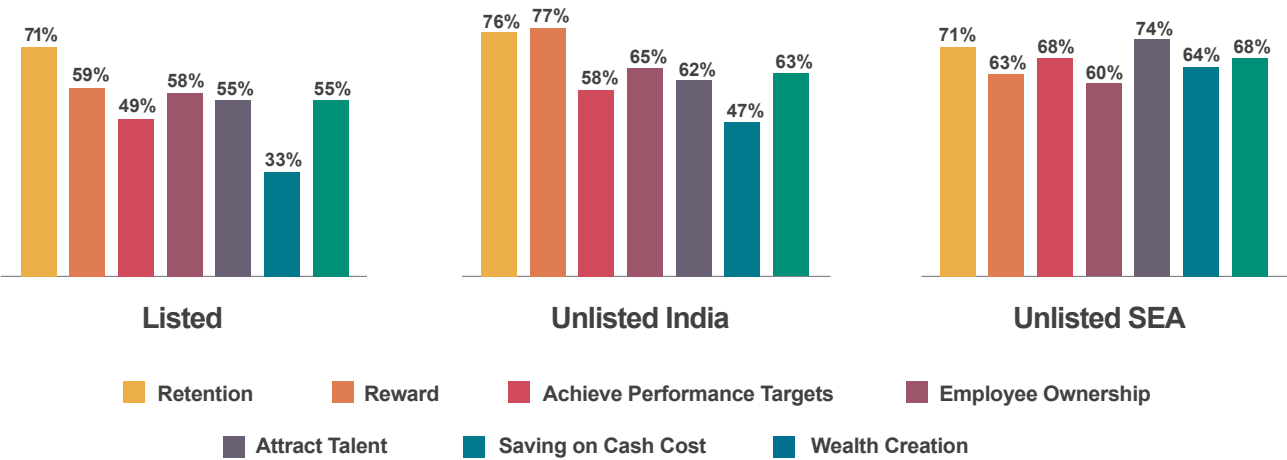


PLAN DESIGN

OBJECTIVES AND EFFECTIVENESS OF ESOP PLANS

2.1

Overall objectives of implementing Equity Compensation Plans



**In some cases, totals may not add up to 100 percent due to rounding or Companies having selected more than one answer*

In line with the past trend, retention and reward continue to be the main drivers for Companies to implement an Equity Compensation Plan.

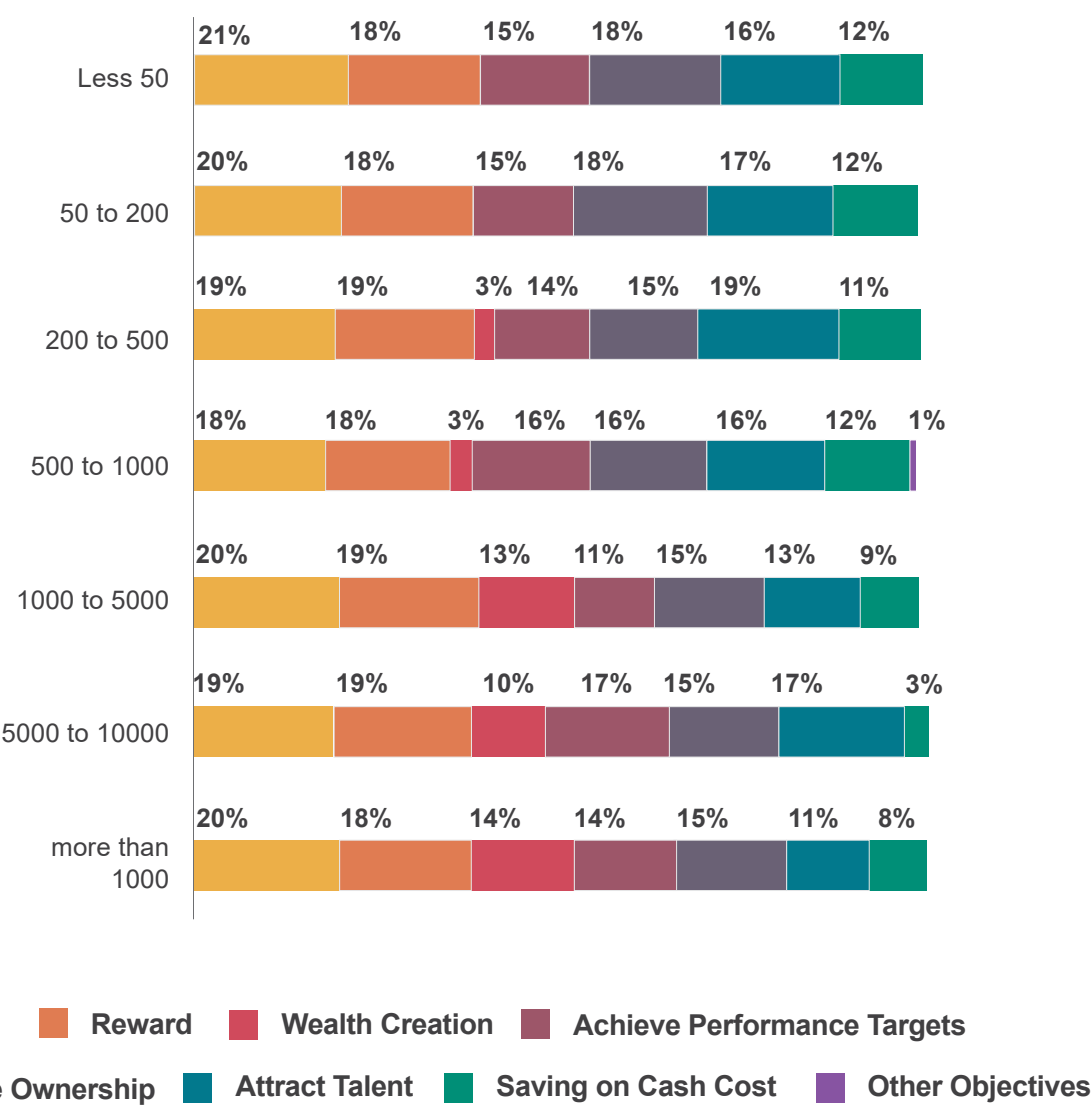
71% (2020:84%) of the Listed Companies responded retention, and 59% (2020:78%) of the Listed Companies responded rewards to be the main objectives of implementing Equity Compensation Plans.

Key drivers for implementing an Equity Compensation Plan, even in the case of Unlisted Companies, are retention 76% (2020:98%) and reward 77% (2020:85%), but weightage has also shifted towards other objectives of wealth creation and saving on cash cost.

In this Survey, we noticed that Listed and Unlisted Companies in India, the weightage of retention and reward has shifted towards other objectives, such as attracting talent and wealth creation.

Unlisted Companies in SEA region, attracting talent is a primary objective in implementing equity compensation plans, followed by retention.

Plan objectives vis-à-vis size of Company



We further evaluated the objectives of implementing Equity compensation plans for the Companies based on their employee strength.

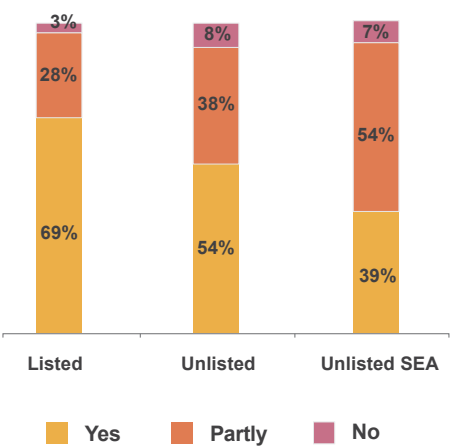
We can see a very clear trend of increasing importance of providing wealth creation opportunities as the size and strength of the Company is increasing.

A trend of decrease in weightage of saving on cash cost can be seen as the Company increases in strength. Employee ownership and reward continue to be rated as one of the important objectives of implementing an Equity compensation plans in all Companies.

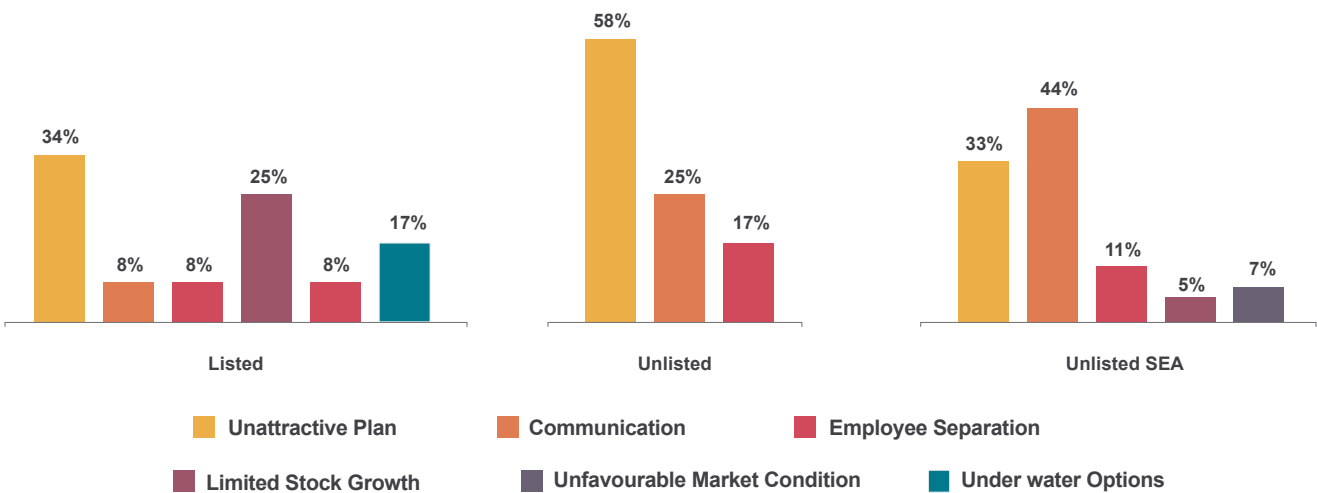
Have Equity compensation plans achieved their objectives?

Over 90% of the Companies feel that their Equity compensation plan objectives were fully / partly achieved. Insignificant small number of Companies feel that Equity compensation plans did not achieve their stated objectives. Achievement of desired outcome from Equity based plans, is higher in Listed Companies as compared to Unlisted Companies in India and SEA.

We further asked the Companies the reasons, in their opinion, their Plans did not succeed.

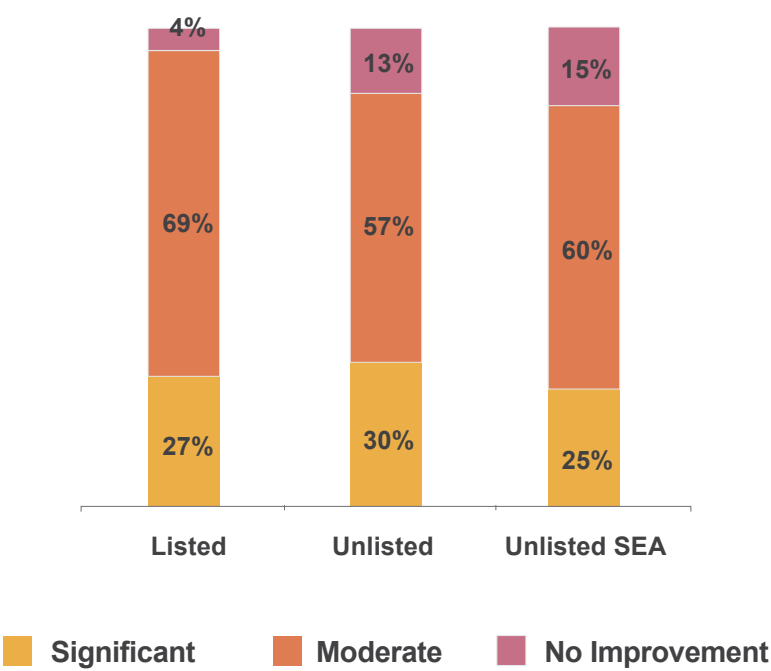


Reasons for not achieving objectives



While Listed Companies feel that the growth of their stock and market conditions did not favour achievement of objectives or partly achieving objectives, for Unlisted Companies most important reasons for not achieving or partly achieving objectives are unattractive plans and employee separation, which could be due to lack of proper communication or grant of inadequate quantum as Equity compensation to ensure retention of employees in the Companies.

Whether Equity compensation has brought a cultural change in the organization?



Apart from quantitative factors, we also asked if the Companies have experienced any cultural change due to Equity Compensation Plans. About 96% of Listed Companies and Over 85% of Unlisted Companies (India and SEA) have seen significant to moderate levels of cultural change in the organization. This trend clearly supports that Companies have not only achieved quantifiable objectives as well as qualitative objectives, through Equity Compensation Plans.

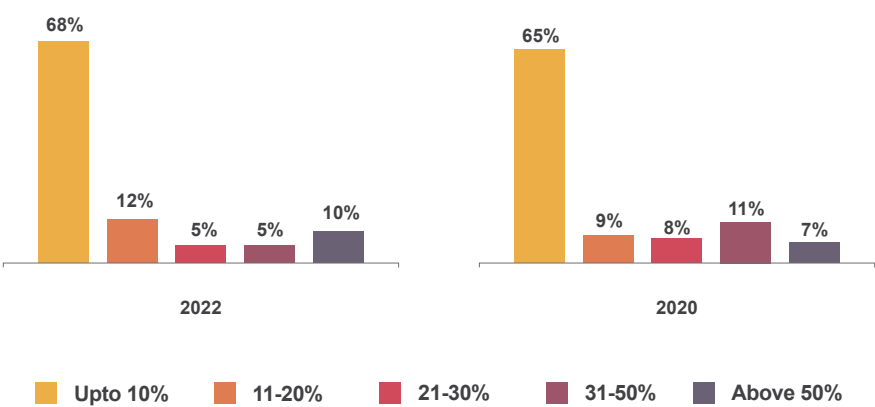


DESIGN TRENDS - LISTED COMPANIES IN INDIA

COVERAGE

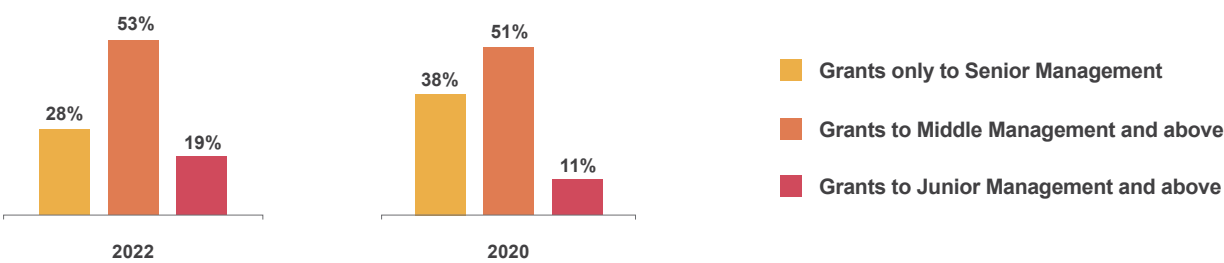
3.1

Employees covered under Equity Compensation Plan



Over the years, a clear trend towards covering fewer employees instead of having a broad-based plan has emerged for Listed Companies. There is a slight increase in the category of coverage up to 20% and coverage above 50% of the total employee strength. This looks mostly broad based one time plans in some of the companies.

Mix of grant of options to senior/middle/junior management level of management



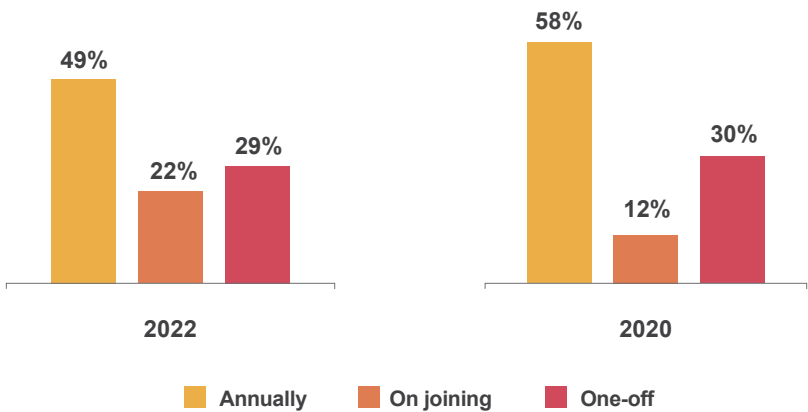
Around 53% of Companies granted to Middle Management and above, and 28% covered only Senior Management. There is a considerable reduction in Companies granting only to Senior Management as compared to covering of all employees, i.e. Junior Management and above (2022:19%) (2020:11%)

GRANT PRACTICES

3.2

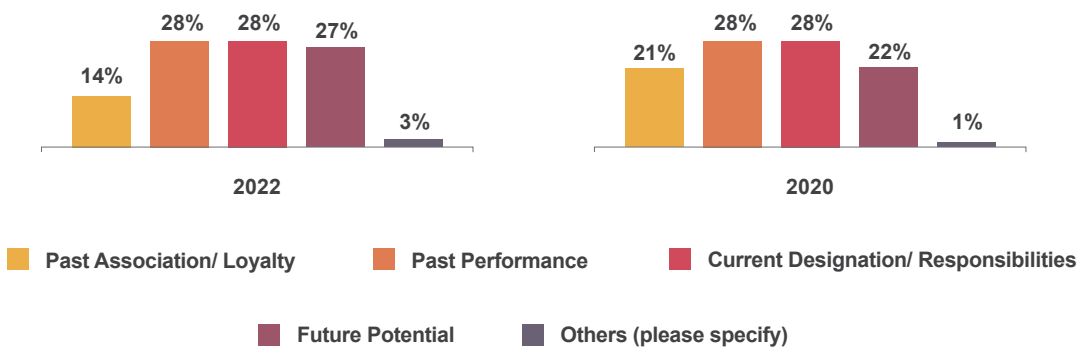
Frequency of Grants

49% (2020:58%) of the Companies continue to follow last year’s trend of granting options annually. 51% (2017:34%, 2015:23%) of the Companies have either on-joining or one -offs grants as compared to 42% in 2020. There is an inclination towards joining grants by Companies. This clearly shows of attracting talent is one of the main objectives of grant under Equity based Plans.



Parameters for selection of employees for Equity Compensation

There appears to be a shift in preference for grating based on Loyalty 14% (2020:21%) to grating based on the future potential of employees 27% (2020:20%). Past performance and the Current role of employees are still dominant parameters for the selection of employees by Listed Companies.



Estimated benefit sought to be passed by way of Equity compensation as per-annum benefit

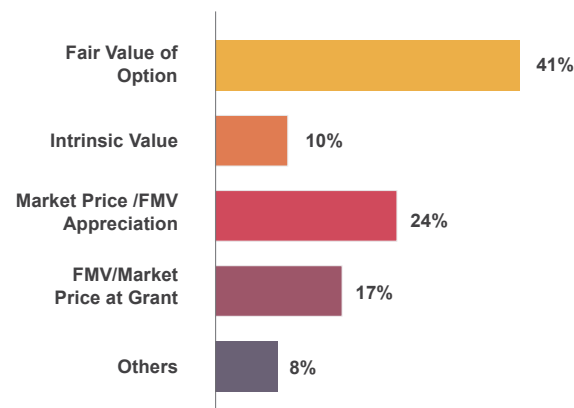
The quantum of benefit passed by way of Equity compensation is one of the key decision points. The most used and easily understood measure for this is what percentage of the annualized CTC should the employee be expected to make from his Equity compensation grants.



Estimated benefit that employees would make is based on the relative criticality of employees in the organization.

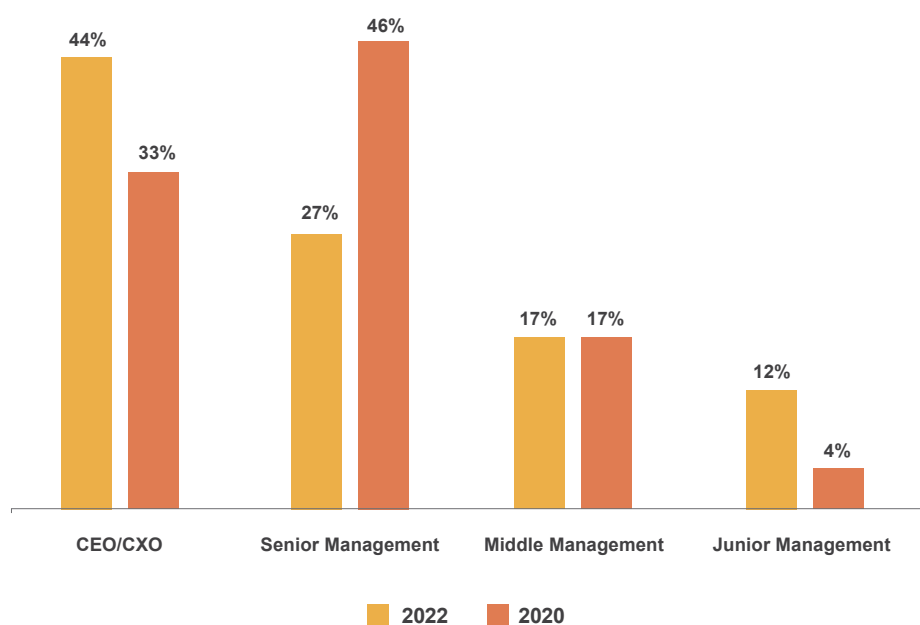
Most Companies tend to give more benefit (more than 100% of CTC per annum) to their highly critical employees and all CXOs; whereas Junior management is getting (up to 25% of CTC per annum) over the vesting period.

We further asked, what methods they have used to decide options to be granted to an employee based on the anticipated value or expected benefits?



Fair Value of options is the most popular and scientific method (using the option pricing model) of allocating options based on anticipated (2022:41%), next being expected appreciation in Market price (2022:24%).

Employee-wise mix of options granted (stock options, SARs, other instruments) as a % of total options granted



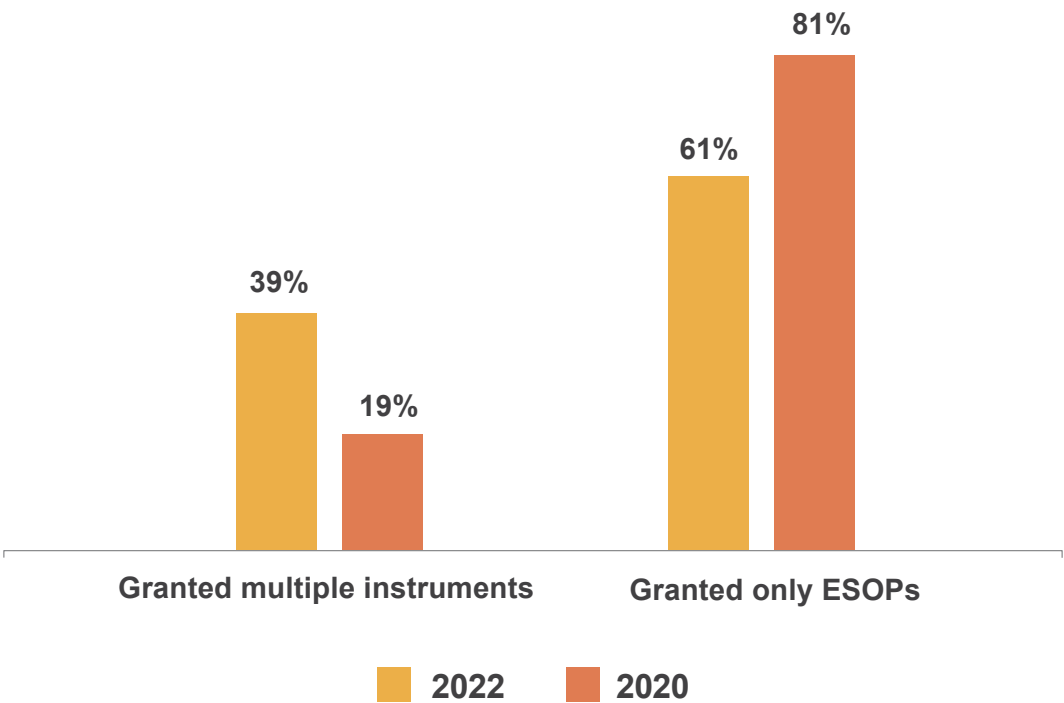
The concentration of grants to CEO/ CXO level employees has often been debated. We asked Companies about the concentration of their grants.

Over the last 5 years, the total allocation to CEO, CXO has increased from 20% in 2015 to 44% in 2022. If we club the senior management team (CXO reportees) with CEO/CXO, this team gets more than 70% of the total allocation.

These trends are in line with the earlier observation that Companies are following the principle of granting more to fewer employees.

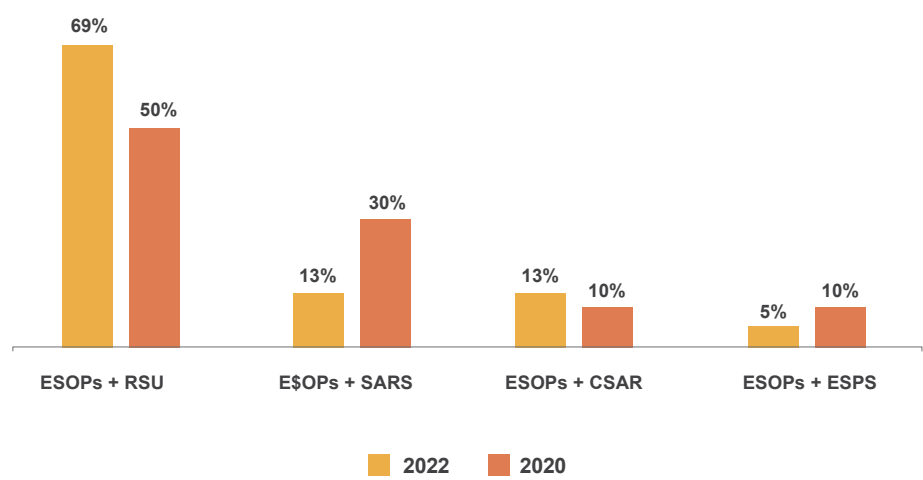
Instruments implemented viz: ESOPs, SARs, RSUs, Phantom, others?

61% (2020:81%) of the Companies have granted only ESOPs to their employees. 39% of the Companies have granted other instruments like RSUs (deep discounted ESOPs), stock appreciation rights (SARs), Cash settled SARs (CSARs), and Employee stock purchase scheme (ESPS) along with ESOPs. The grant of combination of instruments has increased significantly during the last two years.



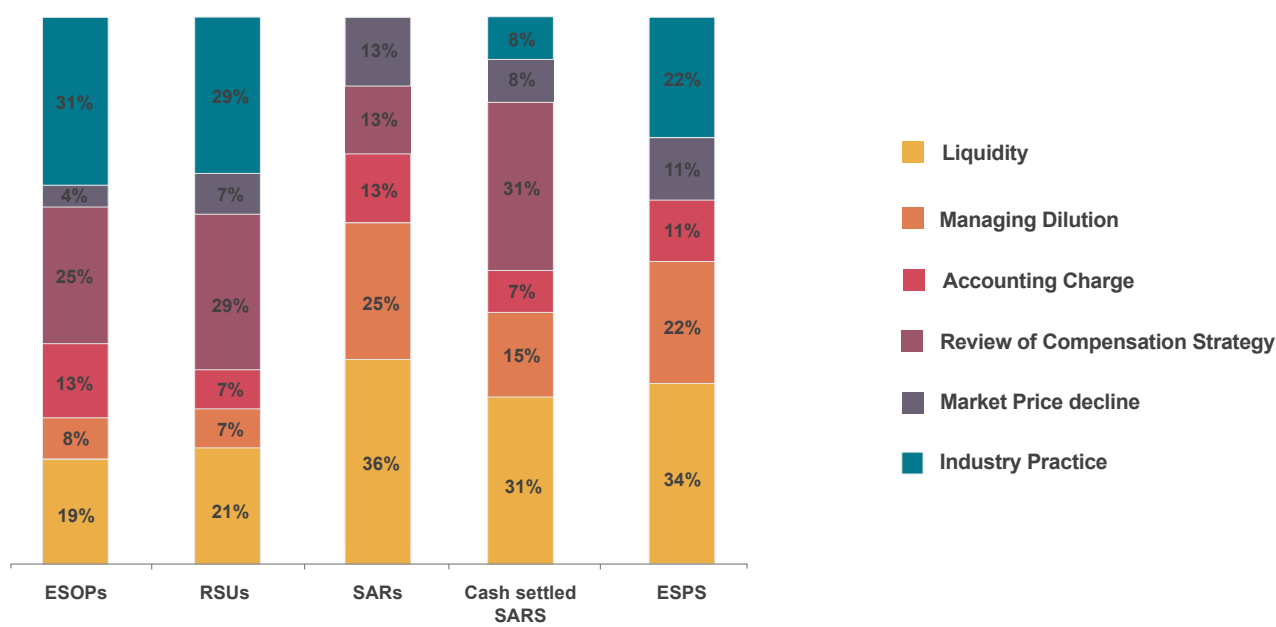
Granting ESOPs in combination with other instruments

We wanted to check which instruments are preferred along with ESOPs -



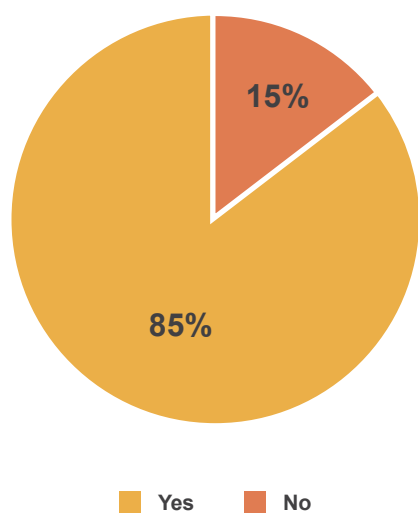
In earlier years, SARs along with ESOPs was the preferred instrument (2020:30%); however in 2022, this combination has been replaced with RSUs. 69% (2020:50%) Companies granted RSUs along with ESOPs to their employees.

Further, we asked Companies what were the drivers for implementing multiple instruments.



Liquidity, Accounting charge, Review of compensation strategy and industry practice are drivers for implementing ESOPs. Whereas, RSUs are implemented mostly for aligning with Industry practices and changes in compensation strategy. SARs and Cash settled SARs were granted primarily to manage dilution & provide liquidity to employees.

If Phantom/Cash settled SAR, is there a provision in the Scheme for capping the liability of cash outflow?

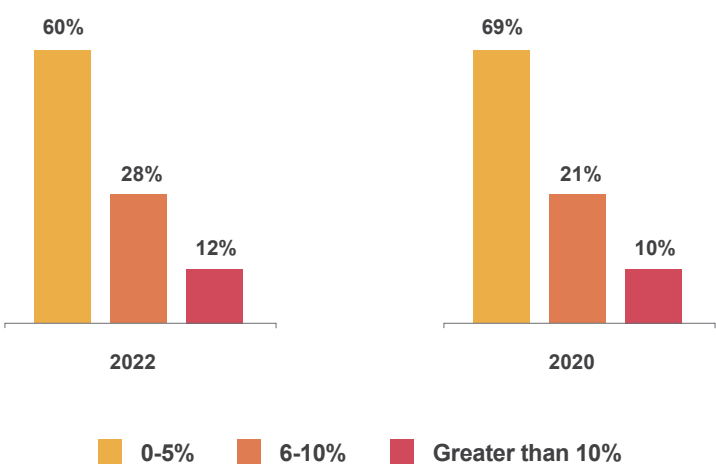


85% of the Companies have not capped liability arising due to settlement of Phantom or Cash Settled Option, and 15% of the Companies prefer to put a cap to settlement amount or cash outflow.

ESOP POOL

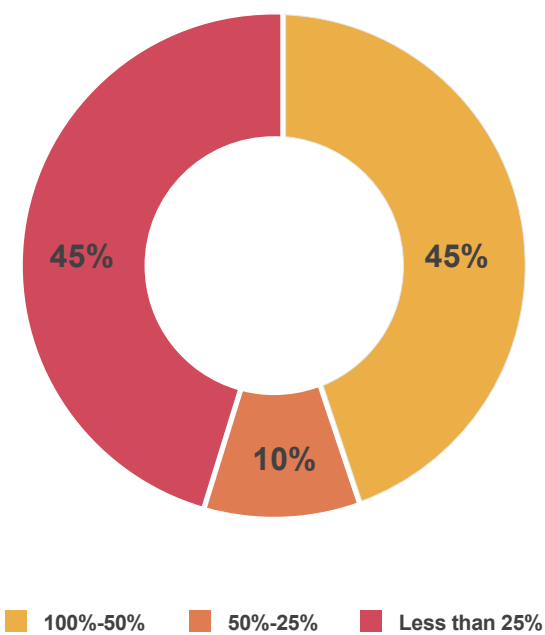
3.3

Percentage of total options (equity-settled) approved by the shareholders



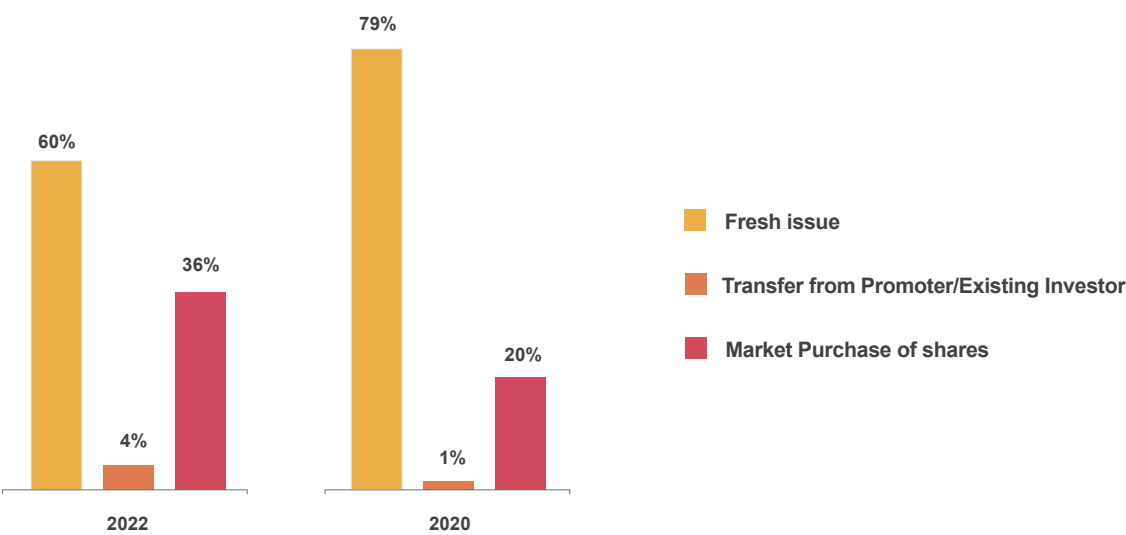
ESOP Pool approved by shareholders up to 5% has reduced from 69% in 2020 to 60% in 2022. 28% of Listed Companies are expanding their pool or made grants due to which ESOP pool has increased up to 10% as compared to 21% in 2020.

Percentage of ESOP pool utilized out of total pool approved



45% of Companies have utilized between 50%- 100% of the ESOP pool approved and the same percentage, i.e. 45% of Listed Companies have utilized less than 25% of the ESOP pool.

Source of Equity

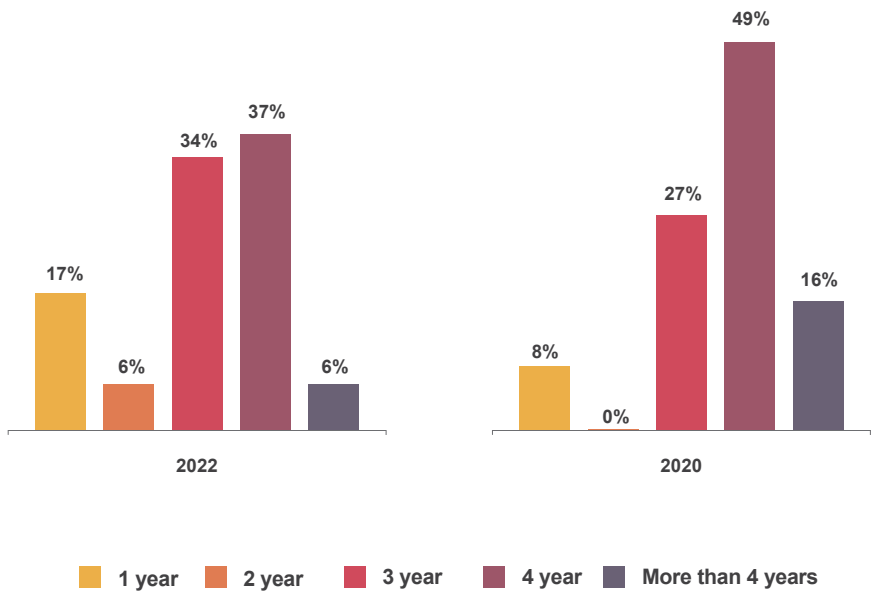


There is a significant decline in the number of Companies going for Fresh issue of Shares, i.e., from 79% in 2020 to 60% in 2022 and a corresponding increase in the Market purchase of Shares (Secondary acquisition) 36% in 2022 from only 20% in 2020.

VESTING

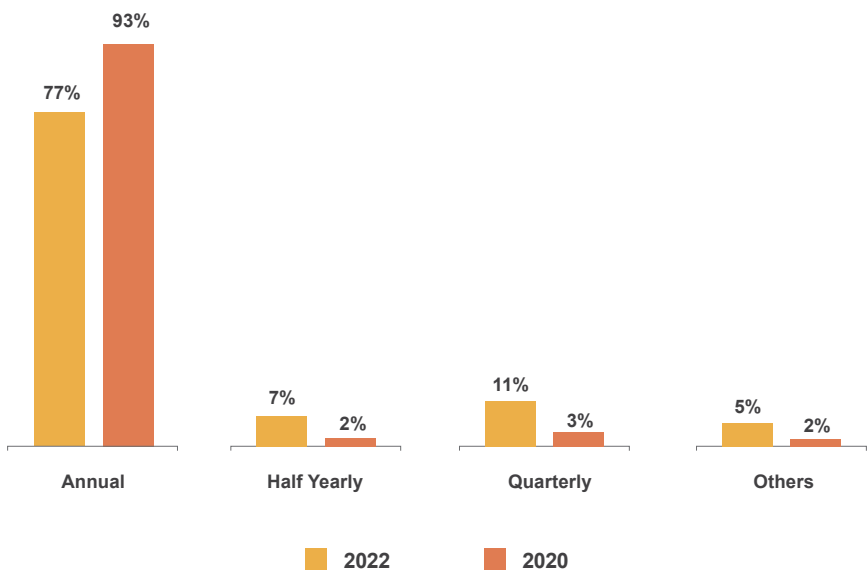
3.4

Vesting Period



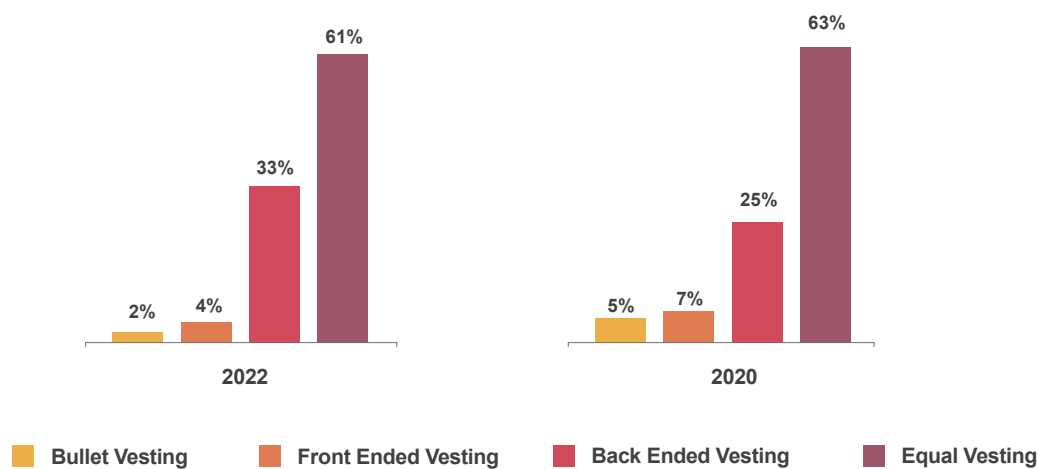
71% (2020:76%) of the Companies have a vesting period of 3 or 4 years, with more companies preferring a 4 year vesting period (2020:37%).

Vesting Frequency



77% of Companies continue to have annual vesting as compared to 93% in 2020. Shift in the trends is due to Companies also moving towards Half yearly and Quarterly vesting schedules.

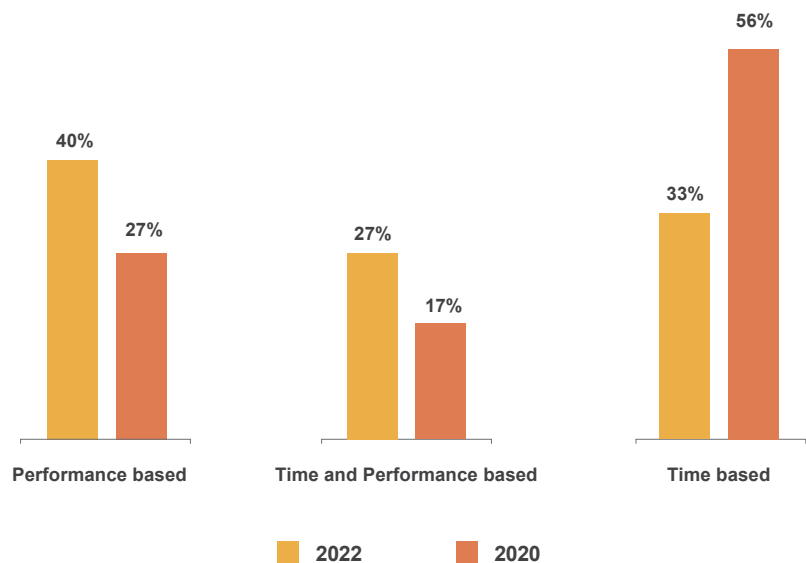
Vesting Type



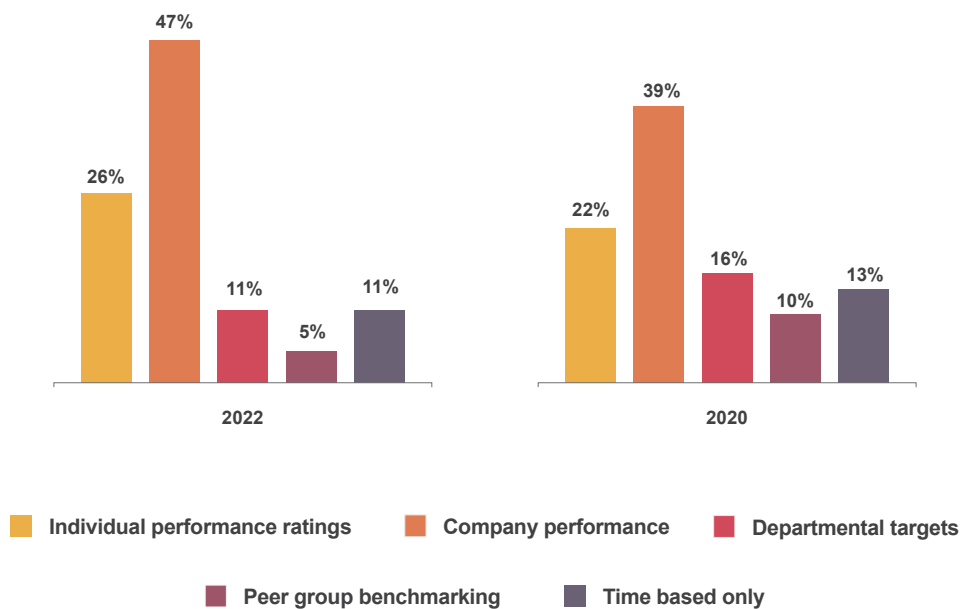
Similar to last year’s trend 61% of Companies still prefer equated vesting. 33% of Companies have Backend vesting to ensure talent retention.

Time-based or performance-based vesting

As compared to our last Surveys (2020 & 2017), Companies seem to be moving towards granting performance-based options.

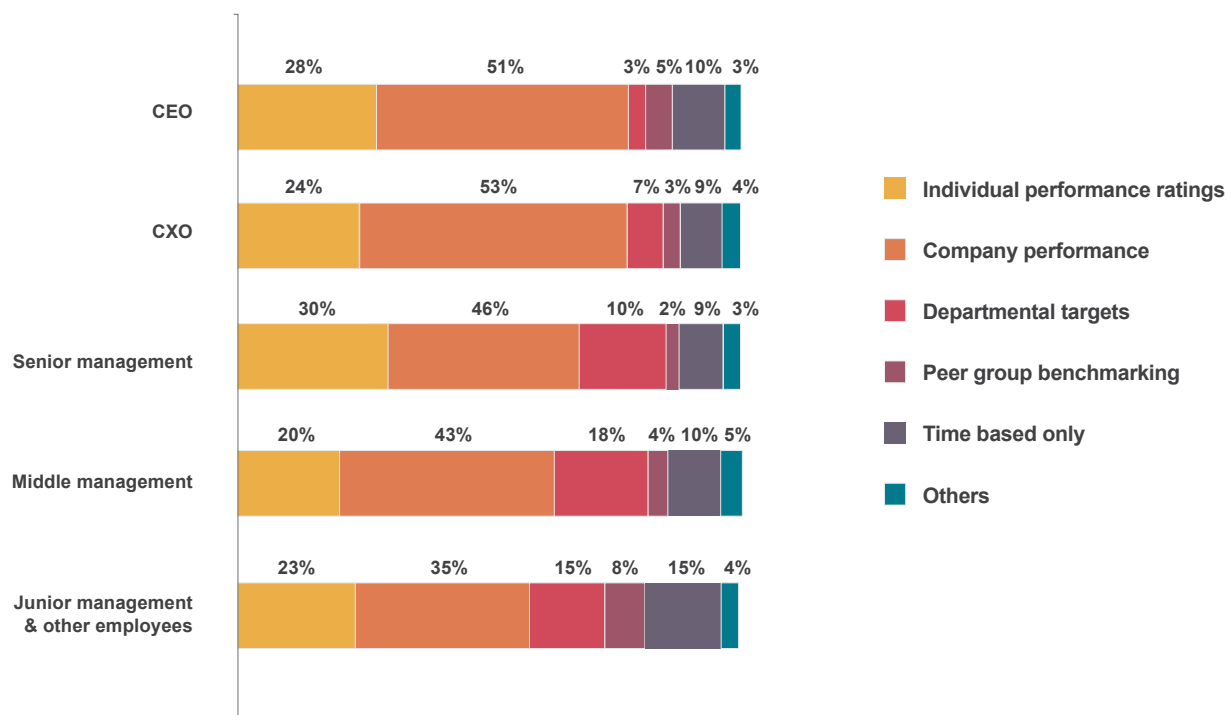


40% of the Companies have 50% or more weightage for performance-based conditions were as 33% of Companies have only Time (continued service) as the vesting condition. Listed companies now preferring either Performance or a mix of Time and Performance as vesting conditions compared to only Time-based vesting.



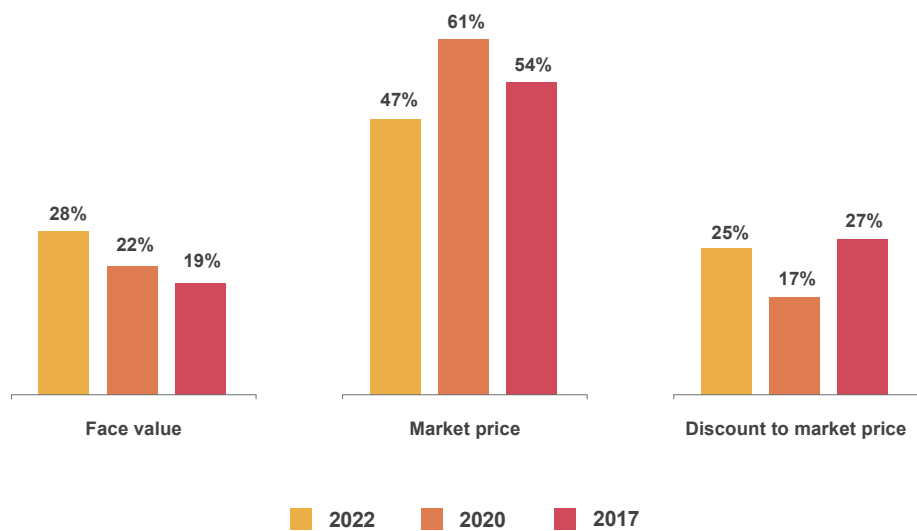
47% (2020:39%) Companies have Company performance as a vesting criteria, and 26% (2020:22%) Companies have individual performance as vesting criteria. We have noticed a substantial increase in Companies having company performance as a vesting criterion.

We further analyzed; designation wise various performance conditions preferred as vesting by companies.

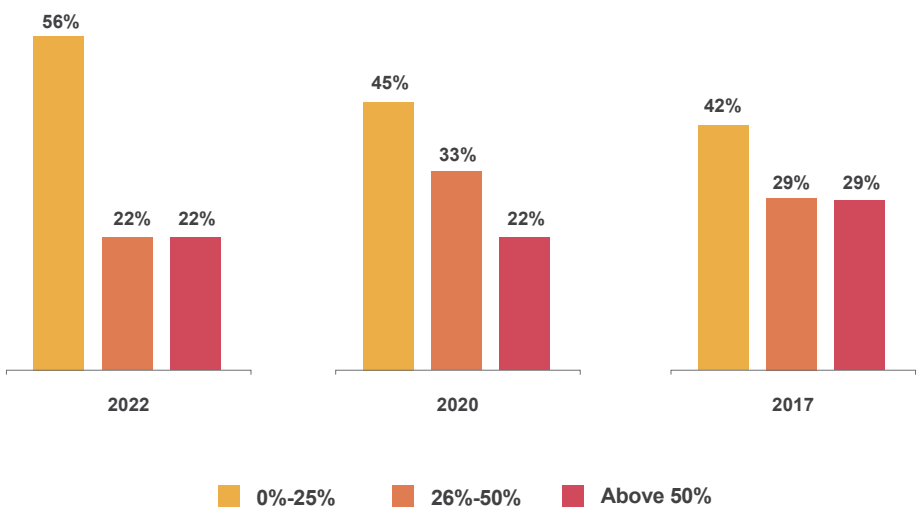


EXERCISE PRICE

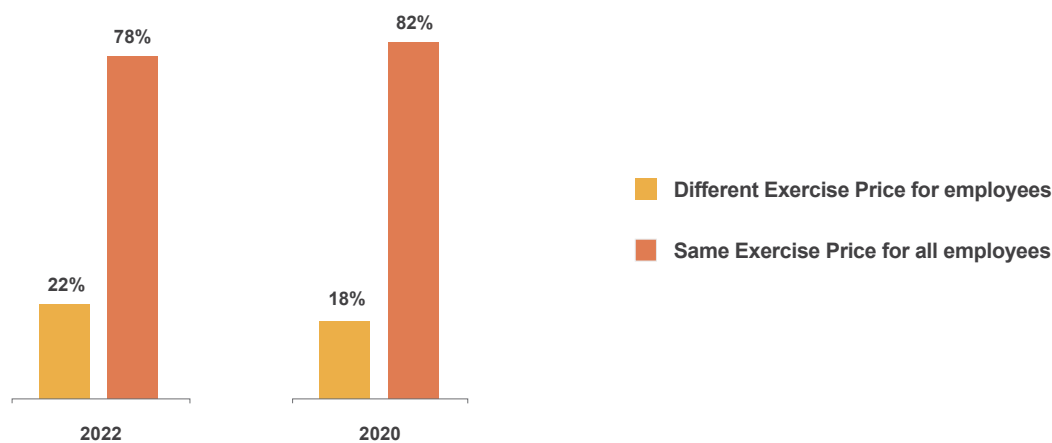
3.5



While Market price is the most preferred exercise price with 47% of Companies (2020:61%), we also observe that face value grants have shown an increasing preference for the last few years, i.e. 28% (2020:22%, 2017:19%). Discount to Market price has increased weightage as compared to previous years i.e. 25% (2020:17%).



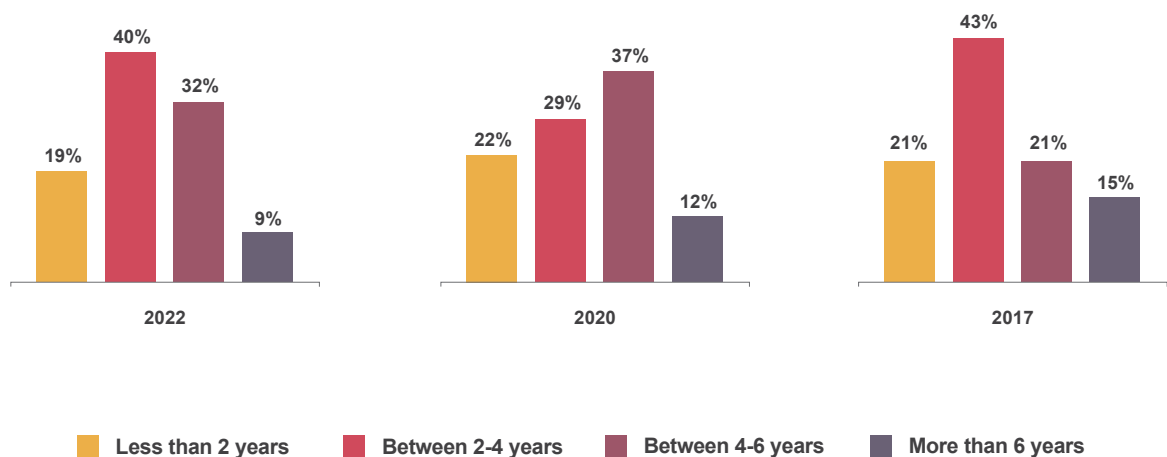
56% of Listed Companies grant options at a discount of up to 25% of the market price. Whereas we can see a downward trend in the category of discounts up to 25%- 50% with only 22% (2020: 33%, 2017:29%) of Companies.



78% (2020:82%) of the Companies do not have different prices for a different set of employees as compared to 22% (2020:18%) who have different exercise prices for various employees. Listed companies are gradually moving towards a mix of instruments and different exercise prices to meet various organizational objectives.

EXERCISE PERIOD

3.6

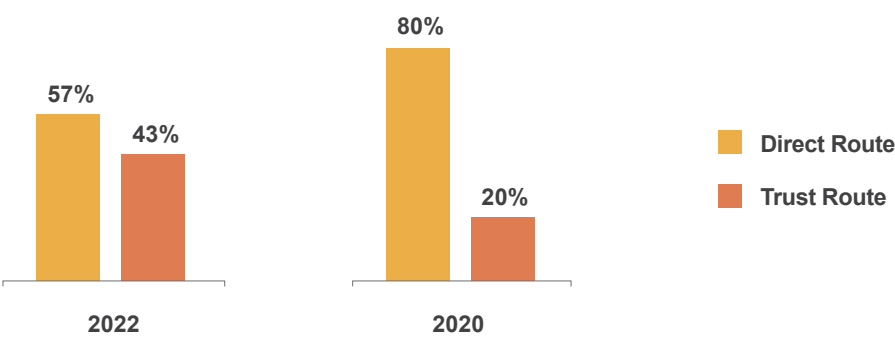


40% (2020:29%) of the Listed Companies have an exercise period between 2 to 4 years. Only 9% (2020:12%, 2017:15%) of Listed Companies have opted for an exercise period of more than 6 years. 32% (2020:37%) of Companies still prefer 4-6 years of exercise period.

GENERAL TRENDS

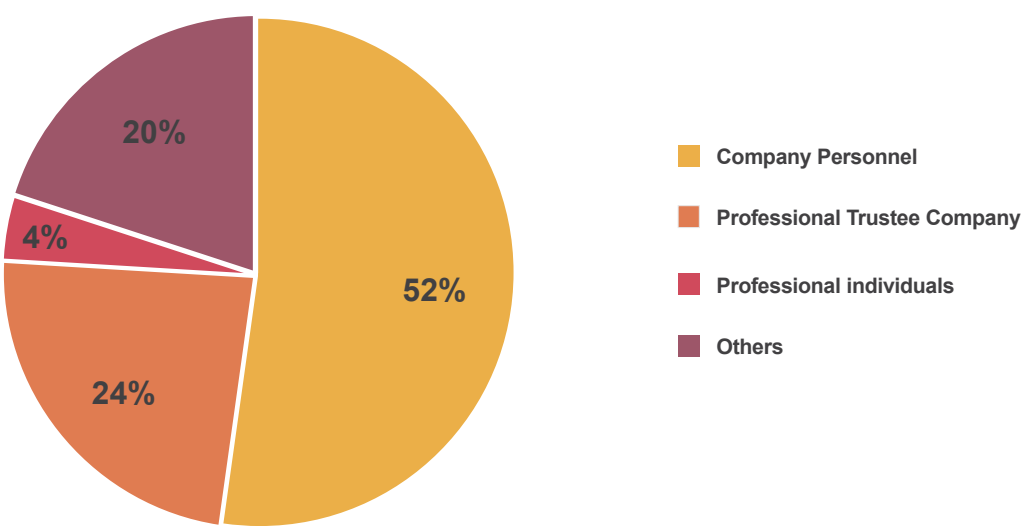
3.7

Route for implementing ESOPs



Direct Route remains the preferred mode for implementing ESOPs by Listed Companies, though the Trust route has also gained significant weightage over the years.

Constitution of Trustees



Only 28% of Companies appointed a professional trustee company or professional individuals as their trustees in 2022. Whereas the Companies appointing for Company Personnel has increased to 52% over the past years (2020:33%).

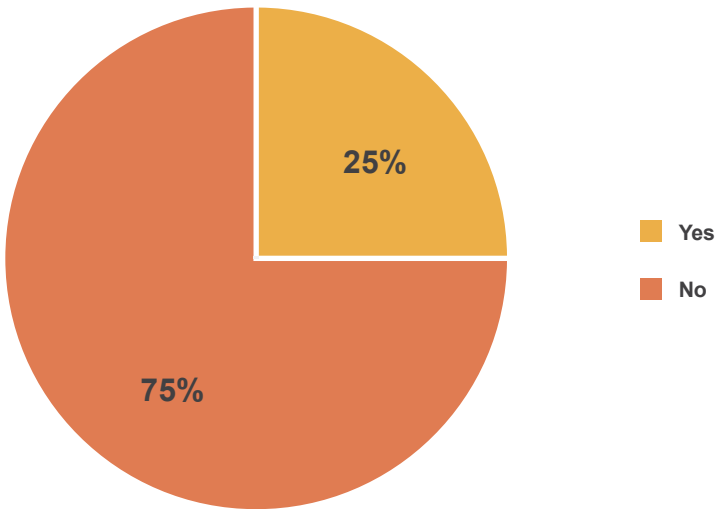
How does the Company recover perquisite tax from the employees?



UNDERWATER OPTIONS

3.8

We asked Listed Companies whether they have faced options of being underwater



How did Companies address the underwater situation?

Most companies decide to revise their exercise price and exercise period while some also consider granting RSUs in lieu of underwater options to create value in options. Buyback of shares was also implemented by a few Companies to reinstate faith and value in the ESOP Plan.

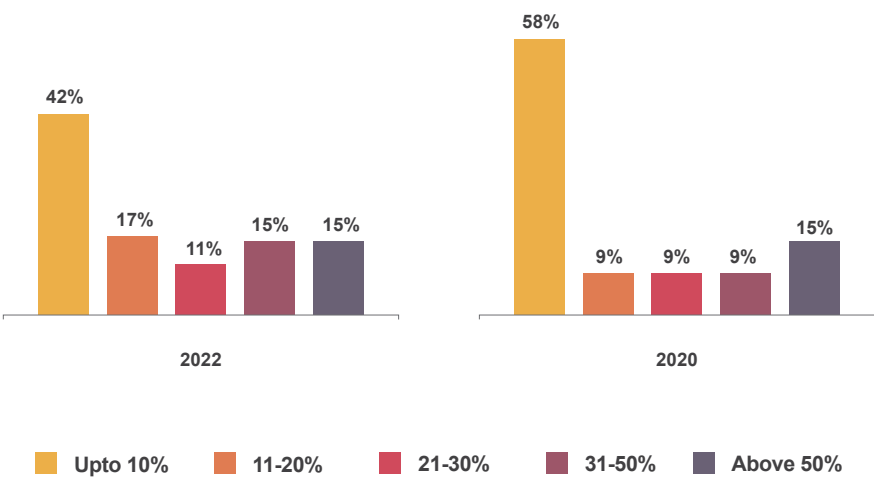


DESIGN TRENDS - UNLISTED COMPANIES IN INDIA

COVERAGE

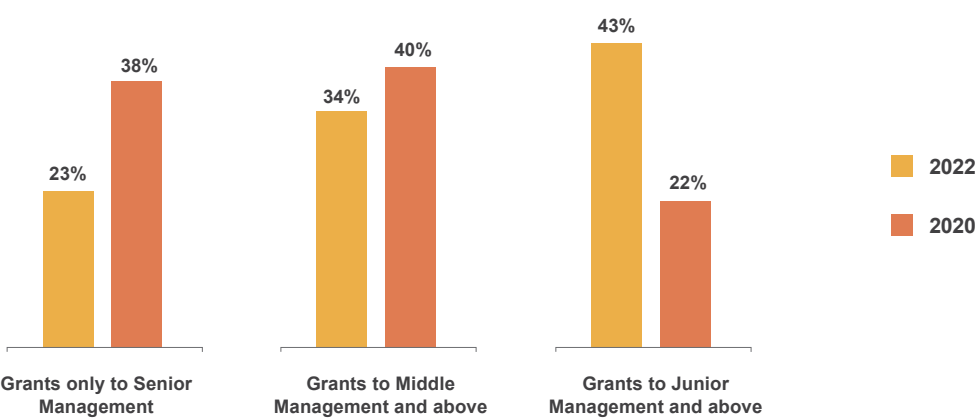
4.1

Employees covered under an Equity Compensation Plan



The practice of covering fewer employees instead of having a more broad-based plan continues, with 42% of Unlisted Companies in India still covering only 10% of total strength (2020:58%). But, it is also observed that Companies are moving towards increasing the coverage up to 20% of total strength (2020:9%) as a trend.

Mix of grant of options to senior/middle/junior management level of management



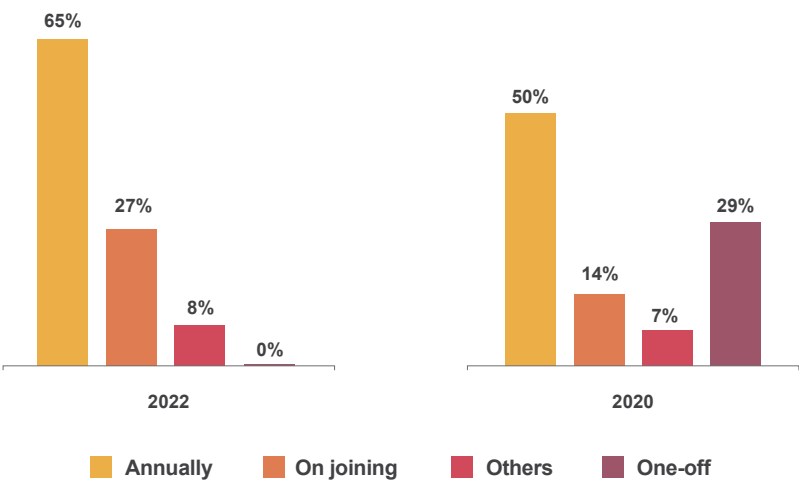
In line with the trend to cover fewer employees, Companies are granting to only Middle and Senior Management. Around 57% of Companies are granting to Senior and Middle Management. There is a considerable increase in Companies granting to Junior management from 22% in 2020 to 43% in 2022.

GRANT PRACTICES

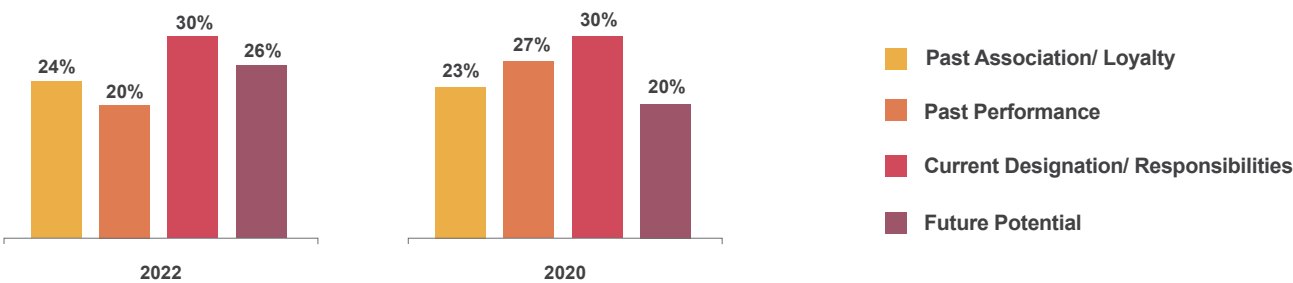
4.2

Frequency of Grants

Increasing trend of annual grants can be seen amongst 65% of Unlisted Companies in India 50% in 2020. 35% of the Companies grant on-joining and includes Companies who said that there is no set frequency of grant or options are granted quarterly or granted options on a case-to-case basis.



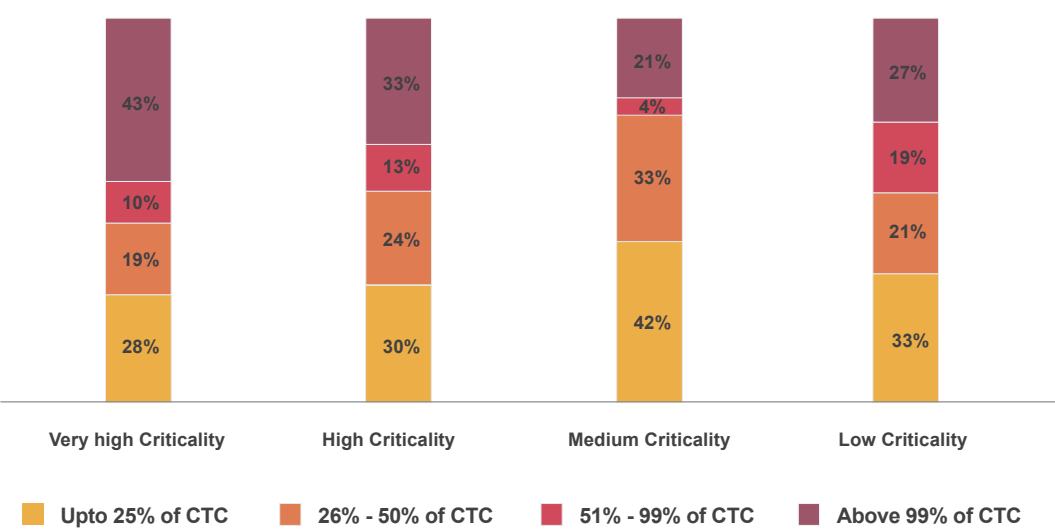
Parameters for selection of employees for Equity Compensation



There does not appear to be a single dominant parameter on which Companies decide on whom to grant. Current designation still remains the topmost selection criteria for the entitlement, i.e. 30%, followed by future potential 26% in 2022.

Estimated benefit sought to be passed by way of Equity compensation as per-annum benefit

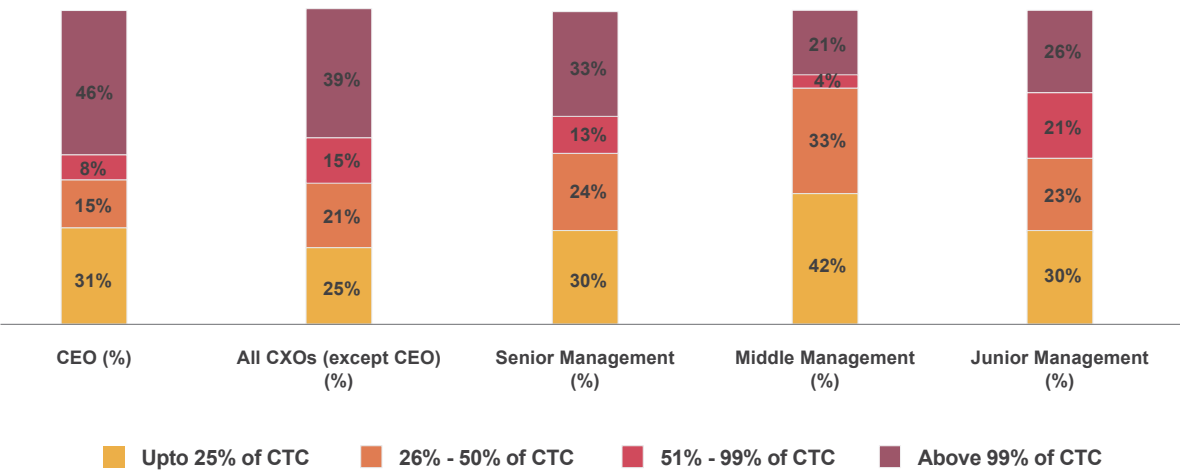
The quantum of benefit passed by way of Equity compensation is one of the key decision points. Most used and easily understood measure for this is what percentage of the annualized CTC should the employee be expected to make from his Equity compensation grants?



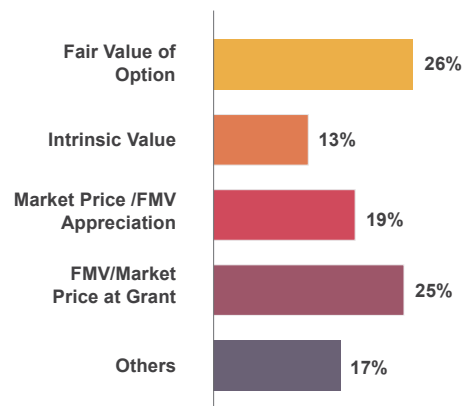
Estimated benefit that employees would make is based on the relative criticality of employees in organization.

43% of Companies tend to give more benefits (more than 100% of CTC per annum) to their highly critical employees; we can also see the quantum of benefit reducing as the criticality decreases.

Estimated benefits offered as per the designations

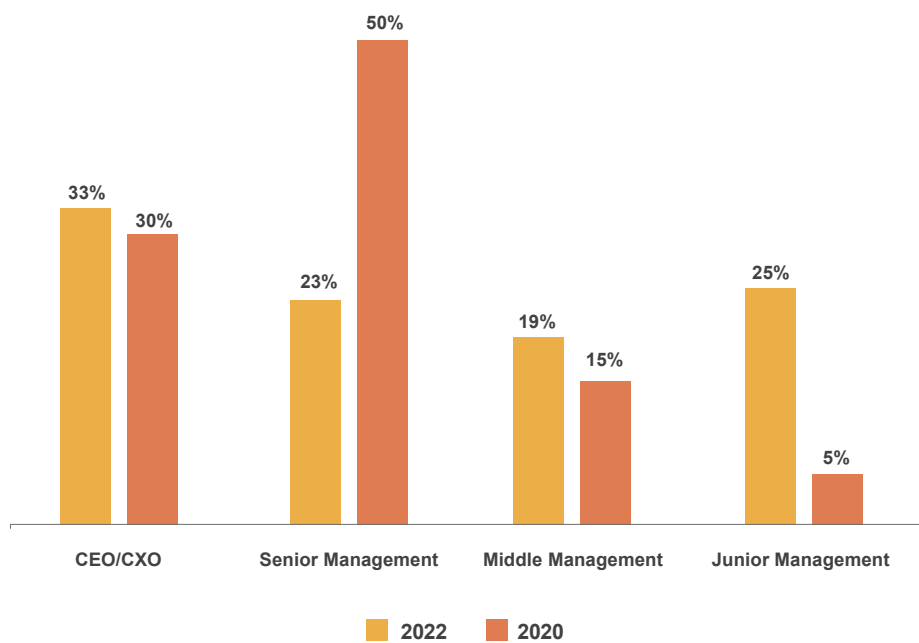


Methods used to decide how many options should be granted to an employee based on the anticipated value of benefits



Unlisted Companies in India prefer to allocate options either based on Fair Value of options (calculated using option pricing model) or Current FMV on the date of grant.

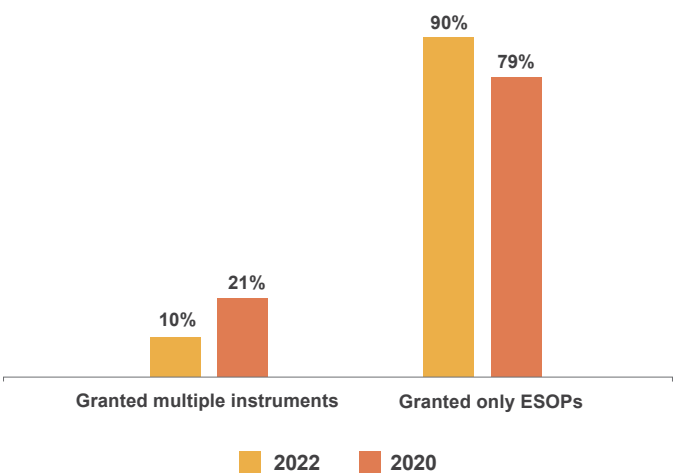
Employee wise mix of options granted (stock options, SARs, other instruments) as a % of total options granted



Over the last 2 years, the total allocation to CEO, CXO has decreased and Unlisted Companies are moving towards the trend of covering Junior employees as well.

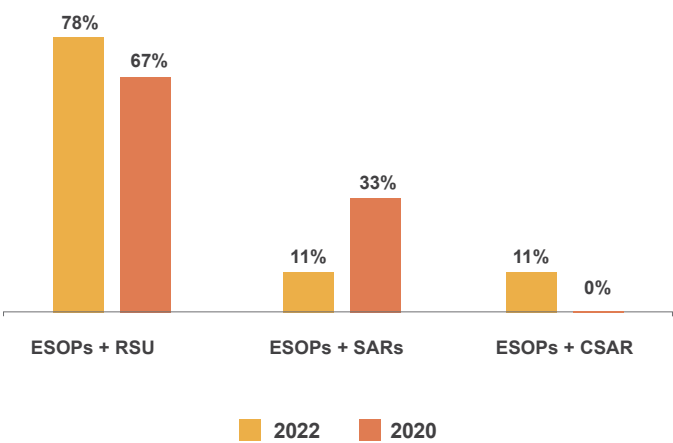
Instruments implemented viz: ESOPs, SARs, RSUs, Phantom, others?

90%(2020:79%) of the Companies have granted only ESOPs to their employees. 10% of the Companies have granted other instruments like RSUs (deep discounted ESOPs), stock appreciation rights and Phantom options along with ESOPs.



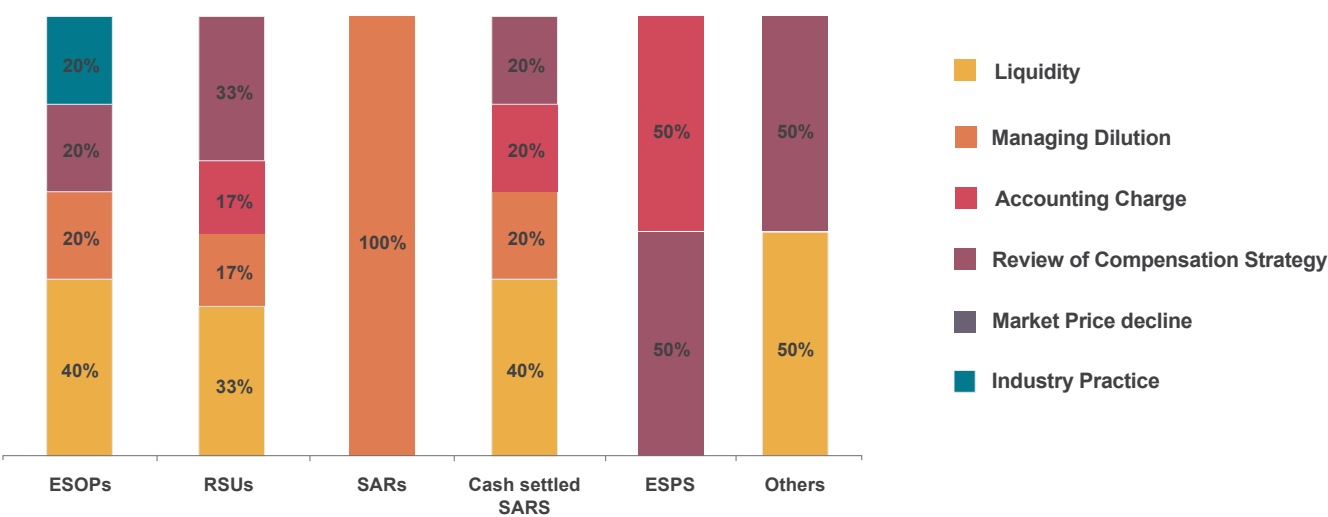
Granting ESOPs in combination with other instruments

We wanted to check which instruments are preferred along with ESOPs -



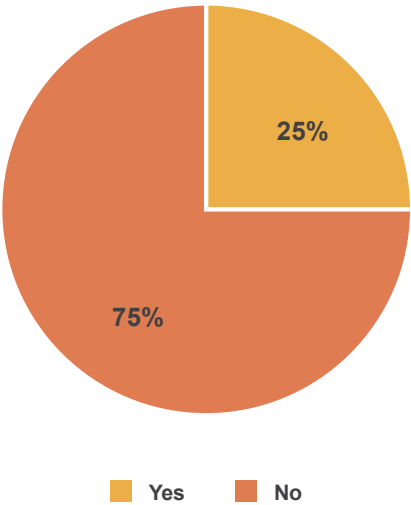
In earlier years, SARs along with ESOPs was the preferred instrument (2020:33%) however in 2022, this combination has be replaced with RSUs. 78% (2020:67%) and CSARs 11%(2020:0%). Companies granted RSUs along with ESOPs to their employees.

Further we asked Companies what were the drivers for implementing multiple instruments.



While ESOPs, RSUs, ESPS and Cash settled SARs have been chosen by Unlisted Companies in India to manage various drivers. Equity-settled SAR have been granted to manage dilution.

If Phantom/Cash settled SAR, is there a provision in the Scheme for capping the liability of cash outflow?

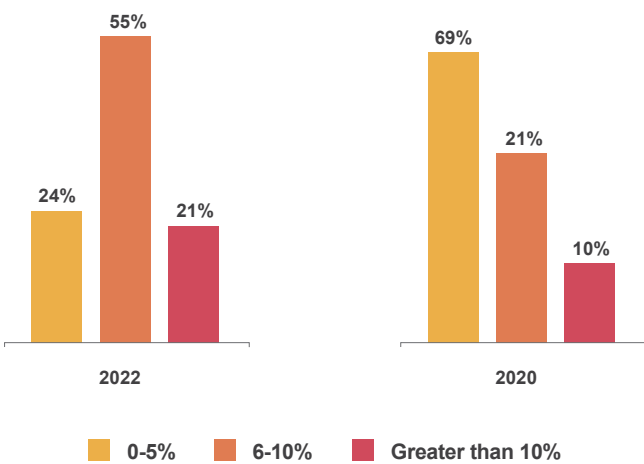


75% of the Unlisted Companies have not capped liability arising due to settlement of Phantom or Cash Settled Option, or capping is not applicable. Rest 25% of the Unlisted Companies prefer to put a cap on the settlement amount or cash outflow.

ESOP POOL

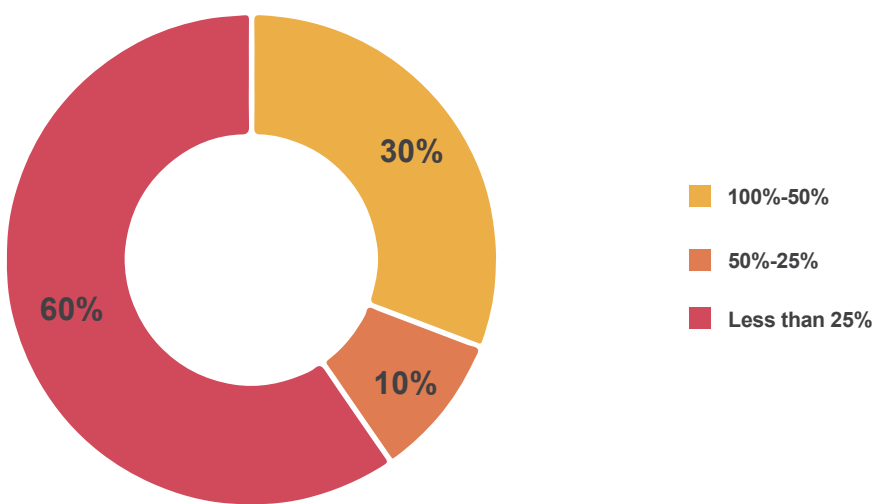
4.3

Percentage of total options (equity-settled) approved by the shareholders



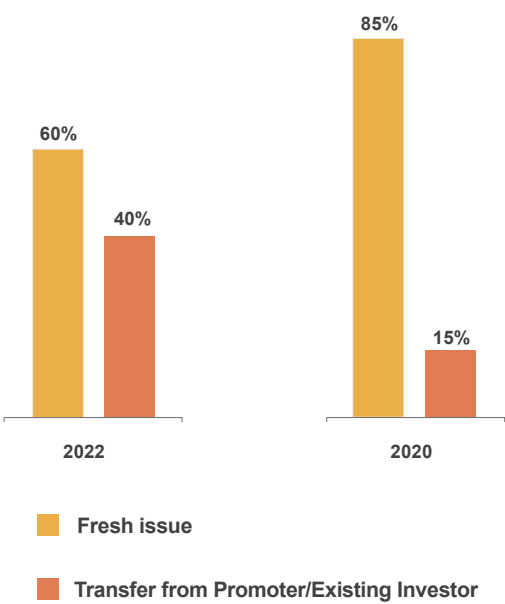
6%-10% of the ESOP Pool approved by shareholders in 55% of Unlisted Companies in India (2020:21%), and 21% of Companies have more than 10% of total Equity Share capital (2020:10%). This trend indicates that Unlisted Companies are increasing the component of Equity-based Compensation plans in employees’ pay mix and hence increasing pool size.

Percentage of ESOP pool utilized out of total pool approved



60% of the Unlisted Companies in India have utilized less than 25% of the pool approved by shareholders, keeping almost 75% of the pool in reserve for future grants and hires.

Source of Equity

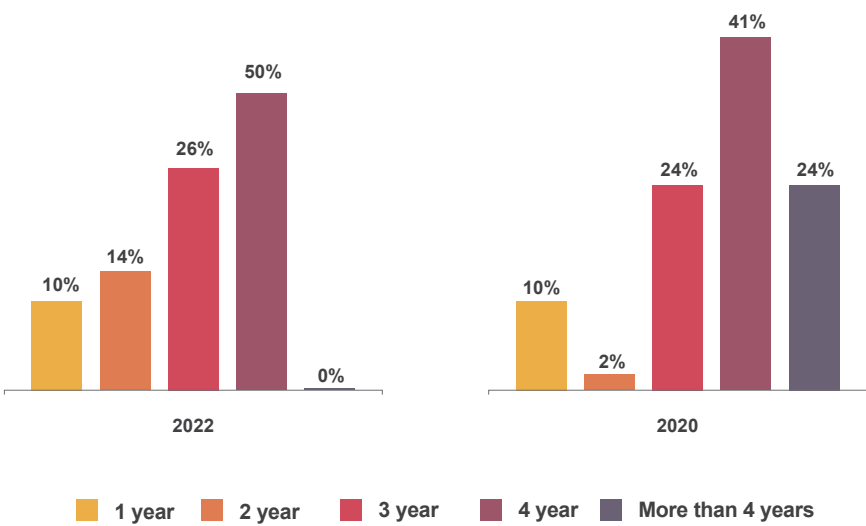


Preference for using secondary shares by transfer from Promoter or existing investors by Unlisted Companies in India is increasing (2020:40%, 2020:15%). There is a corresponding decrease in the number of Companies going for the fresh issue of shares for settlement of vested options exercised (2020:60%, 2020:85%).

VESTING

4.4

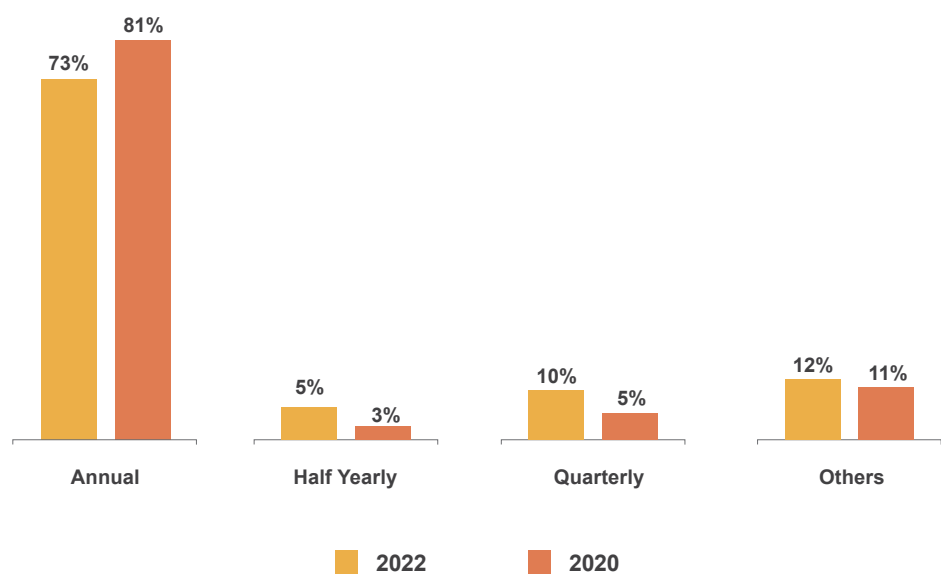
Vesting Period



76% of the Unlisted Companies in India have a vesting period of 3 to 4 years, with more companies preferring a 4 year vesting period (50%).

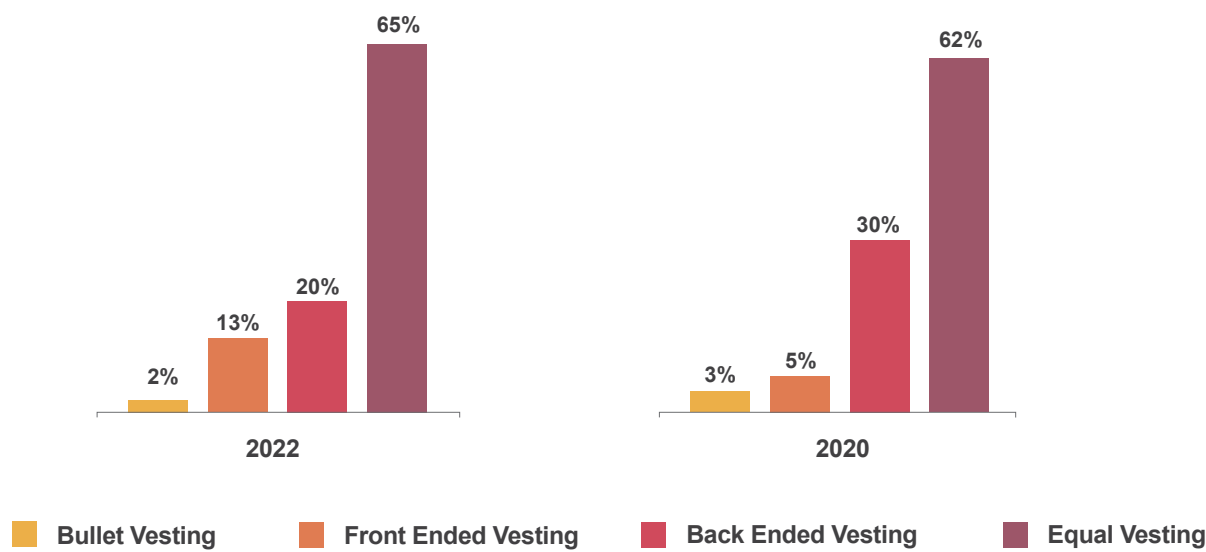
More Unlisted Companies are looking at longer vesting periods (4 years) to ensure longer retention.

Vesting Frequency



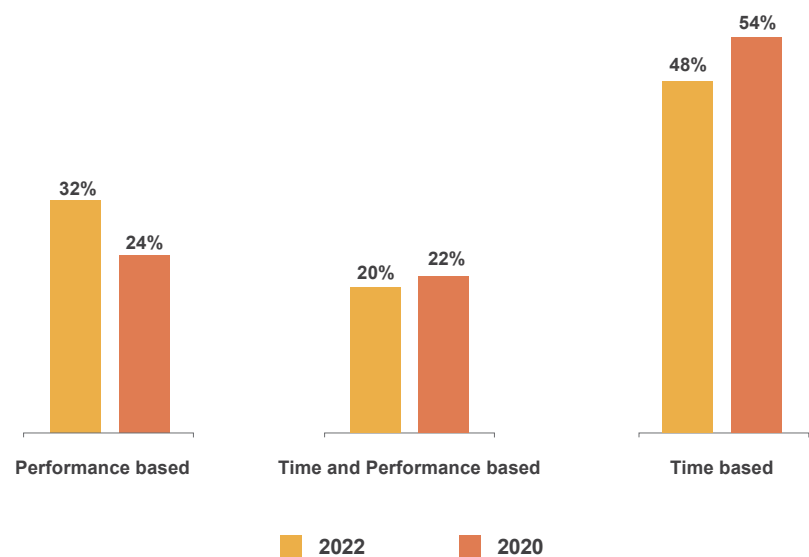
73% of Unlisted Companies in India continue to have annual vesting as compared to 81% in 2020. There is a shift in trend towards half-yearly and quarterly vesting schedules (2020:15%, 2020:8%).

Vesting Type



65% of Companies continue to prefer equated vesting. Also, there is an increase towards front-ended vesting by 13% of the Unlisted Companies in India.

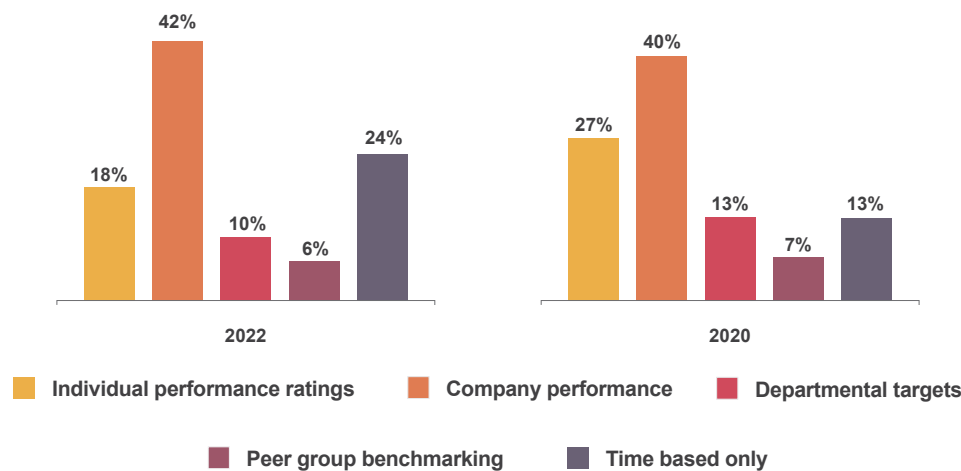
Time-based or performance-based vesting



As compared to our last Survey, Unlisted Companies in India seem to be moving towards granting performance-based options i.e., 32% in 2022 (2020:24%, 2017:19%). 48% of these companies are still considering Time based vesting.

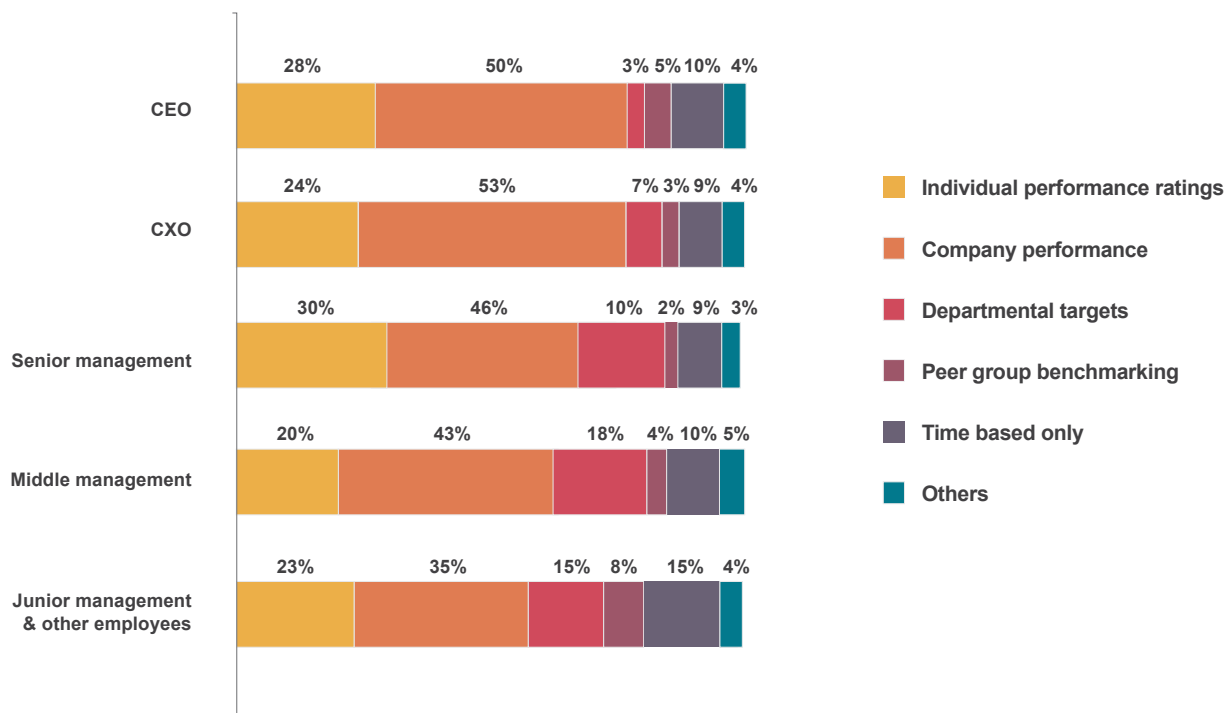
52% of the Companies have less than 50% weightage for performance-based conditions out of the above 20% of Companies which have a mix of Time and Performance as the vesting condition.

Types of performance-based vesting conditions



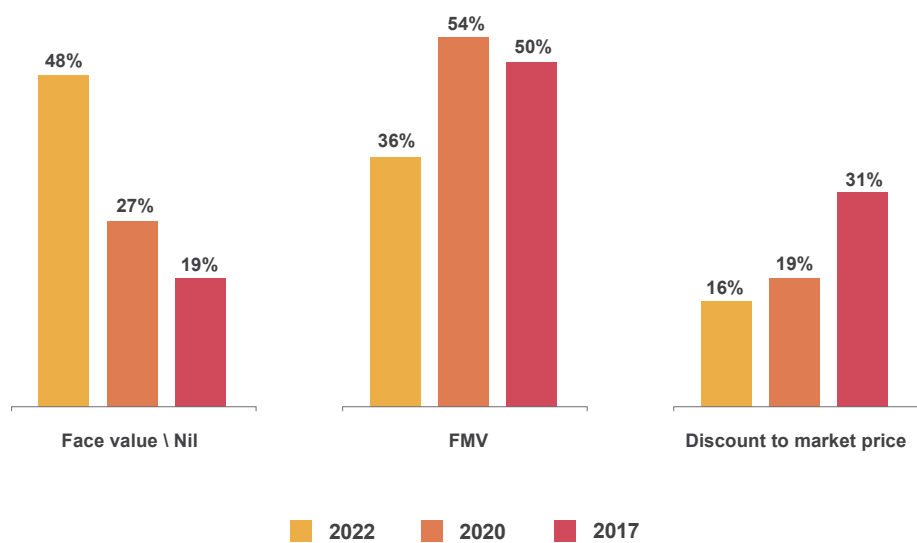
52% (2020:53%) Unlisted Companies in India have company performance and departmental targets as the vesting criteria. We have noticed a substantial decrease in Companies (2020:18%, 2020:27%) having individual performance as a vesting criterion. Also, there is an increase in the number of Companies which prefers vesting to be on continued service only, without any further conditions (2022:24%, 2020:13%).

We further analyzed; designation wise various performance conditions preferred as vesting by Unlisted Companies in India

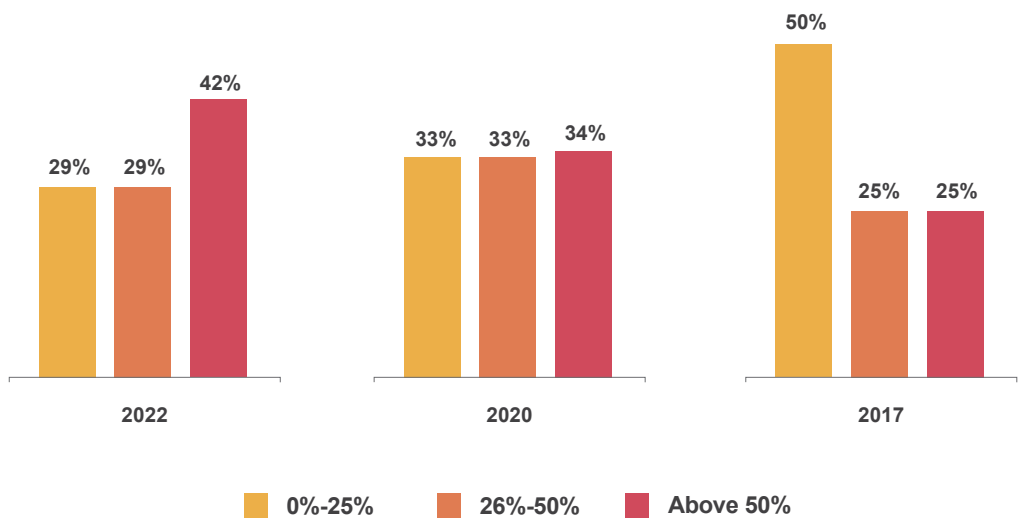


EXERCISE PRICE

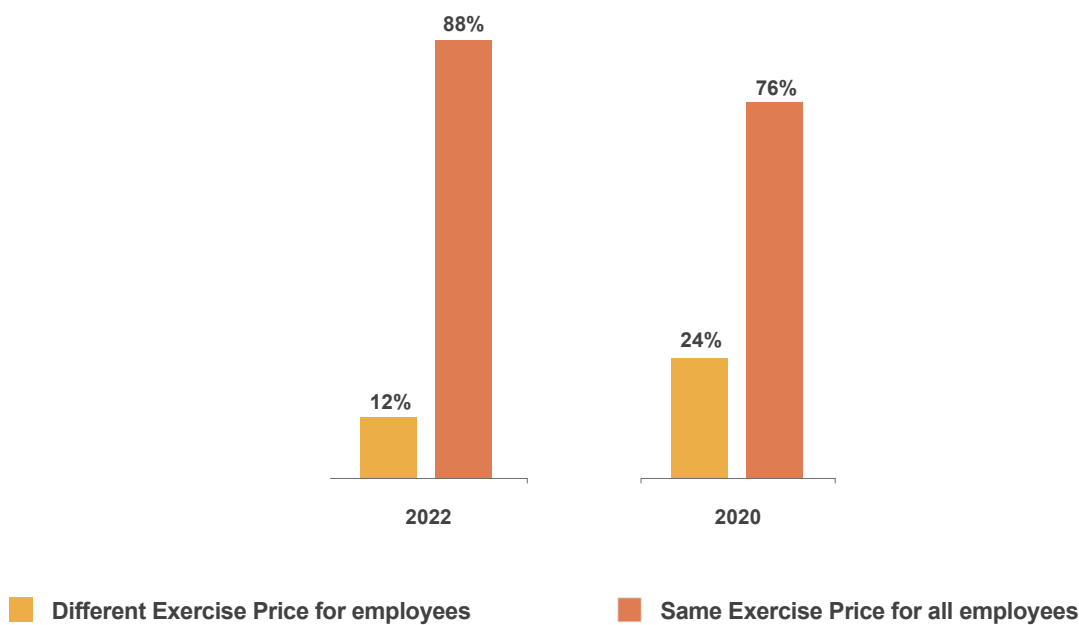
4.5



Grant at FMV on the date has been the most preferred exercise price in the past, but we observe that face value grants gained more weightage over the years, i.e. 48% in 2022 (2020:27%; 2017:19%) as compared to previous years.



42% of the Unlisted Companies in India grant options at a discount of more than 50% to the FMV/Market price, which is in line with the above observation of grants at Face value.

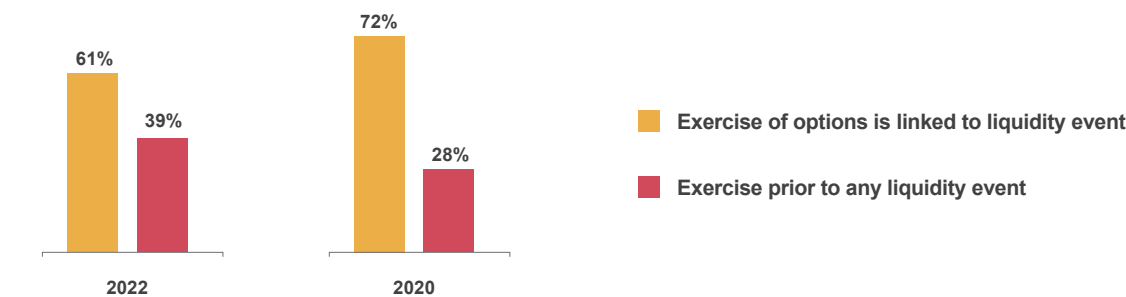


Maximum Unlisted Companies in India (2020:88%, 2020:76%), do not have different prices for a different set of employees as compared to 12% (2020:24%) who have different exercise prices for various employees.

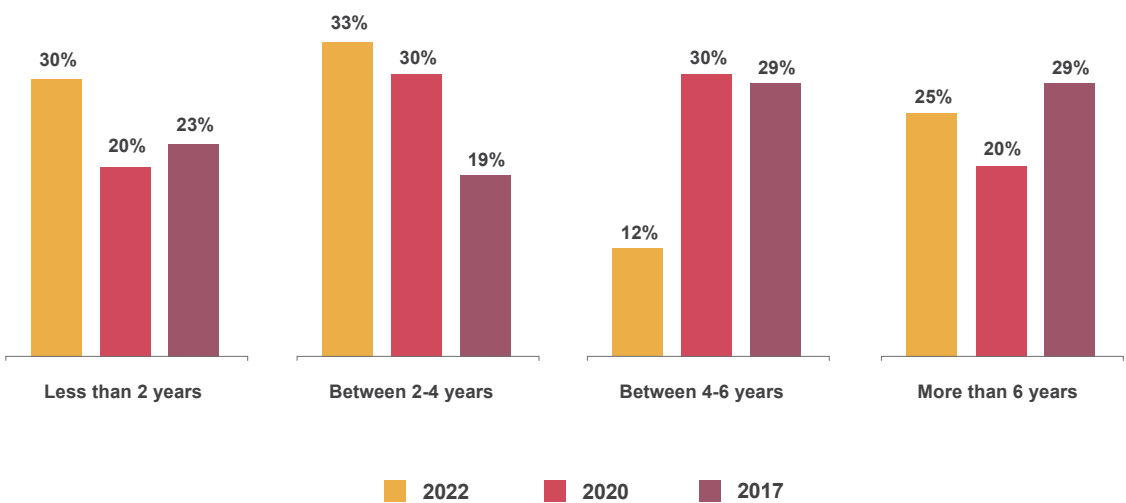
EXERCISE PERIOD

4.6

Whether exercising of options is linked to liquidity?



Even though 61% of Unlisted Companies in India have linked their exercise to a liquidity event (2020:72%, 2015:43%), there is a significant reduction in the number of Companies going for linked to liquidity exercise, instead 39% have other arrangements to provide a definitive exercise period to employees.

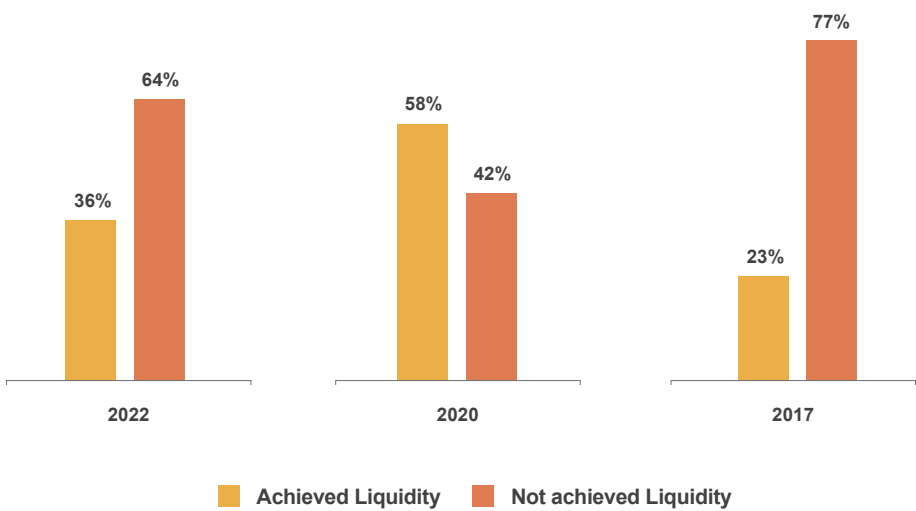


In 2022, only 63% of the Unlisted Companies in India had an exercise period of less than 4 years. It implies maximum number of Unlisted Companies in India are providing an opportunity to exercise within 4 years from the date of vesting of options. We can also notice that the exercise period has reduced over the years by Unlisted Companies; only 37% have more than 4 years of exercise period (2020:50%, 2017:58%)

UNLISTED CHALLENGES

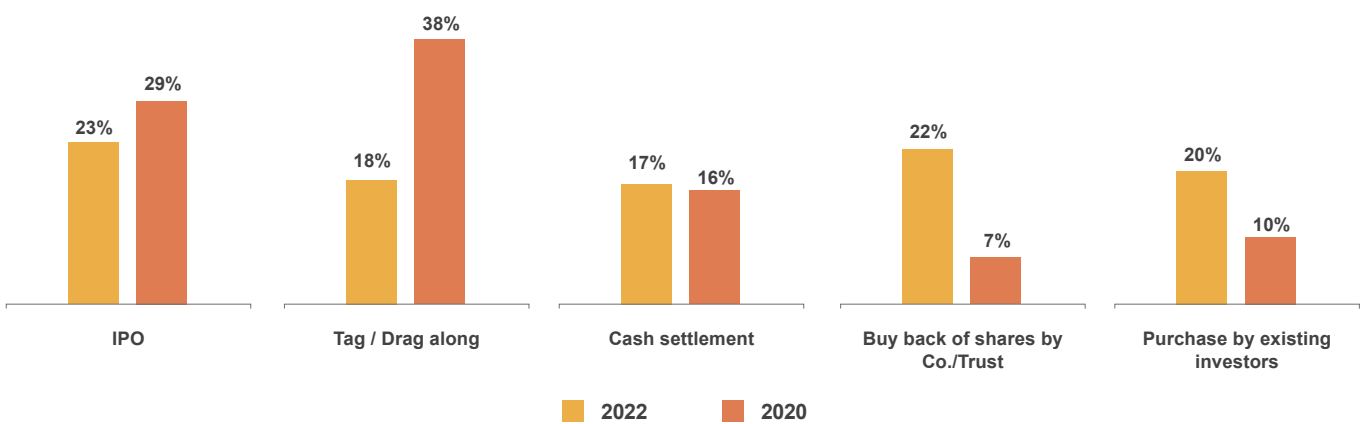
4.7

Whether Companies were able to achieve liquidity?



We see Unlisted Companies in India able to achieve liquidity in 2022 got reduced to 36% as compared to 2020 (58%). This could be the reason for more Unlisted companies moving to fixed exercise period.

How did Companies plan exit route for their Equity based schemes?

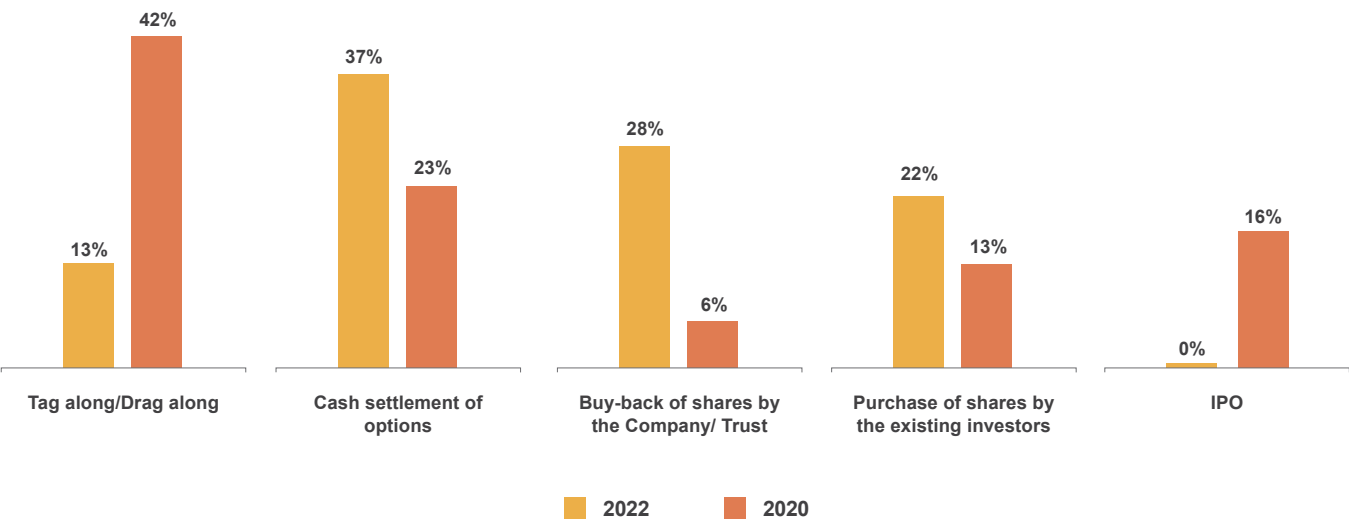


Providing liquidity alternatives for ESOPs of Unlisted Companies is a major challenge. However, Companies provide alternatives in the Plan document.

23% of Companies provide IPO as one of the liquidity alternatives. In 2022 more Companies (42%) have committed buyback of shares by Trust or offer for sale by Promoters/ exiting Investors as a liquidity event, and fewer Companies (18%) have included Tag along /Drag along clauses in their Plan document.

We further asked Companies how they provided liquidity to their employees.

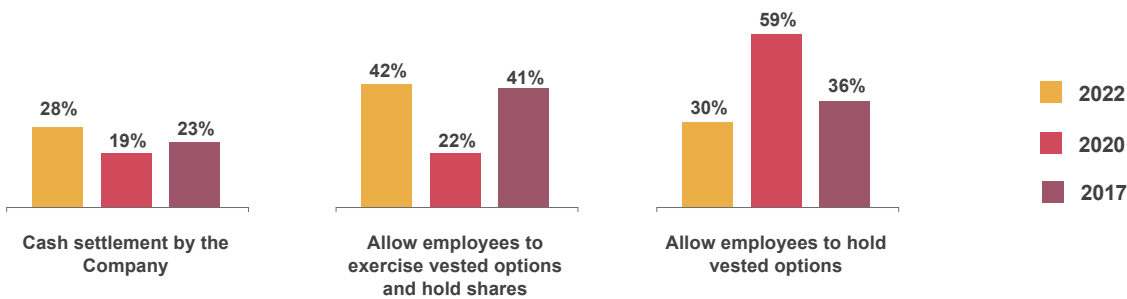
How did Companies achieve an exit route for providing liquidity?



Out of the companies that achieved liquidity apart from IPO, around 37% (2020:28%) of the Companies settled options by cash payout. We noticed a significant increase in Companies achieving liquidity through Buy back of shares (2022:28%,2020:6%) and purchase by existing Investors as compared to previous years (2020:13%).

Also, providing liquidity in strategic sale events through Tag / Drag along has reduced to 13% in the year 2022 as compared to 42% in 2020.

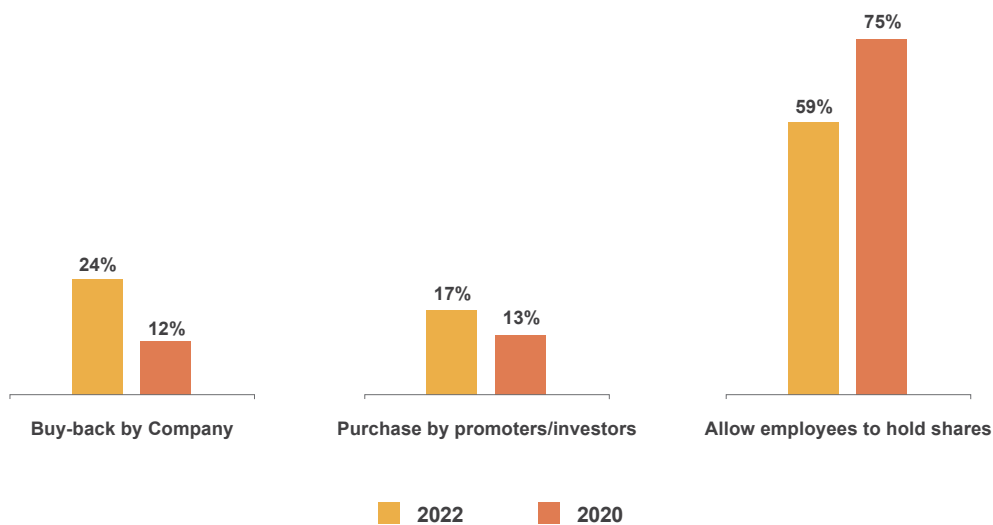
If exercise is linked to a liquidity event, then how are vested options dealt with upon separation?



On separation of employees, 42% of Unlisted Companies in India are dealing with vesting options by allowing them to exercise those options and convert them into shares, compared to only 22% in 2020.

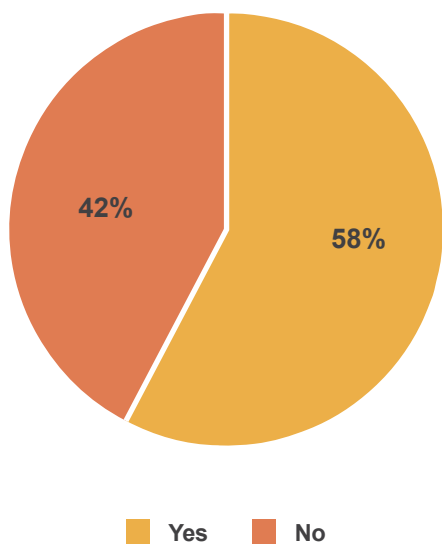
30% of these companies allow separated employees to hold the vested options until a liquidity event, and 28% offer cash settlement of vested options at prevailing FMV or discounted FMV (2020:19%).

If the Scheme allows exercise, then how are these shares dealt with at the time of separation?



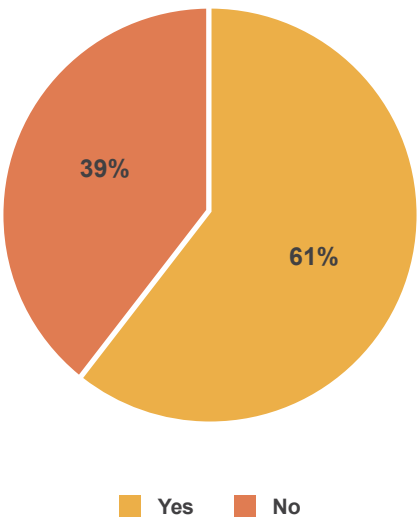
59% (2020:75%, 2017:87%) of Companies allow the exercise of options and holding of shares even on separation, irrespective of any liquidity event, whereas 41% of Companies arrange for a buyback of these shares or purchase by Promoters or Investors.

Does the Scheme require mandatory accelerated vesting of options on happening of liquidity events?



Most of the Unlisted Companies in India (2022:58%) have provision for acceleration of vesting of unvested options, on happening of any liquidity event, including IPO. Remaining 42% of Companies do not have such a provision.

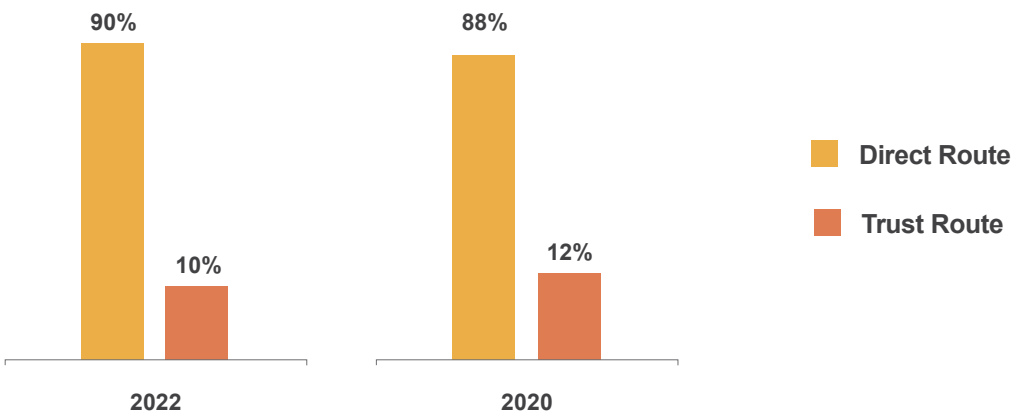
Are separated employees entitled to the same benefits as existing employees for their vested options?



61% of the Unlisted Companies in India are providing the same benefits to even separated employees as the existing employees in case of a liquidity event.

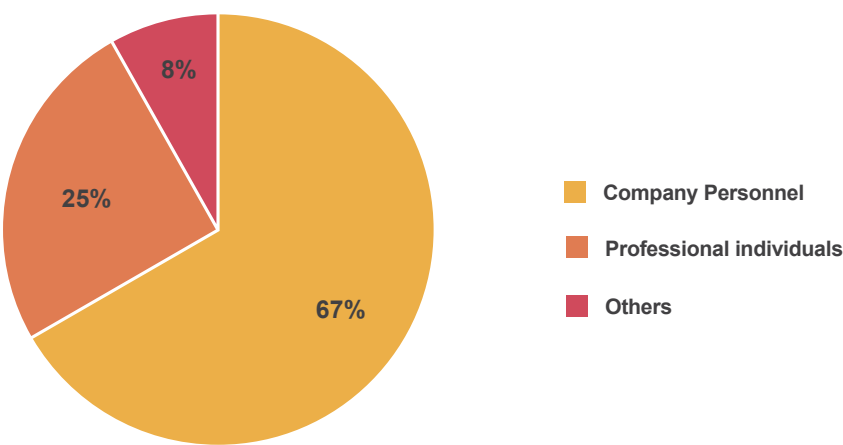
GENERAL TRENDS4.8

Route for implementing ESOPs



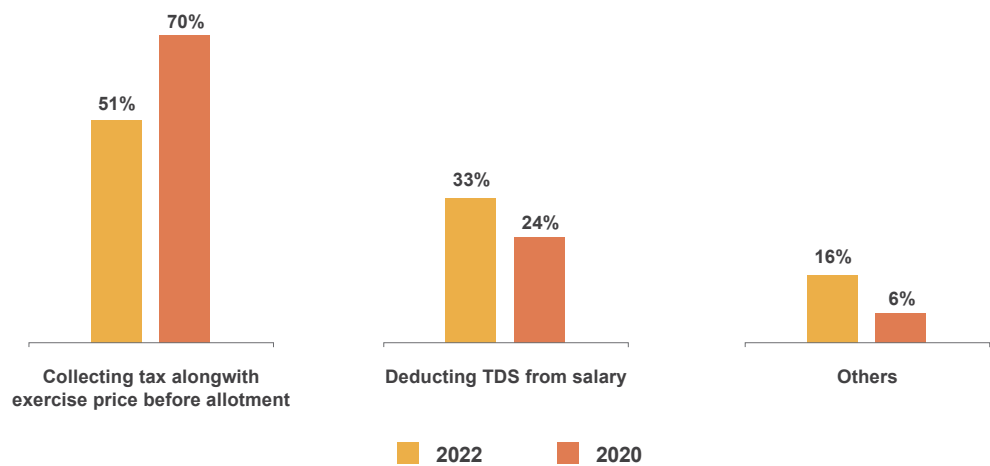
Direct Route remains the preferred mode of implementing ESOPs by 90% of the Unlisted Companies in India.

Constitution of Trustees



Only 25% of Unlisted Companies in India have appointed a professional individual as their trustees in 2022 for ESOP Trusts. 67% of the Companies appointing Company’s Personnel as their Trustees, and the rest 8% have other arrangements.

How does the Company recover perquisite tax from the employees?



Most of the Unlisted Companies in India are collecting tax with exercise price (2020:51%) but the weightage has shifted towards Companies deducting TDS from the salary of employees has increased to 33% in 2022 as compared to 24% in 2020.

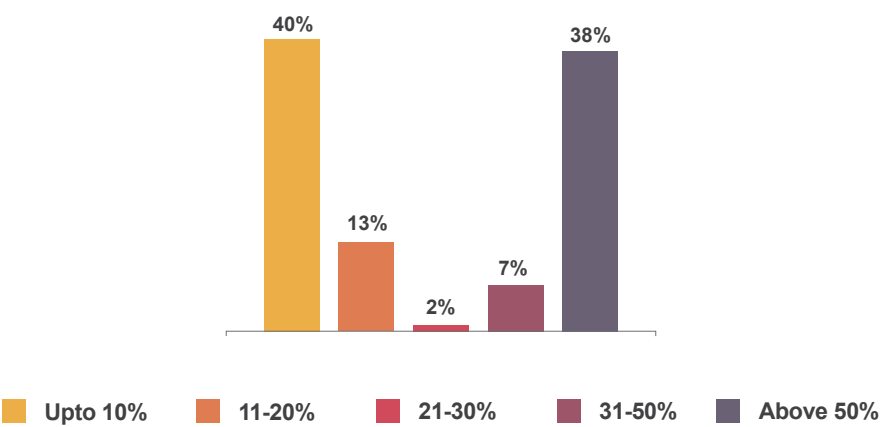


DESIGN TRENDS – UNLISTED COMPANIES IN SOUTH EAST ASIA (SEA)

COVERAGE

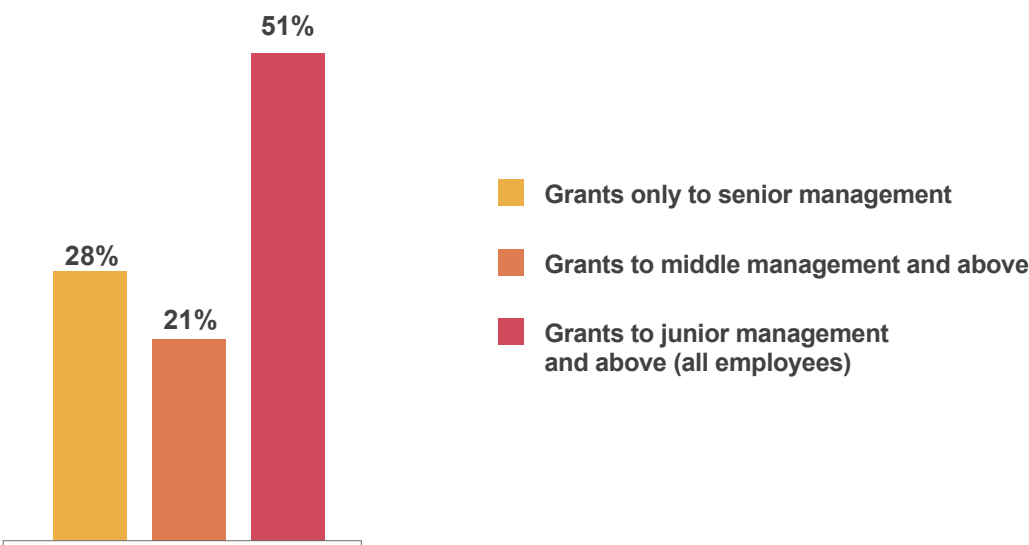
5.1

Employees covered under an Equity Compensation Plan



Unlisted Companies in SEA are also in line with the trend of covering up to 10% of total employee strength. 40% of Companies have selected up to 10% of employees for an Equity Compensation plan, while 13% prefer to cover up to 20% of the employees. 38% of Unlisted Companies in SEA have a broad-based plan covering more than 50% of the employees.

Mix of grant of options to senior/middle/junior management level of management

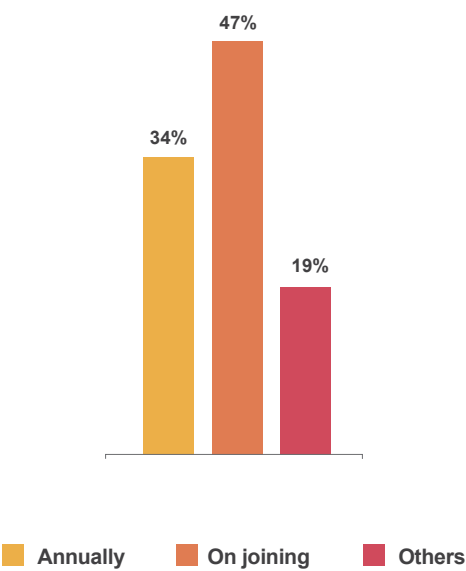


GRANT PRACTICES

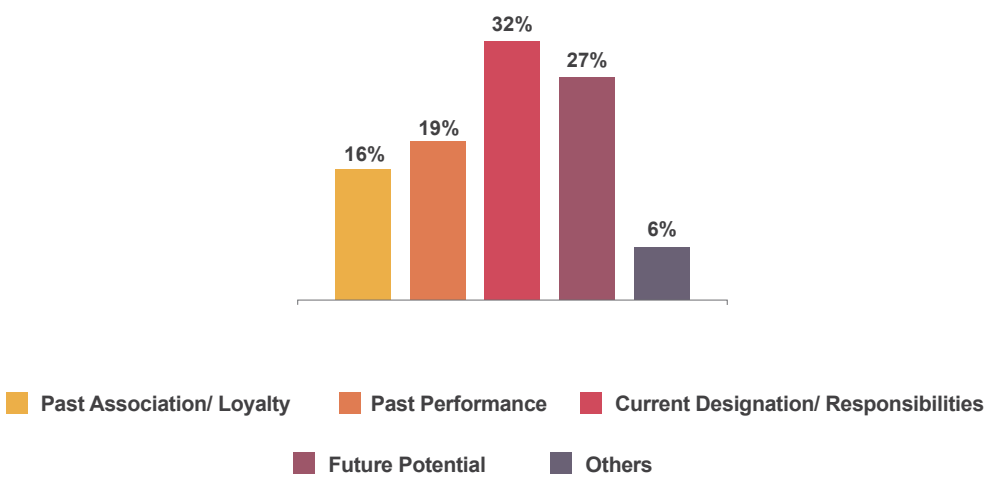
5.2

Frequency of Grants

Maximum Unlisted Companies in SEA prefer to grant options on Joining (47%), 34% grant at annual frequency, while 19% do not have a definitive frequency.



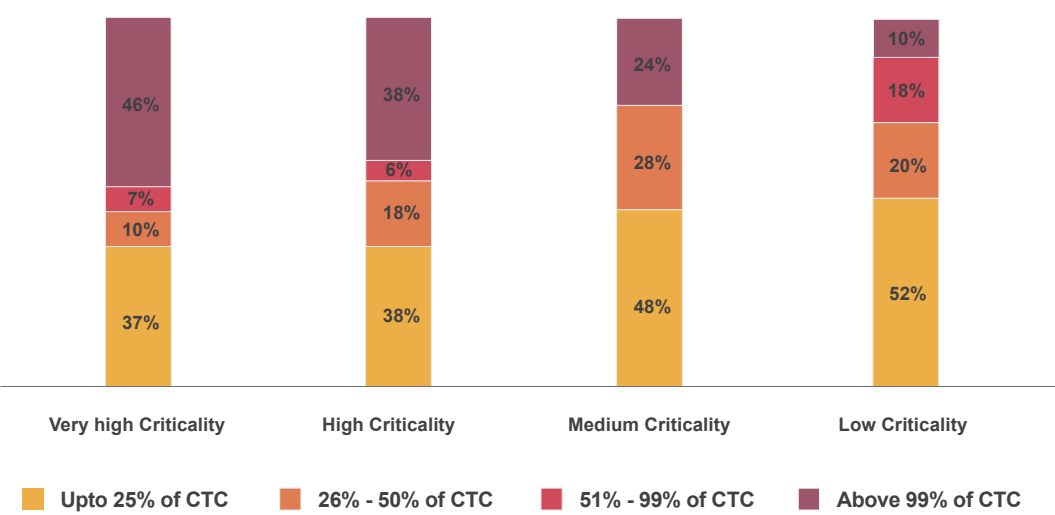
Parameters for selection of employees for Equity Compensation



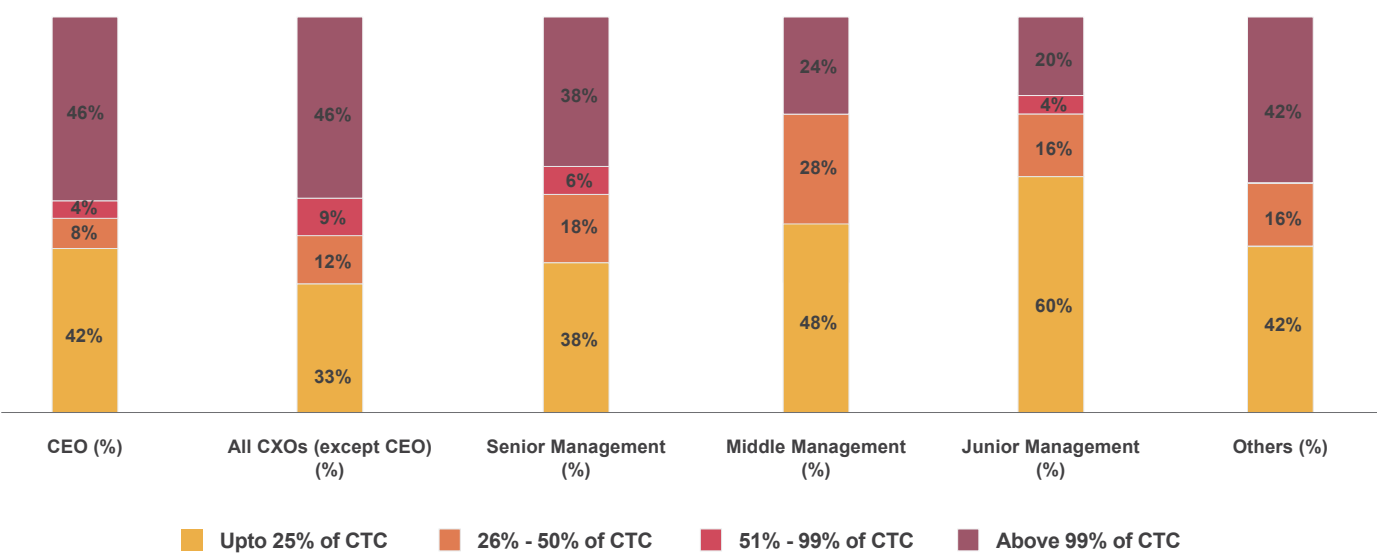
Current role appears to be a single dominant parameter for the selection of employees as 32% of Unlisted Companies in SEA. Future potential is the next prominent factor for selection, preferred by 27% of Companies.

Estimated benefit sought to be passed by way of Equity compensation as per annum benefit

The quantum of benefit passed by way of Equity compensation is one of the key decision points. Most used and easily understood measure for this is what percentage of the annualized CTC should the employee be expected to make from his Equity compensation grants?



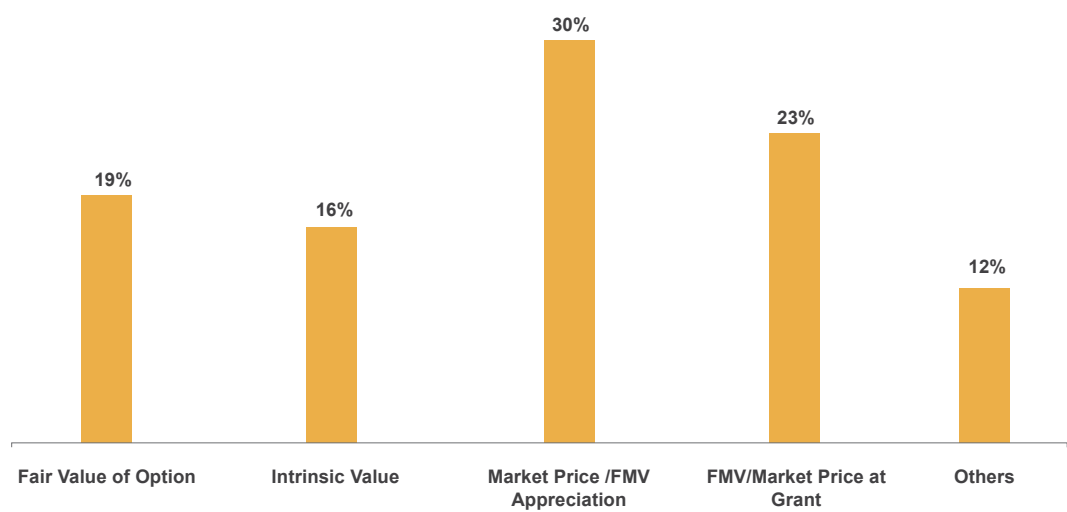
Estimated benefits offered as per the designations



Estimated benefits offered to the employees are based on the relative criticality of employees in the organization.

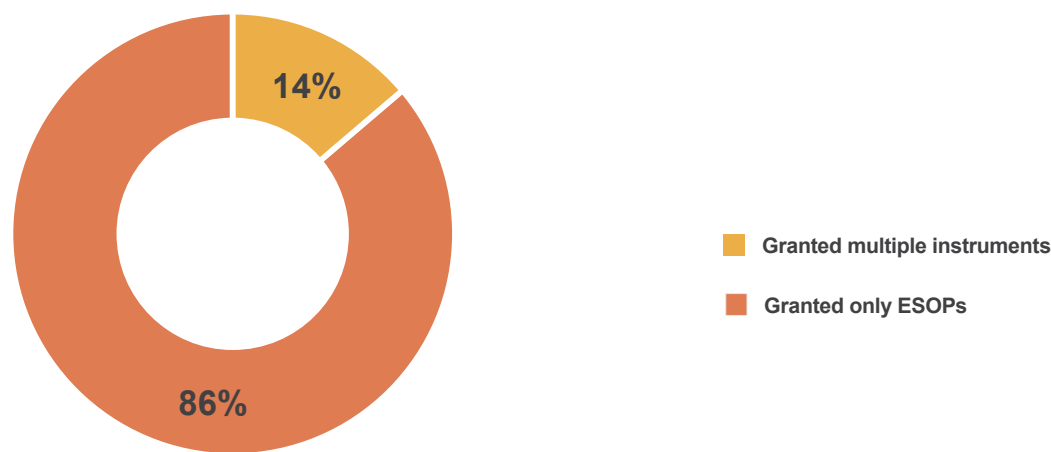
46% of Unlisted Companies in SEA tend to give more benefit (more than 99% of CTC per annum) to their highly critical employees, including CEOs and other CXOs, and 52% of Companies provide up to 25% per annum to the least critical employees.

Which of these methods is used to decide how many options should be granted to an employee based on the anticipated value of benefits?



Unlisted Companies in SEA prefer to allocate options either based on future appreciation (2022:30%) in FMV or Current FMV (2022:23%)

Multiple Instruments implemented?



86% of the Unlisted Companies in SEA have granted only ESOPs to their employees, while 14% of the Companies have granted other instruments along with ESOPs.

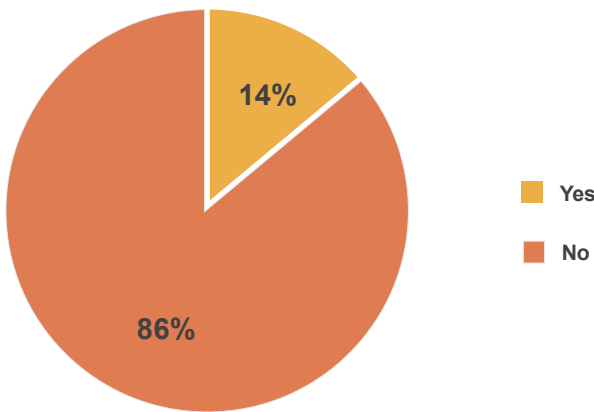
Further we asked Companies what were the drivers for implementing multiple instruments.



While ESOPs have been chosen by Unlisted Companies in SEA, to manage various drivers, RSUs, ESPS, and Cash settled SAR have been granted with a view of managing Liquidity only.

If Phantom/Cash settled SAR, is there a provision in the Scheme for capping the liability of cash outflow

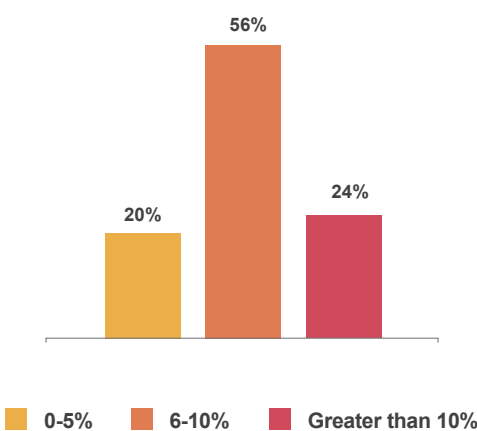
Around 86% of the Unlisted Companies in SEA have not capped liability arising due to settlement of Phantom or Cash settled option, 14% of the Companies prefer to put a cap on the settlement amount.



ESOP POOL

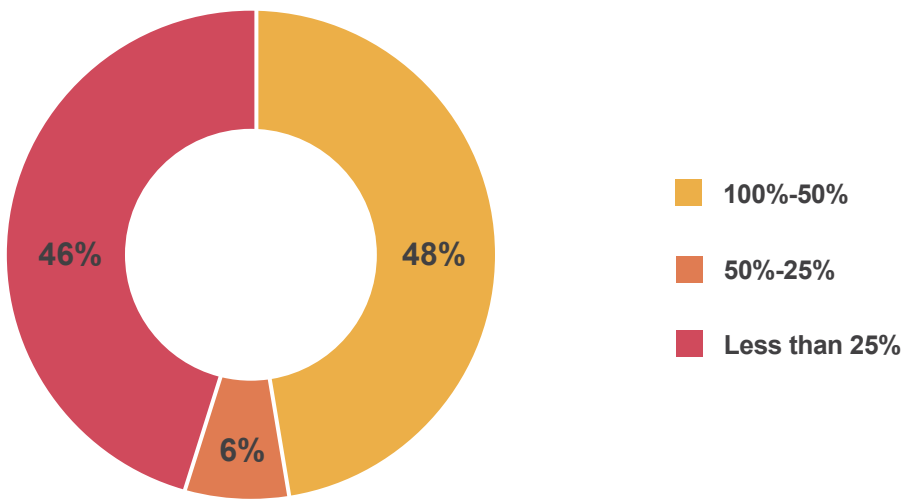
5.3

Percentage of total options (equity-settled) approved by the shareholders



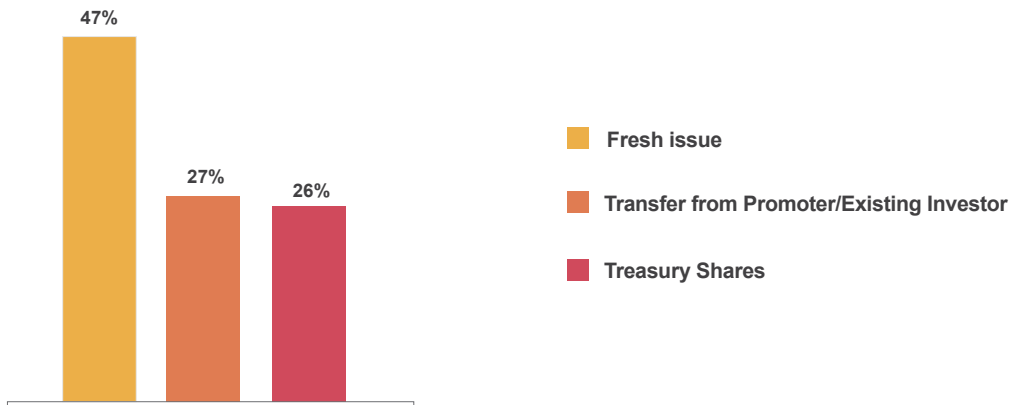
6%-10% of ESOP Pool approved by shareholders in 56% of Unlisted Companies in SEA, and only 24% of Companies have more than 10% of total Equity Share capital.

Percentage of total options pool has been utilized out of pool approved



46% of Unlisted Companies have utilized between 50%- 100% of the ESOP pool approved, and 48% of Unlisted Companies have utilized only less than 25% of the ESOP pool.

Source of Equity

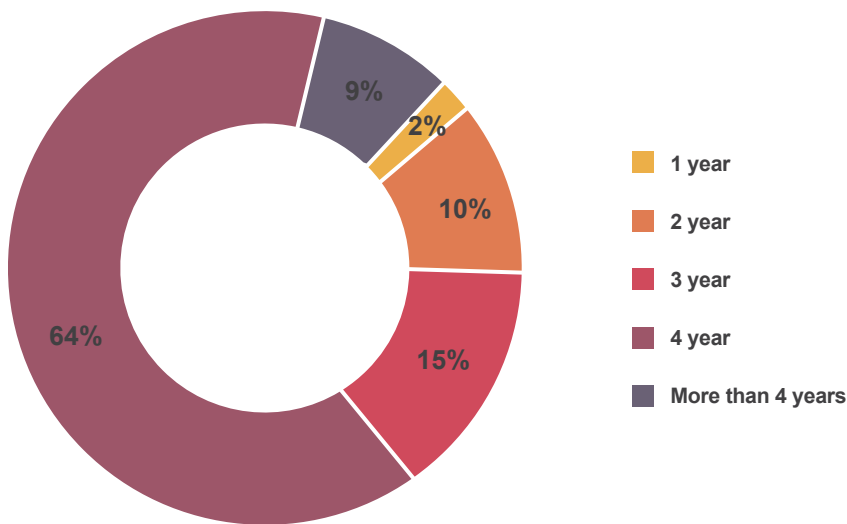


47% of Unlisted Companies in SEA issue fresh equity to settle outstanding options, followed by 27% of Transfer from Promoters and 26% Treasury Shares.

VESTING

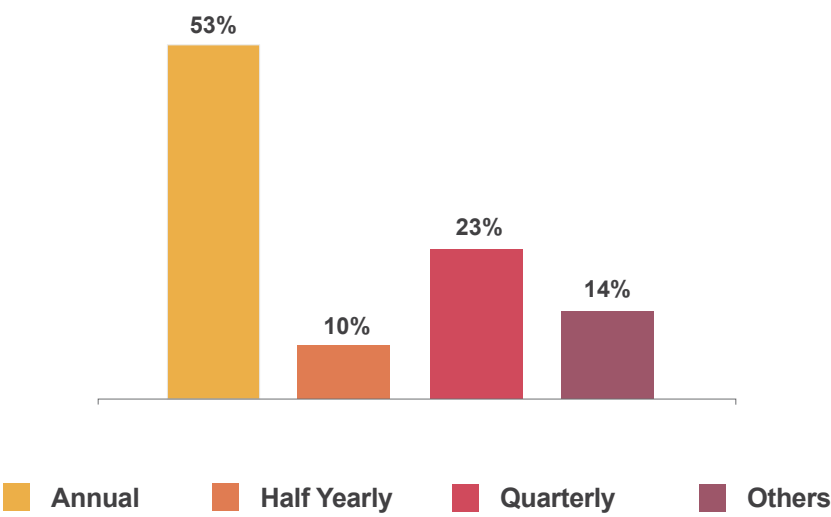
5.4

Vesting Period



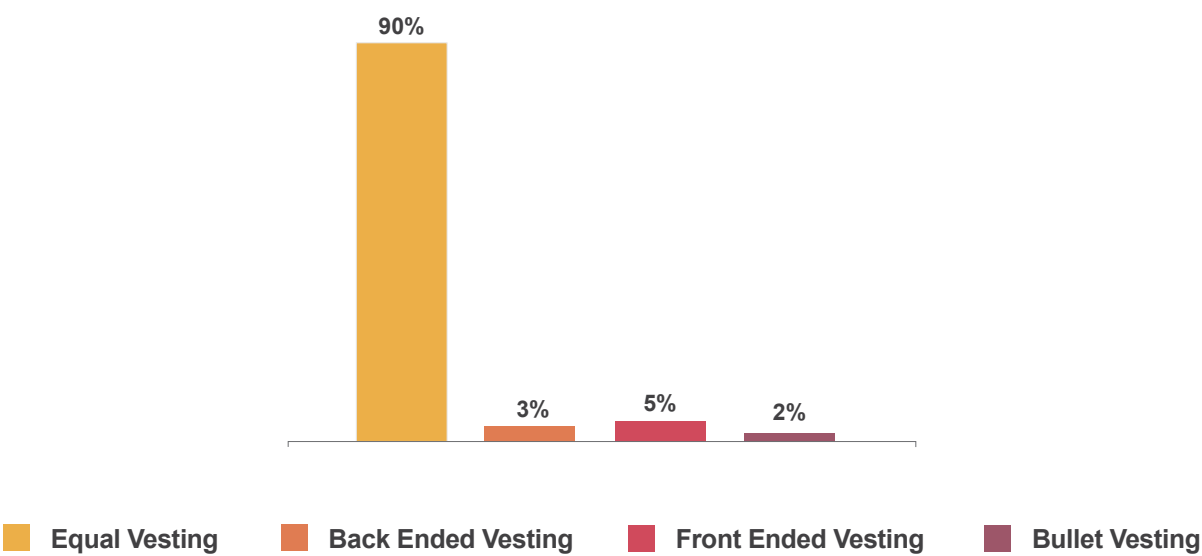
79% of the Unlisted Companies have a vesting period of 3 or 4 years, with the majority of Companies preferring a 4 year vesting period (64%).

Vesting Frequency



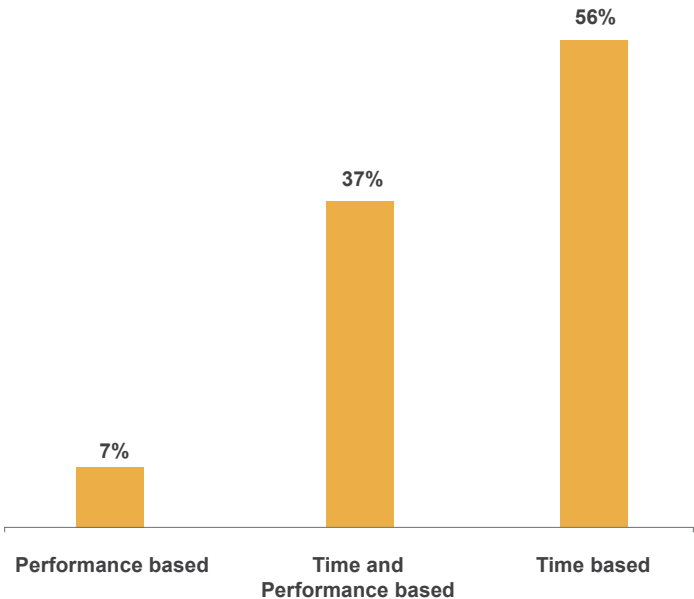
53% of Unlisted Companies in SEA have annual vesting, and 23% prefer to keep a Quarterly vesting schedule.

Vesting Type



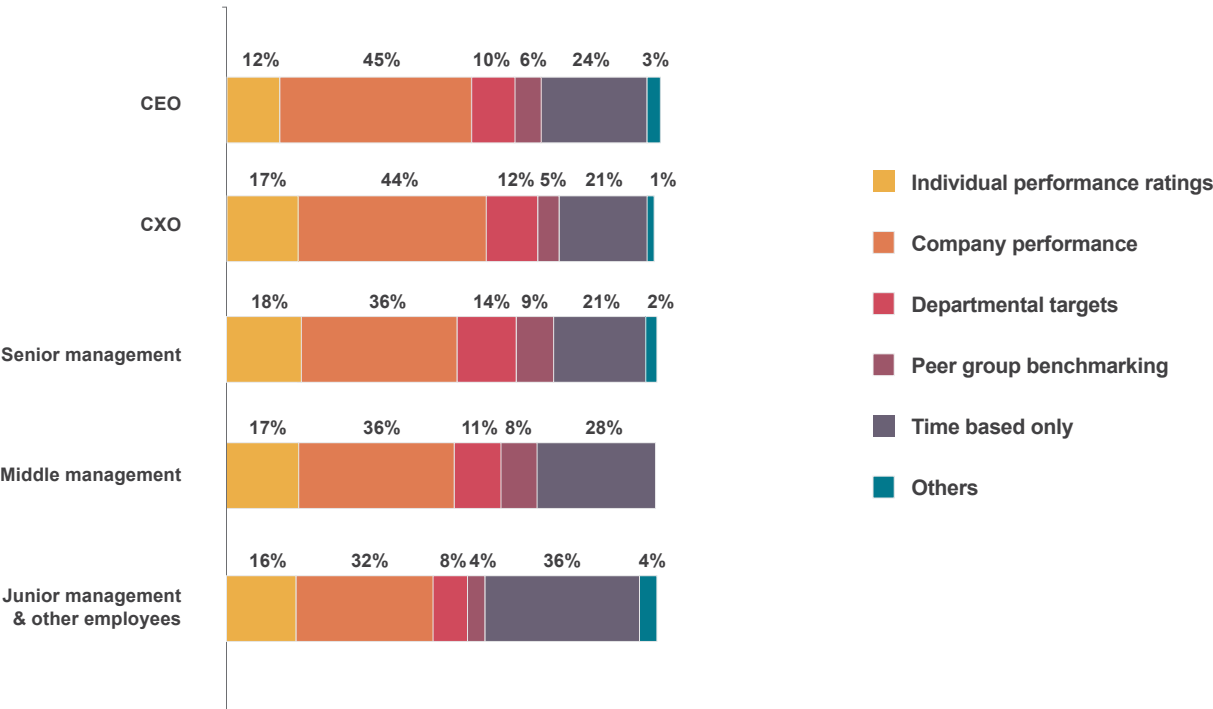
90% of Unlisted Companies in SEA prefer equated vesting over other vesting schedules.

Time-based or performance-based vesting



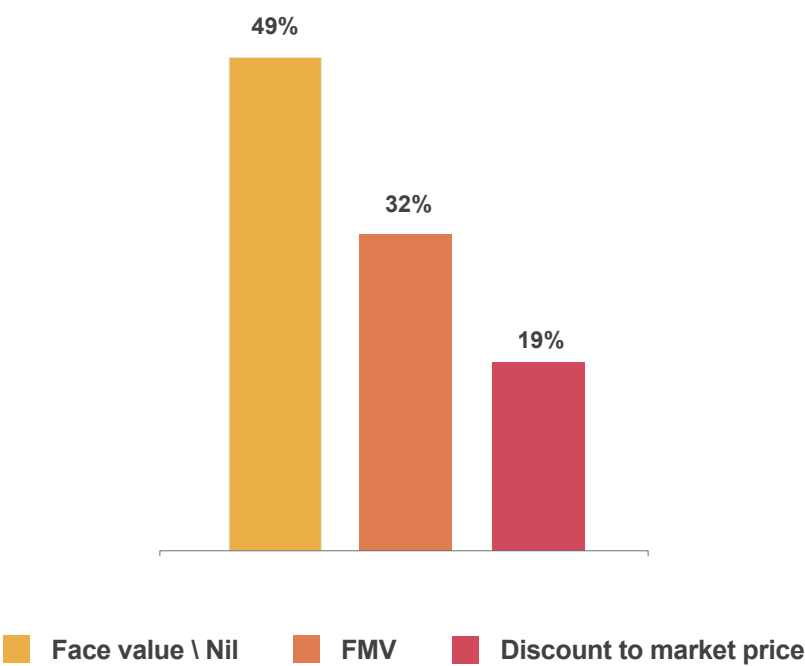
56% of Unlisted Companies in SEA are not having any performance conditions for the vesting of Options and they like to give benefits for the continued service of an employee. 37% of the Companies have a mix of time and performance conditions for vesting.

We further analyzed; designation wise various performance conditions preferred for vesting by Unlisted companies in SEA

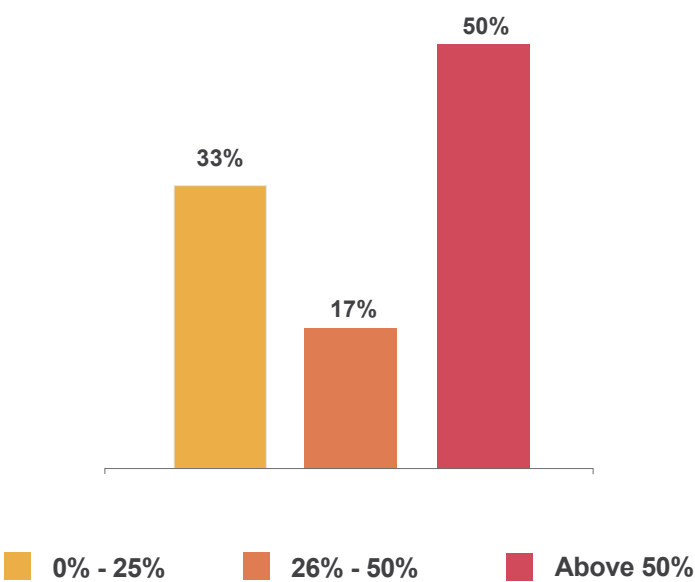


EXERCISE PRICE

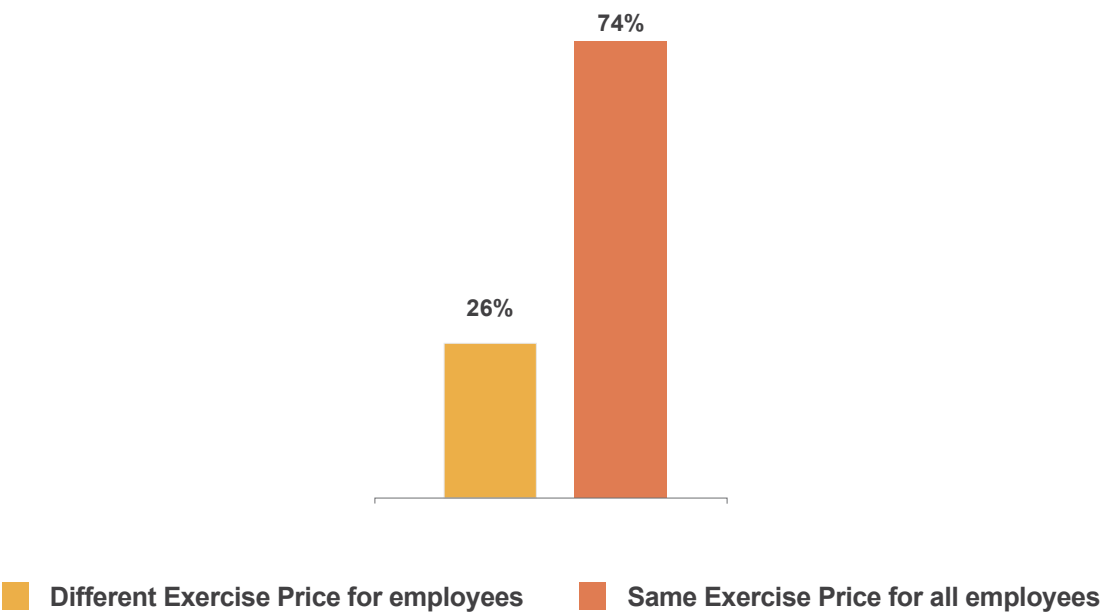
5.5



RSUs with Face value Grants or Nil exercise price is the most preferred Exercise price by Unlisted Companies in SEA. 32% of Companies also prefer to do FMV / Market price grants, and only 19% grant at discounted FMV/ Market Price.



Almost half of the Unlisted Companies in SEA, grant options at a discount of more than 50% to the FMV/Market price. This trend is in line with the above observation of grants at Face value / Nil exercise price.

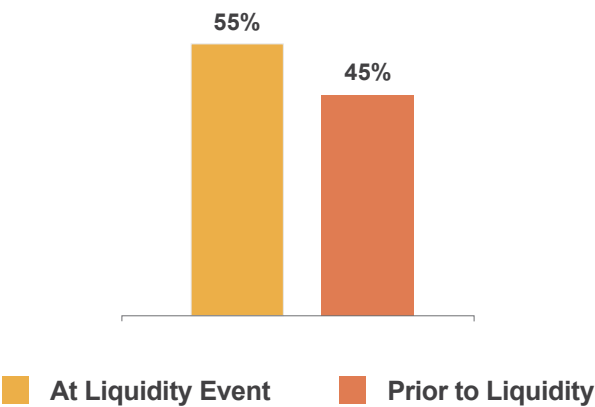


74% of the Unlisted Companies in SEA do not have different prices for a different set of employees as compared to 26% who have different exercise prices for various employees.

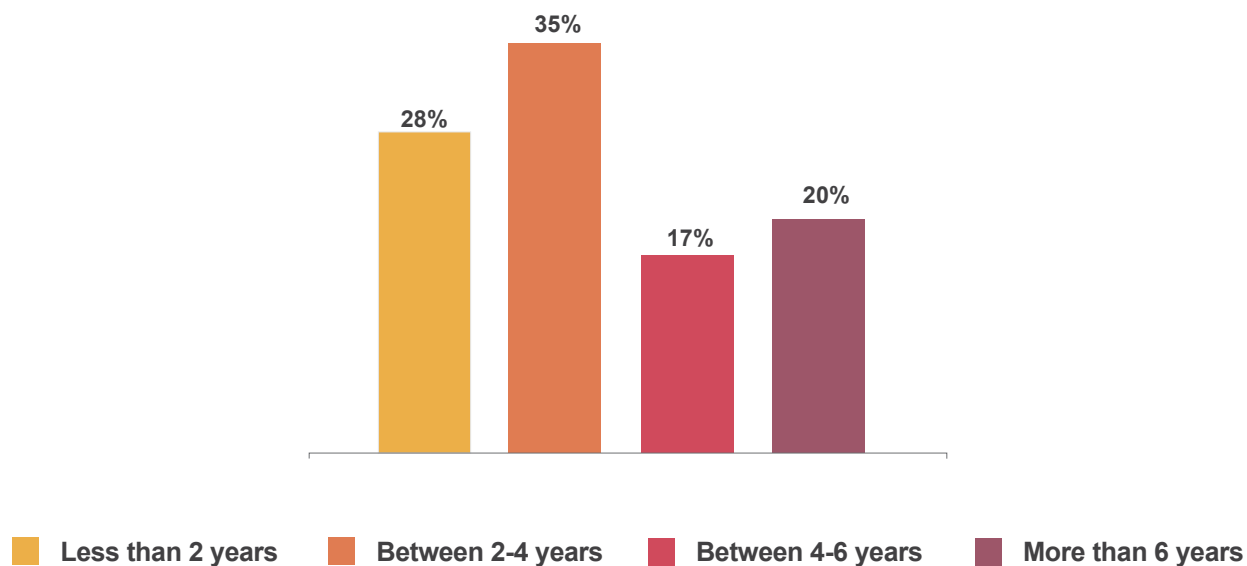
EXERCISE PERIOD

5.6

Whether exercising of options is linked to liquidity?



Almost 55% of Unlisted Companies in SEA are linking the exercising of their options with liquidity events. Still, also 45% are providing exercise of options at fixed period post vesting and prior to any liquidity event.

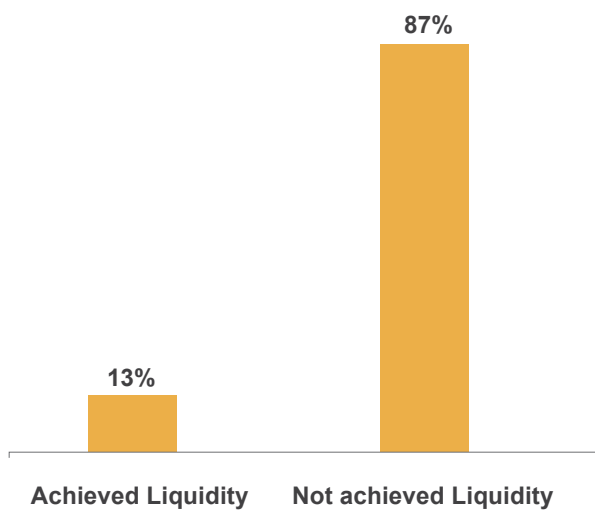


63% of the Unlisted Companies in SEA have an exercise period of less than 4 years. Only 37% of Unlisted Companies in SEA have opted for an exercise period of more than 4 years.

UNLISTED CHALLENGES

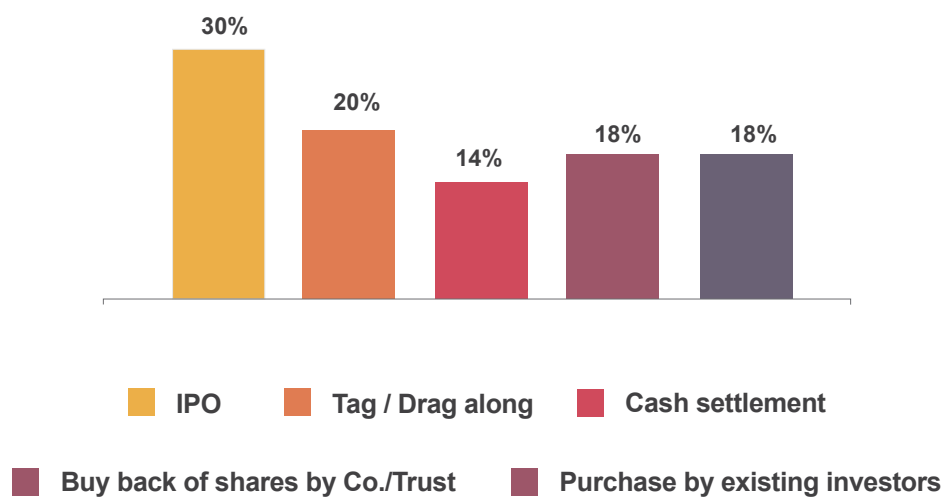
5.7

Whether exercising of options is linked to liquidity?



We see very marginal % of Unlisted Companies in SEA are able to achieve liquidity for options granted to employees.

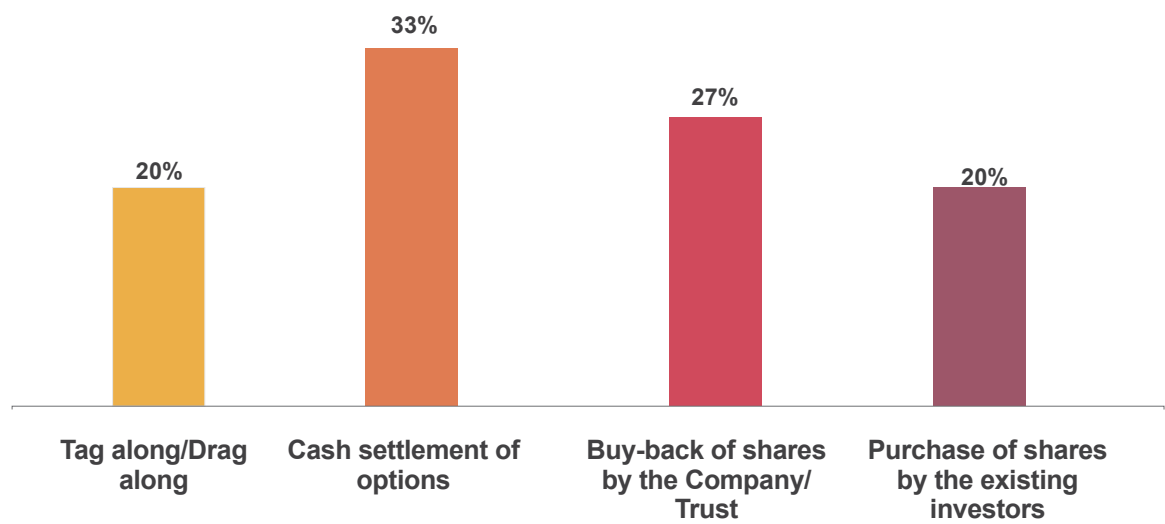
How did Companies plan exit routes for their Equity based schemes?



Providing liquidity alternatives for ESOPs of Unlisted Companies is a major challenge. However, Companies provide alternatives in the Plan document.

30% of Unlisted Companies in SEA, provide IPO as one of the liquidity alternatives. Only 18% of companies are committing buyback of shares as a liquidity event. 38% of the Companies include Tag along or drag-along clauses and purchase by existing investors, in their Plan documents.

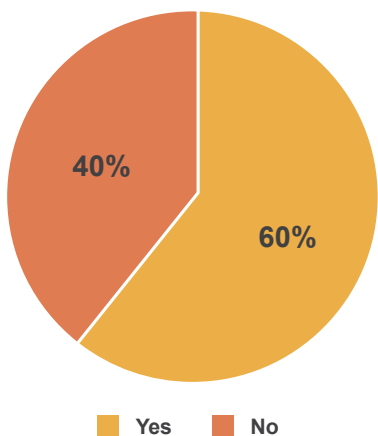
How did Companies achieve an exit route for providing liquidity?



We further asked Companies how do they provide liquidity to their employees.

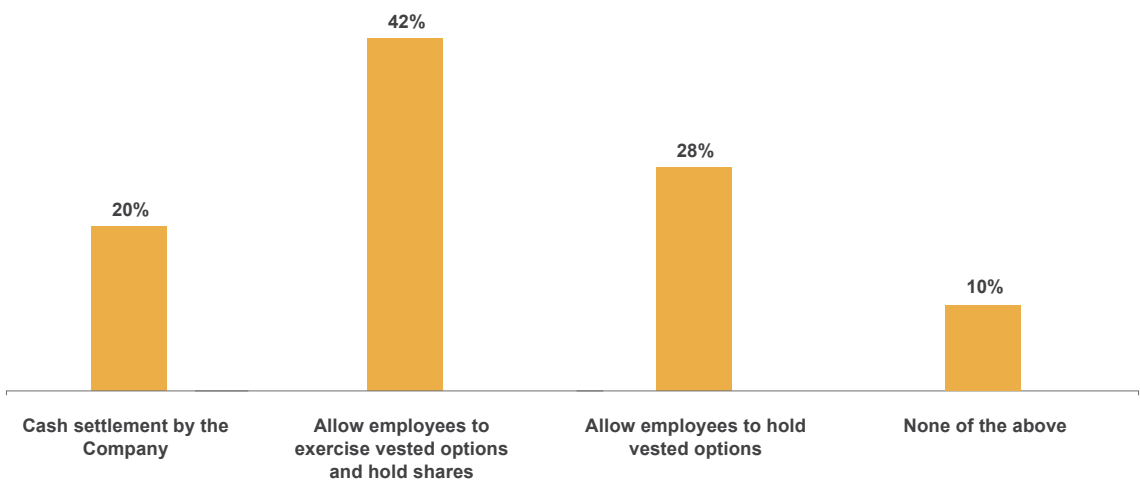
Out of the Companies that achieved liquidity, 33% of the Companies settled options by cash payout. 40% achieved liquidity through strategic sale event i.e. Tag along/ Drag along in the business or purchase of shares by existing investors. We noticed around 27% of Companies are achieving liquidity through Buyback of shares by the Company or through ESOP Trust.

Does the Scheme require mandatory accelerated vesting of options on happening of liquidity events?



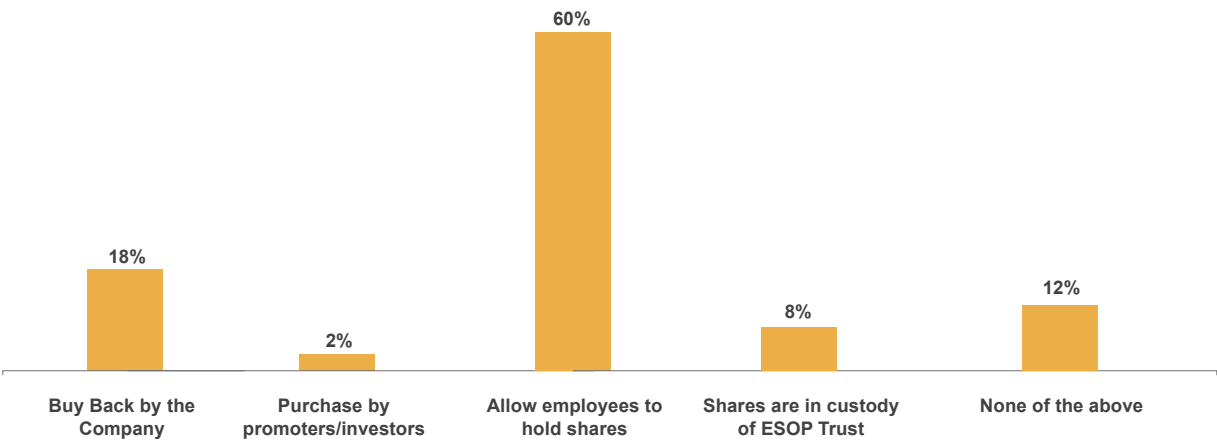
Most of the Unlisted Companies in SEA (2020:60%) have provision to acceleration of vesting of unvested options, on happening of any liquidity event, including IPO. Remaining 40% of Companies do not have such a provision.

If exercise is linked to a liquidity event, then how are vested options dealt with upon separation?



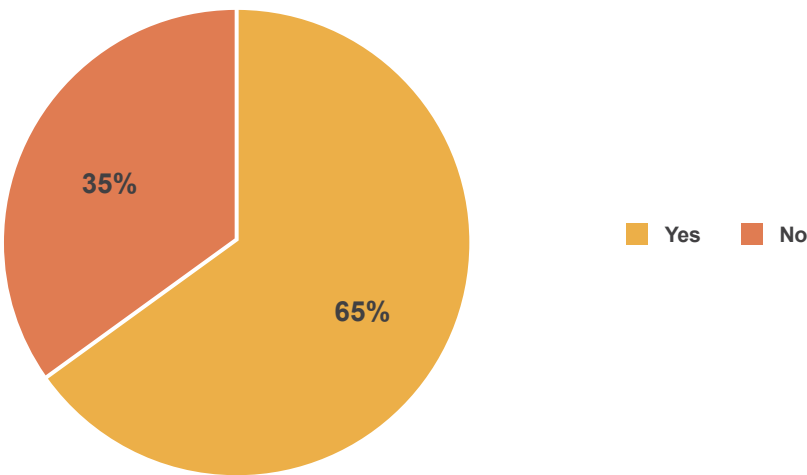
On separation of employees, 42% of Unlisted Companies in SEA deal with vesting options by allowing them to exercise those options and convert them into shares. 28% of these companies allow separated employees to hold the vested option until a liquidity event, and 20% offer cash settlement of vested options at prevailing FMV or discounted FMV.

If the Scheme allows exercise, then how are these shares dealt with at the time of separation?



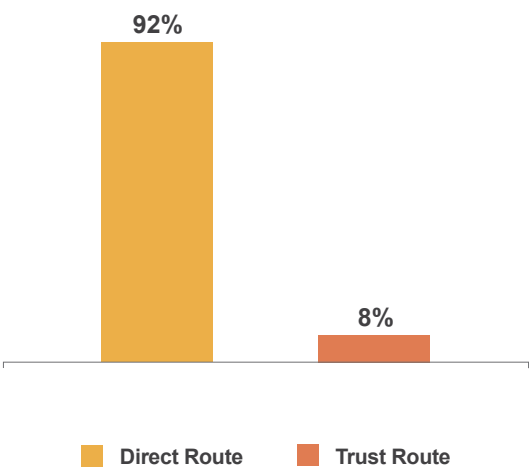
60% of Unlisted Companies in SEA (with a fixed exercise period prior to the liquidity event), allow employees to hold shares, whereas only 20% of Companies arrange for the purchase of those shares either by Company, Trust or Promoters/Investors. 8% of Companies have Trust, which holds shares on behalf of the employees.

Are separated employees entitled to the same benefits as existing employees for their vested options?



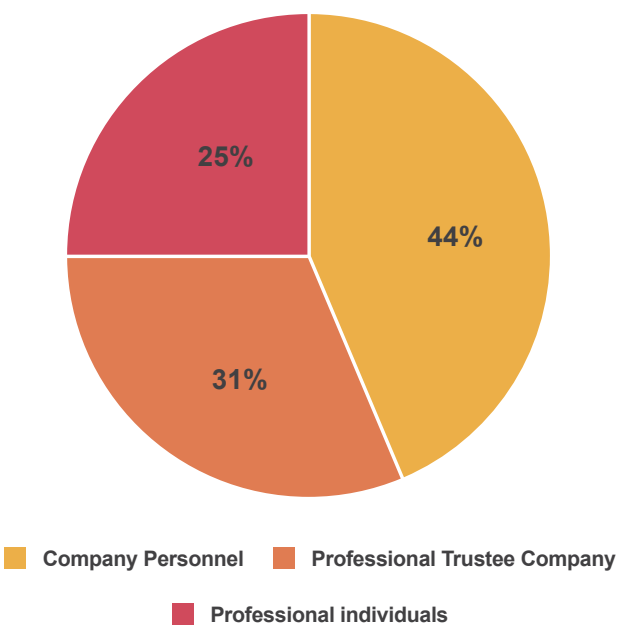
65% of the Unlisted Companies in SEA are providing the same benefits to even separated employees as the existing employees in case of a liquidity event.

Route for implementing ESOPs



Direct Route remains the preferred mode for implementing ESOPs for 92% of the Unlisted Companies in SEA. Only 8% of Companies are going through the Trust route.

Constitution of Trustees



56% of Unlisted Companies in SEA appointed a professional trustee company or professional individuals as their trustees in 2022 for ESOP Trusts. 44% of the Companies appointing Company Personnel as their Trustees.

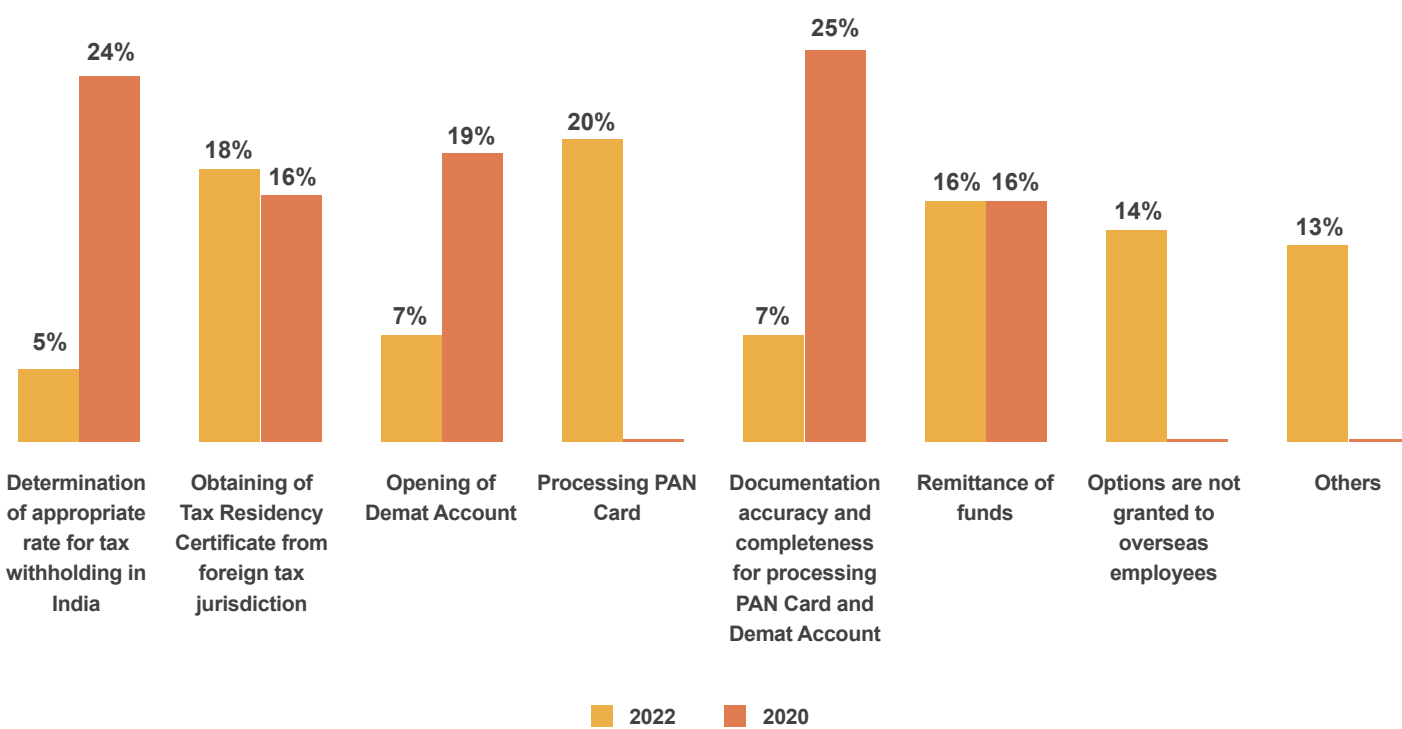


IMPLEMENTATION TRENDS

OVERSEAS EMPLOYEES - INDIA

6.1

If options are granted to overseas employees, what are the pain points faced by them during exercise?

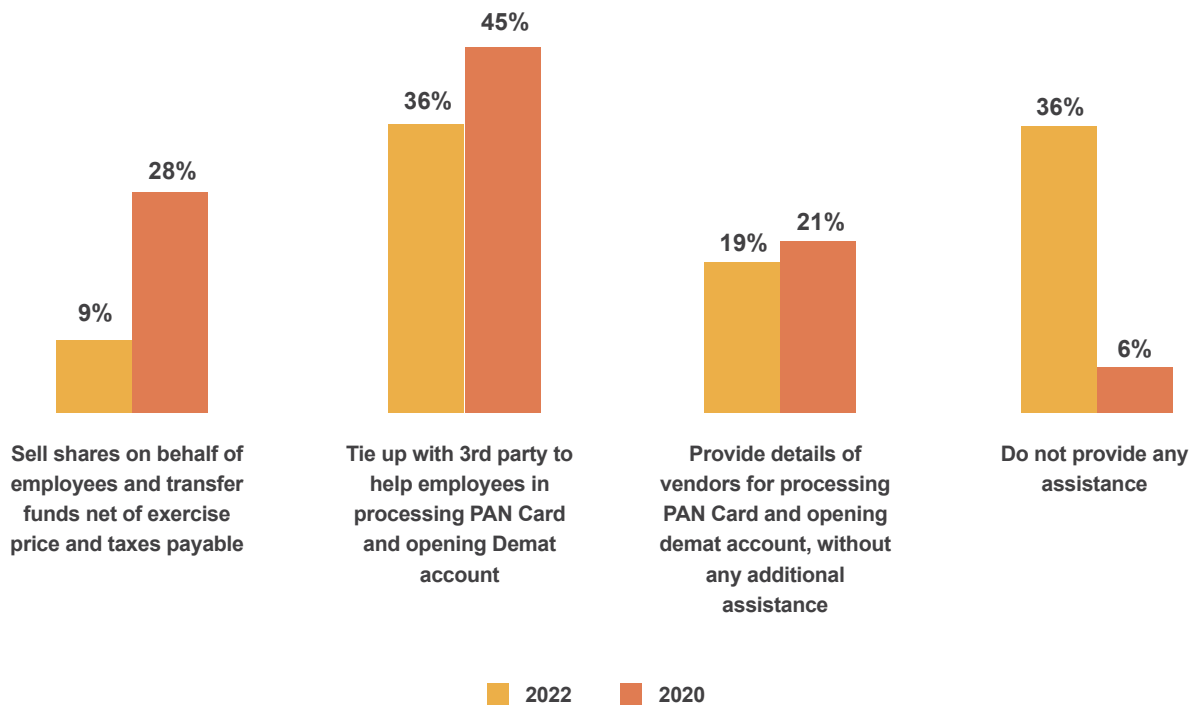


Indian Companies granting options to Overseas employees continues to be a challenge due to FEMA and tax compliances. Nature of challenges includes remittance of funds, obtaining tax residency certificate from foreign tax jurisdiction, and processing of PAN and Demat account for Overseas employees.

Whether and how Companies assist overseas employees in exercising their options?

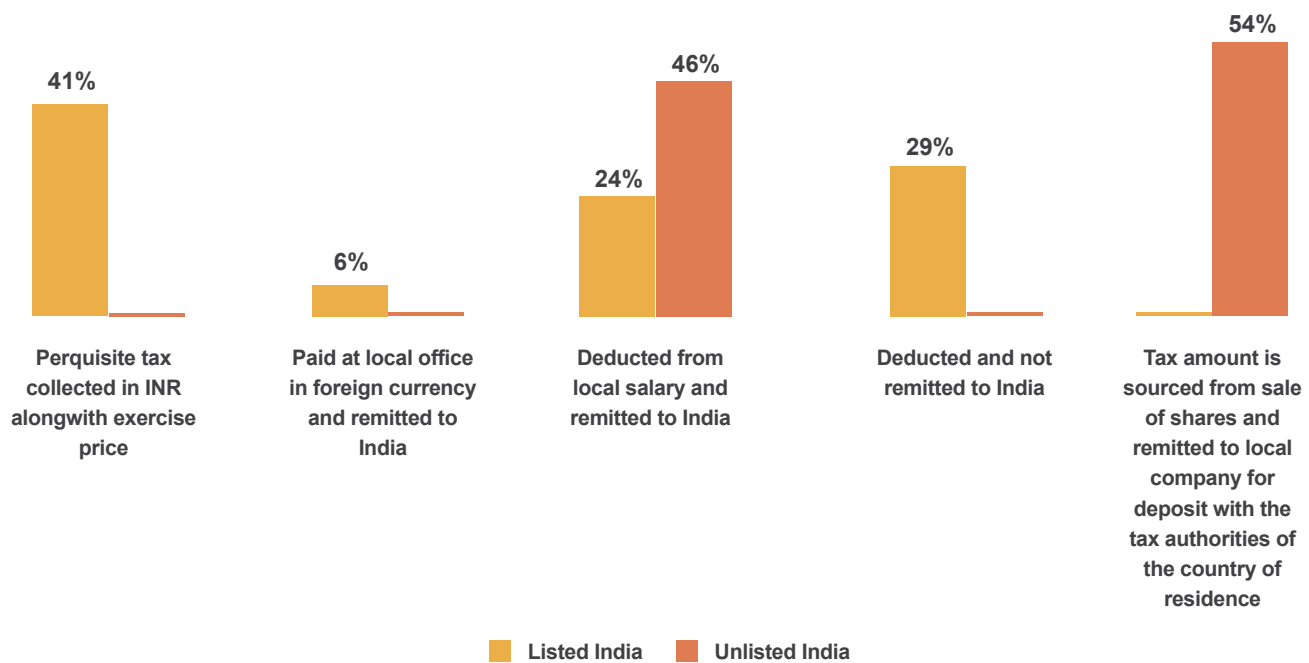
Though 36% of Indian Companies do not provide any assistance to overseas employees to exercise their options, another 36% of the Companies tie up with a 3rd party to help employees in processing PAN Card and opening a Demat account; 19% of the Companies provide details of vendors for processing PAN card and opening Demat account.

Companies providing a Cashless exercise facility to overseas employees by selling shares on their behalf and transferring funds net of the exercise price and tax to the employee reduced to 9% compared to 28% in 2020.



Perquisite tax on options exercised by overseas employees

How do Companies recover the Perquisite tax from overseas employees is often a debated point. We see a variety of ways Companies are complying with this requirement.



Collection of perquisite tax in INR has been the most popular method over the years with Companies collecting tax in INR along with exercise price (consolidated for Listed and Unlisted Companies was 2017:53%, 2015:48%). Around 27% of Unlisted Companies have deducted taxes from the local salaries and remitted the net benefits to their employees.

ACCOUNTING

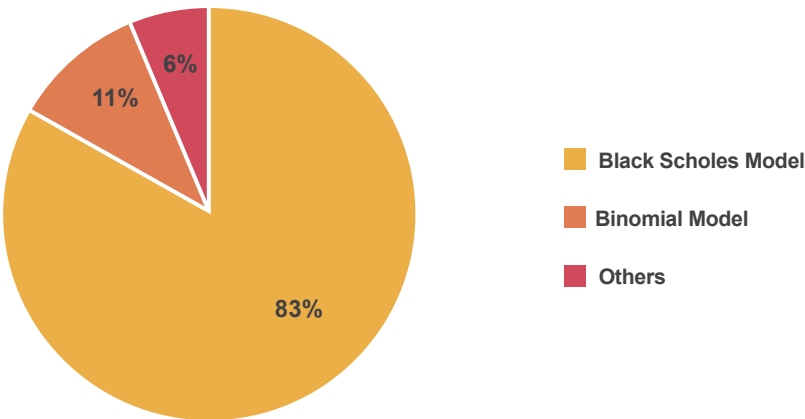
6.2

Method followed for accounting

There are two methods of calculating compensation cost. The fair value method, where compensation cost is calculated based on the fair Value of options as on the date of grant and the intrinsic value method. Intrinsic value method of accounting is where the difference between the fair market value of share on the date of grant and the exercise price is accounted for over the vesting period.

Listed and Unlisted Companies where Ind- AS 102 is applicable must follow the fair value method of accounting for calculating compensation cost. IFRS, US GAAP and Singapore FRS 102 also mandate fair value method of accounting.

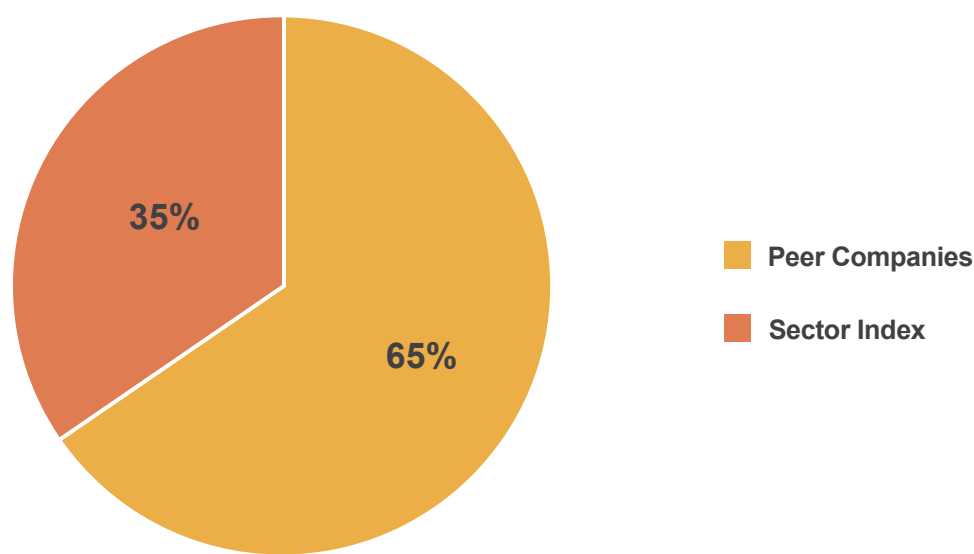
Method to calculate fair value of options



Under Option pricing models, most Companies prefer the Black Scholes model, other methods being used are Binominal and Monte Carlo.

How do Unlisted Companies calculate volatility for the Option Pricing model?

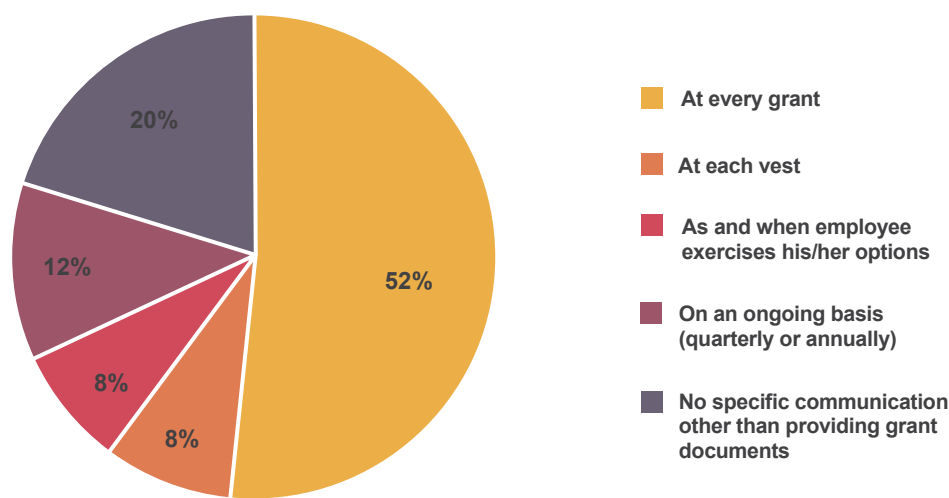
Since Unlisted companies do not have historical data on the volatility of their share prices, they can choose to take the volatility of one or more Listed Peer Companies. While 65% of Unlisted Companies go with this alternative, 35% take Sectoral index volatility, in the absence of a Listed Peer Company.



PLAN COMMUNICATION

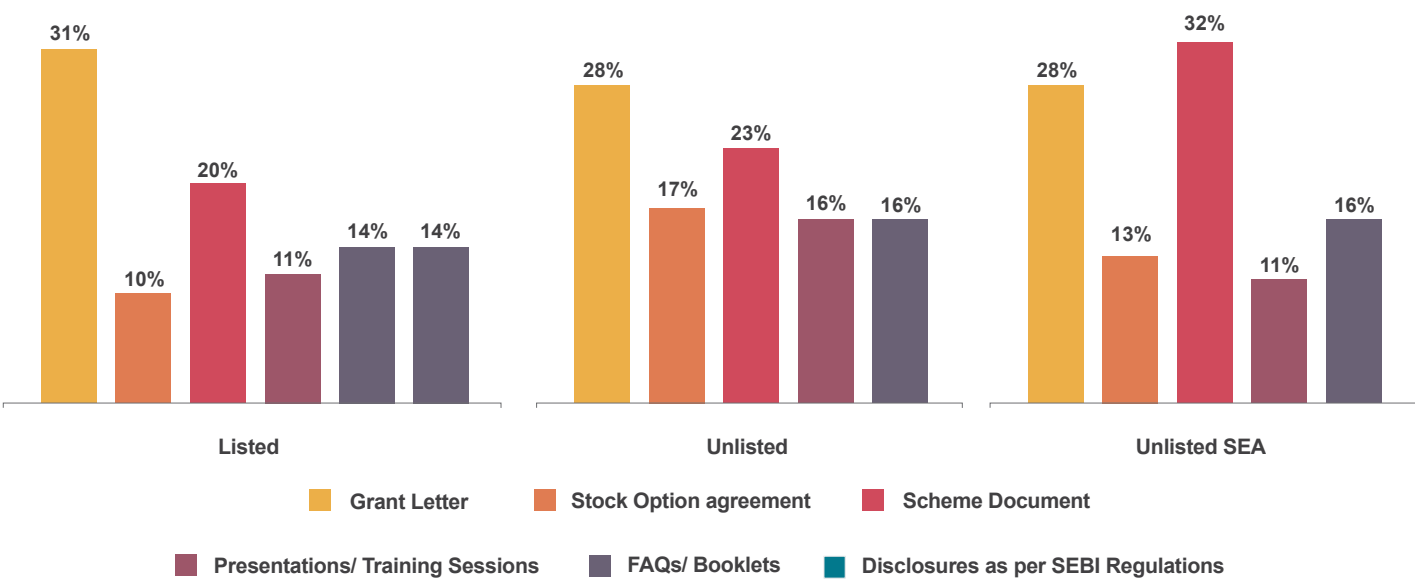
6.3

Frequency of communicating ESOP Plan details to the employees



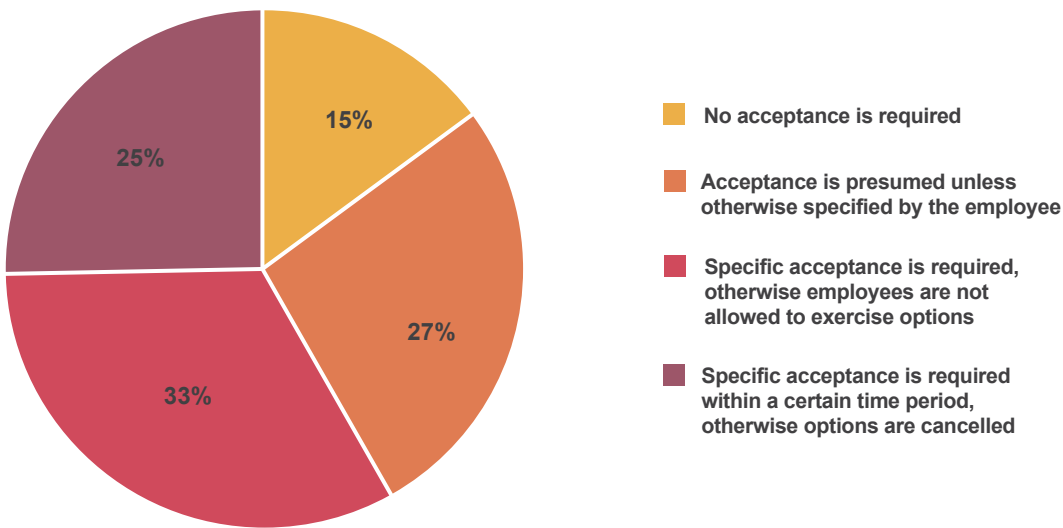
52% of the Companies (2020:73%) communicate ESOP Plan details to employees while granting options. 20% of Companies do not communicate specifically other than giving grant documents.

Grant Documents provided to employees and mode of communication of these documents



Grant Letter and Scheme Document are the two most important documents used for communication at the time of grant of options.

Acceptance of grant by an employee



Only 42% of Companies do not require acceptance of grant or presume that a grant is accepted unless otherwise specified by the employee.

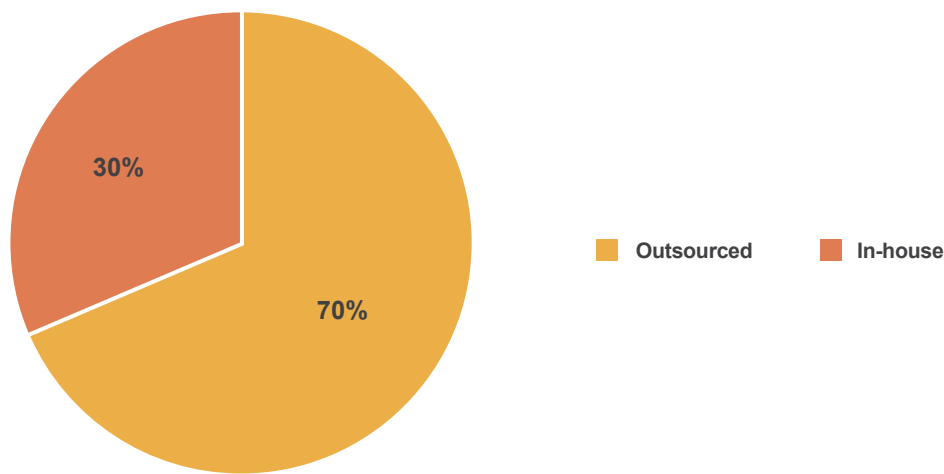
Rest 58% of Companies require specific acceptance of a grant without which either employee are not allowed to exercise options or options are cancelled after a specific time.

PLAN MANAGEMENT

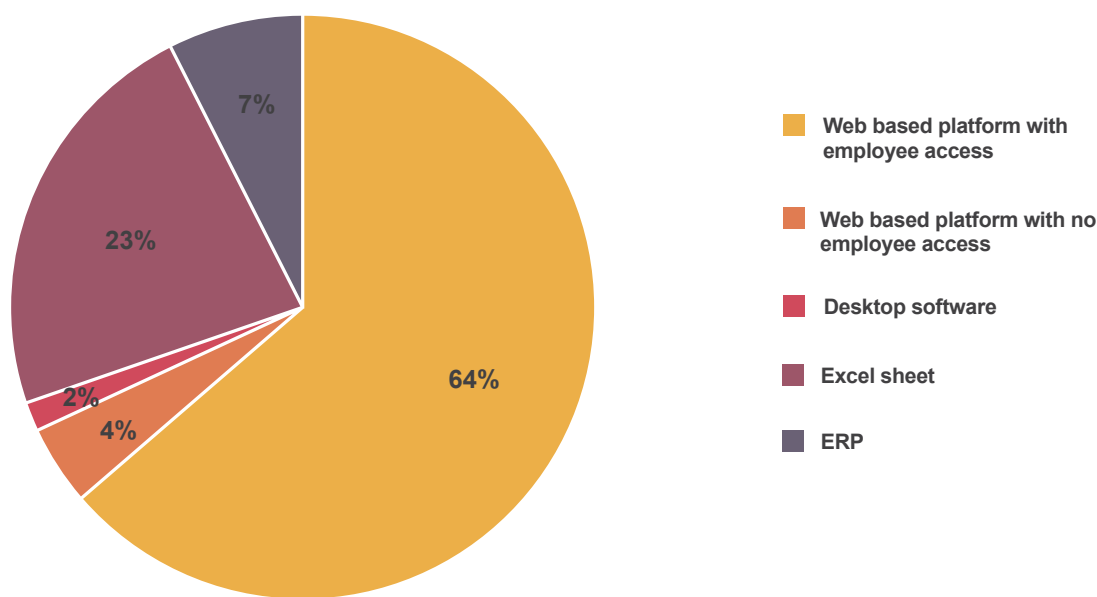
6.4

Plan Management

70% of Companies have outsourced the Management of their ESOP Plans, balance only 30% of Companies manage the administration in-house using MS Excel or other software.

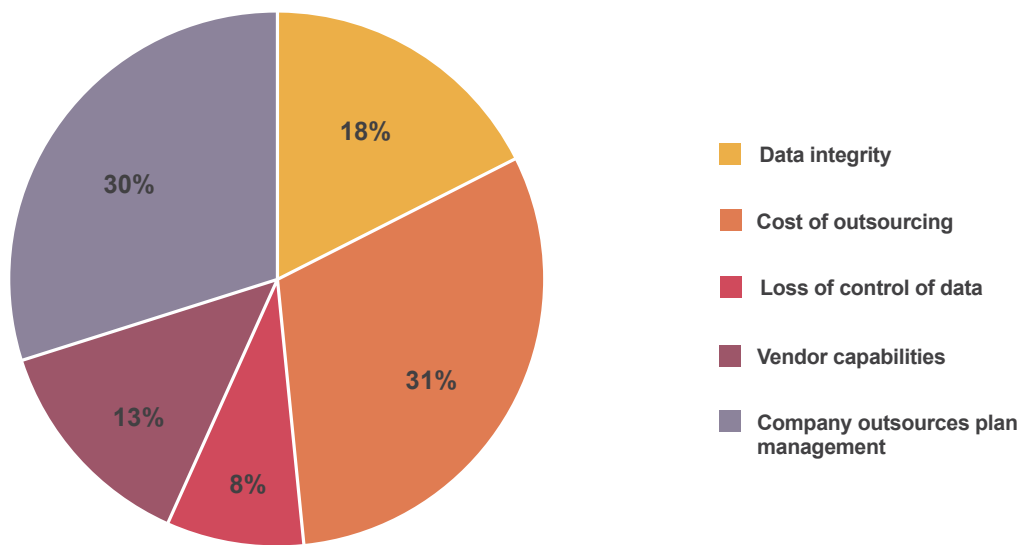


Software used for plan management



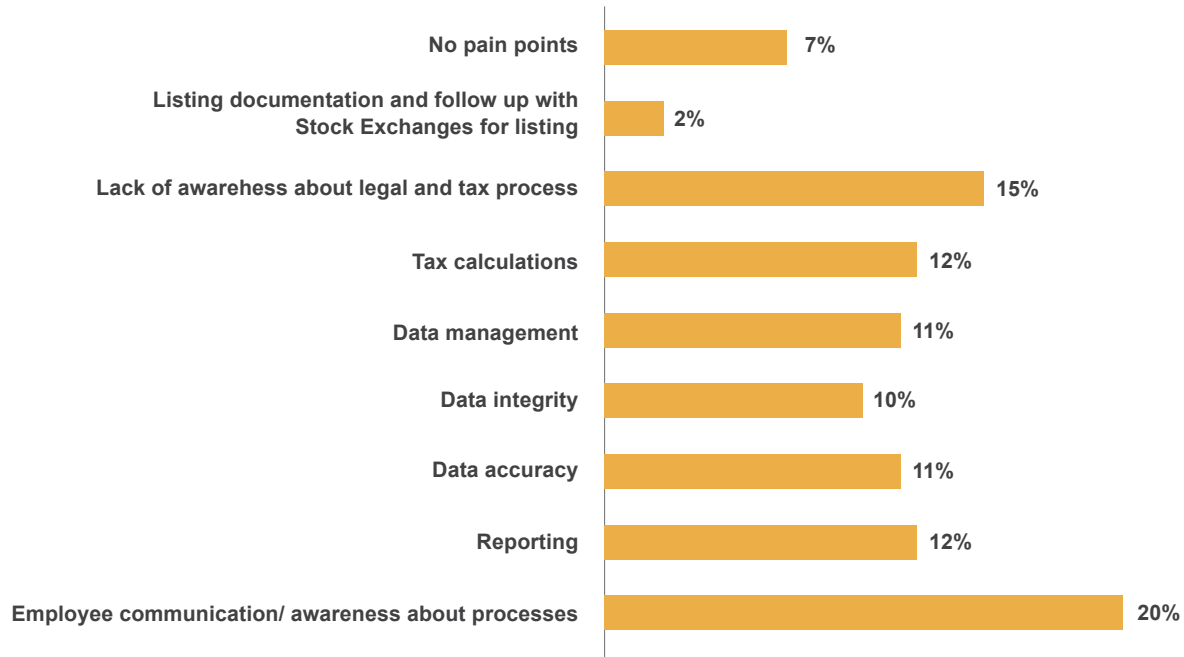
Web-based platform with employee access is the most preferred option for 64% of the Companies who have outsourced plan management.

Reasons for not outsourcing plan management



39% of Companies responded that data integrity, loss of control over data and Vendor capabilities were the reasons for not outsourcing Plan management.

What are the pain points for Plan management?



While managing their ESOP Plans, companies' major pain points are tax calculations and employee communication and awareness about processes (20%).

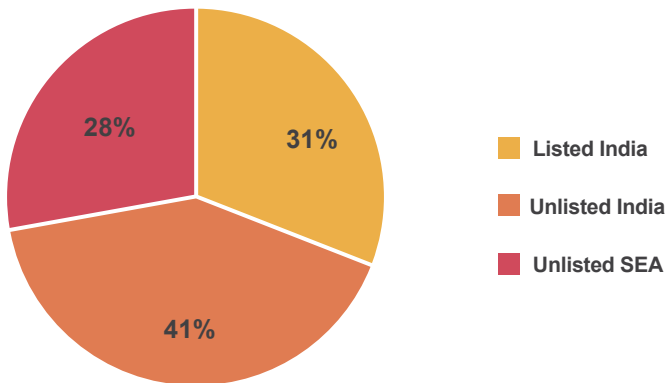
More than 10% feel that reporting, data management, and data accuracy lack of awareness about legal and tax process were also major hurdles in the Management of ESOPs in the Company.



COMPANY DEMOGRAPHICS

COMPANY DEMOGRAPHICS

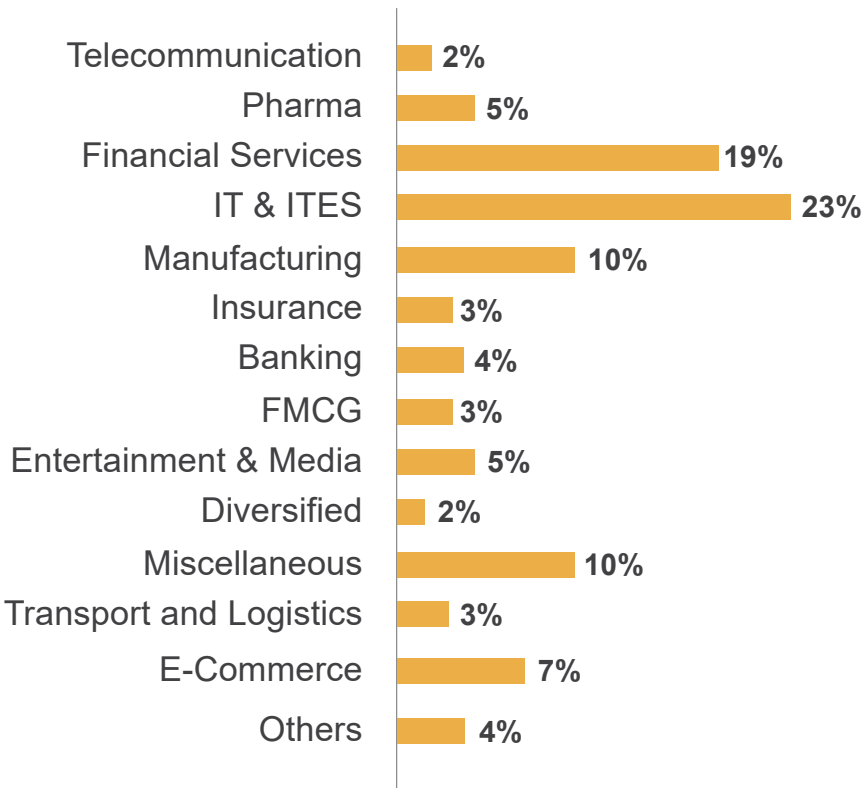
Participants by Legal Status and Region



n=309

Participants by Legal Status and Region

Financial Services, IT & ITES and Manufacturing are the largest industry represented in this survey followed by E-Commerce and Pharma.

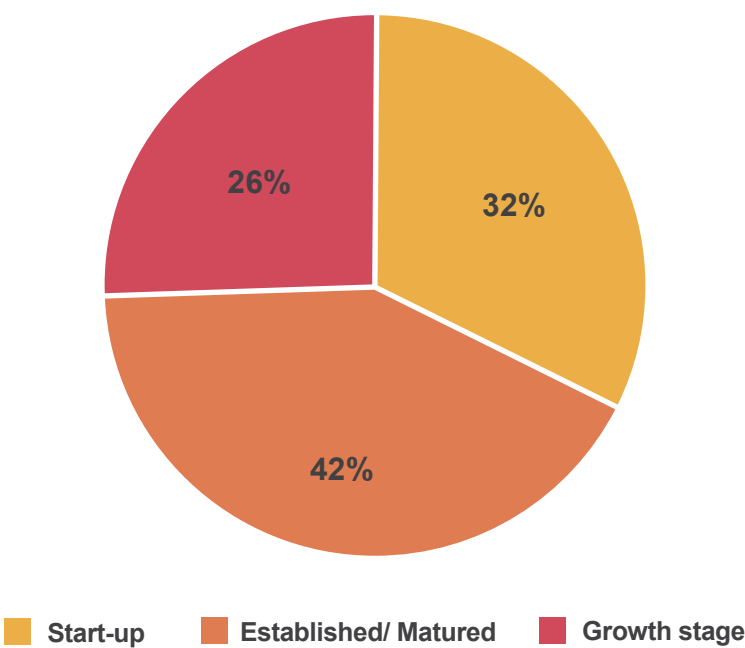


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Note: Others include Automobiles, Infrastructure, Realty & Construction, Healthcare, BPO, Travel agencies, Pharamceuticals Hospitals.

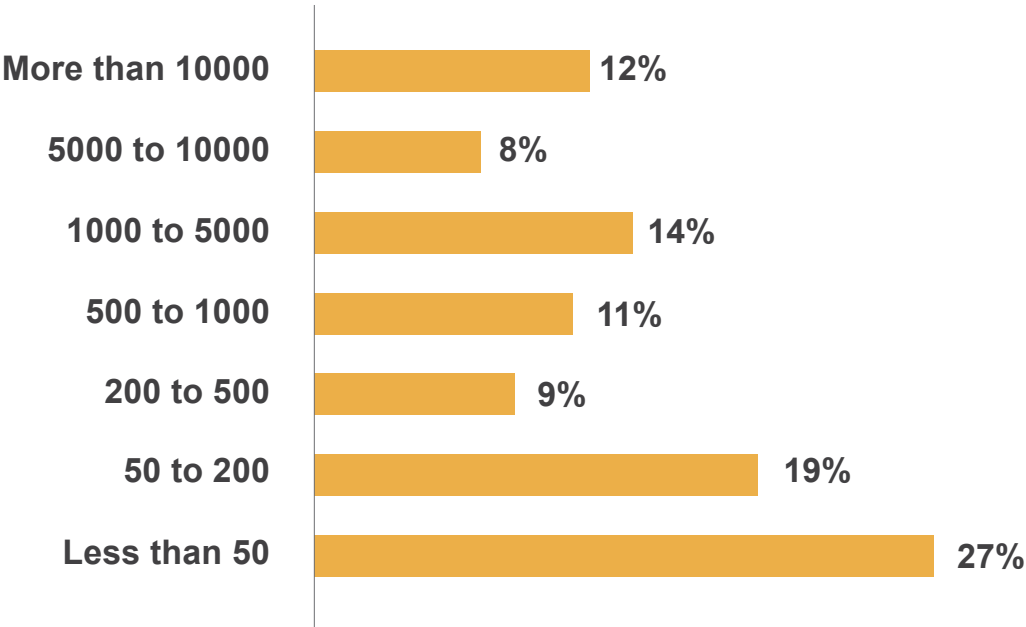
Participants by size of the Company

42% of the participants are Established/Matured companies.



n=309

Participants by Employee Size



n=309

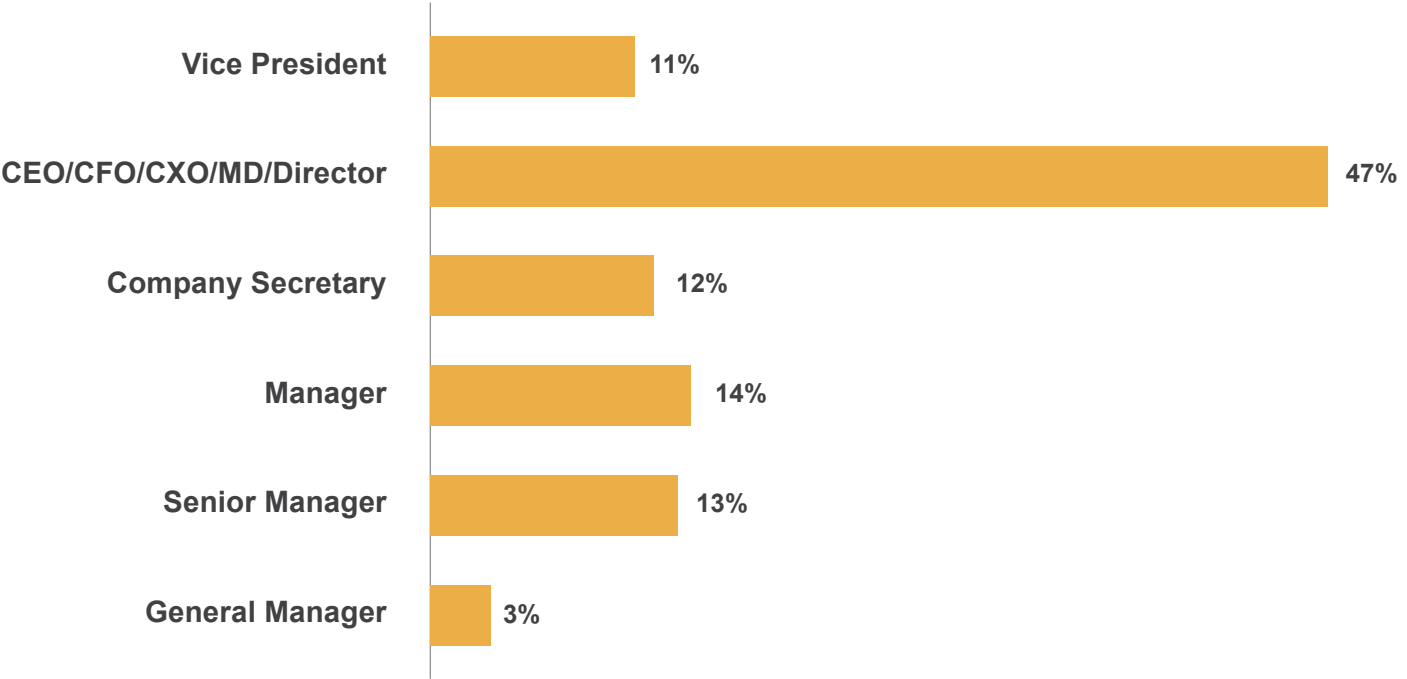
34% of participants have more than 1,000 employees.



PARTICIPANT INFORMATION

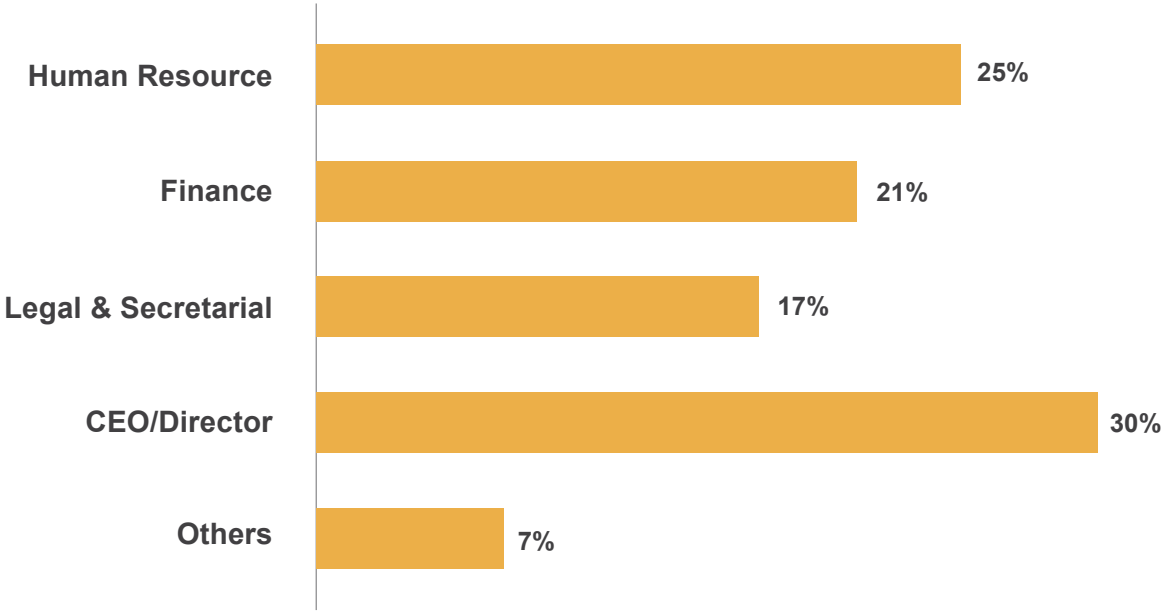
PARTICIPANT INFORMATION

By Designation/ Title



n=309

By Department



n=309

ABOUT US

ESOP Direct is a leading provider of Equity Compensation solutions for startups, unlisted and publicly listed companies. Our service offerings cover the entire life cycle of ESOPs including Plan conceptualization, Design, Documentation, Plan management, Compliance and Reporting. We have serviced over 1200+ clients across all industries, domestic and international, listed and unlisted. ESOP Direct is a subsidiary of Qapita Fintech Pvt. Ltd., a market leader in Equity Management and Marketplace solutions for unlisted and listed companies in India and South East Asia.

Qapita is Asia's largest equity management solution and serves over 1,300 companies in India and South Asia in managing captables, ESOPs and providing liquidity solutions through its digital marketplace. Qapita helps growth companies manage transactions on a single platform, be due-diligence ready at all times, automate investor relations and run future scenarios including fundraising and exits. Qapita partners with fast growing companies through its inception, growth, IPO and beyond journey and offers seamless equity management, ESOP structuring, administration and liquidity solutions at every stage of the company's growth.

OUR SERVICE OFFERINGS

PLAN DESIGN

Consulting

The designing of an Equity based compensation scheme goes through three stages- Conceptualization, Consummation and Communication.

Key to a successful plan design is determining the company's financial and HR goals and structuring the plan to help achieve these goals. Plan design encompasses Finance, Tax, Legal and Corporate Governance and successful Employee Communication. Our service encompasses all these aspects of Plan design.

PLAN MANAGEMENT

Administration

We provide full spectrum ESOP Management solutions powered by our cutting-edge digital platform powered by Qapita. The service includes plan administration, employee communication, helpdesk, on-line Reports.

Qapita is a fully integrated platform with interfaces with your ERP, digitizes plan set-up, digitize grant issuance and on-line grant acceptance through digital signatures, payments gateway, live stock prices, perquisite tax calculations and listing documentation for stock exchanges.

ESOP Cashless

In a pioneering effort, we have designed India's first cashless ESOP exercise module which has been vetted by the legal experts and approved by the regulators. Our cashless exercise module allows employees to exercise their options without bothering to arrange for the funds. The entire process (exercise to cash in hand) happens on-line and with a turnaround time of 5-7 days. Compare this with the existing process which takes anywhere between 30 -45 days and you know the value Cashless, adds to your ESOP experience.

ESOP LIQUIDITY SOLUTIONS

Qapita Marketplace

We provide bespoke liquidity solutions for growth companies through Qapita's unique digital marketplace. Companies can offer liquidity through buyback/surrender programs as well as company governed secondary programs powered by Qapita's syndicate network of family offices, institutional and high net worth investors. Liquidation programs are administered through a digital backed platform automating surrender/sale flow as per preset eligibility limits per employee and digitizing the transaction workflow including KYC documents submission, digital execution of agreements and share transfer process as required.

PLAN COMPLIANCE

ESOP Financials

Accounting standards require expensing of ESOPs in company's books. We help companies with:

- Option valuation (using Black Scholes and other binomial models)
- Expensing
- Reporting & Disclosure as per IGAAP, IFRS and US GAAP
- Consulting on Transition to Ind AS

Merchant Banker Certification

CAT- I Merchant Banker Certification for in-principal approval of the Stock Option Scheme that must be filed with Stock Exchange for listed companies in India.

Share Valuation Services

Independent Share Valuation at the time of grant of options and on exercise of options required by unlisted companies.

409A valuation

A 409A valuation is crucial to determine the fair market value of your common stock and to then set the exercise price of stock options. This is necessary for compliance with the IRS regulations for granting options to US-based employees.

We, at Qapita, specialize in providing high quality 409A valuations and have helped several companies defend the valuation with their auditors (Including the big4). We understand the unique challenges that come with starting and growing a company, and we're here to help you navigate them.

ESOP Trustee

We provide complete service for creation, setup and management of Trusts. We take care of managing the transactions, banking, accounting, administration and the compliance of the Trust. This service is also provided through a web based system, giving you online access to Trust reports and accounts.

We also act as independent Trustees. The Companies Act and SEBI Regulations require ESOP Trusts to have independent Trustees in India.

Key differentiators:

- Our strength lies in our focus, experience, thought leadership and our strong domain expertise in equity based compensation
- We are the only focused player with end-to-end service offerings in this domain
- Our approach is one of a Partner. Our goal is to ensure that your Plan is successful
- Our emphasis is on innovation and the delivery of impactful ideas to aid in the resolution of critical problems in plan implementation
- Our platform supported by managed services automates the entire ESOP administration process, from option grant to monetization, providing participants with real-time reporting and accurate information

ESOP Direct

A  **QAPITA** Company

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