

**Law Office
of
HOWARD L. STOVALL
2131 North Racine Avenue
Chicago Illinois 60614
Telephone (773) 248-8896
Facsimile (773) 248-8897
E-mail Howard@Stovall-Law.com**

**Foreign Company Stock Option Plans
and
Employees in the Arab Middle East**

Employee stock option plans have served for many years as a method by which an employer could provide additional compensation to attract and retain its workforce. By offering employees a share in its own stock, an employer seeks to incentivize those employees towards greater productivity and loyalty. This memorandum summarizes certain legal and tax issues that confront foreign (e.g., U.S. or European) companies that contemplate the offering of stock option plans to their employees working in the Arab Middle East.

An increasing number of countries in the Arab Middle East have enacted regulations governing stock option plans involving the shares of local companies (as well as the shares of foreign companies that are traded on local stock exchanges). Such regulations are beyond the scope of this summary.

Employee stock purchase plans ("ESPPs") typically involve employees electing to make contributions to purchase shares of the employer's common stock at a discount at the end of some specified purchase cycle. Other employee benefit plans include employee stock ownership plans ("ESOPs", a defined contribution plan where the employer allocates stock ownership to the employee via a trust which holds the stock on the employee's behalf); restricted stock units ("RSUs", typically unfunded unsecured promises to issue company shares at no cost to the employee at a later time); and stock appreciation rights ("SARs", giving an employee rights to the monetary equivalent of appreciation in the value of a specified number of shares over a specified period of time). For purposes of this summary, we have focused our analysis on ESPPs, referred to here as stock option plans.

1. Securities Laws

Most countries in the Arab Middle East have enacted securities laws and regulations to control the marketing and offering for sale of foreign

securities within the country. However, a foreign employer would not usually be required to obtain any local securities approvals or make any governmental filings for purposes of its stock option plan for local employees. For example, the award of employee stock options in such Arab countries would not be considered the marketing and offering of securities for these regulatory purposes, for which a prospectus, registration or exemption must be sought by the employer.¹

This conclusion assumes that the stock option offering involves an award related to a foreign (non-local) company, is offered only to employees of the employer or its local affiliate (and not to the general public) and is in the nature of providing additional compensation or bonus to those employees.

For example, Lebanese securities law does not directly address employer stock option plans. However, Lebanese securities law is primarily directed at public placements of shares (rather than private placements of shares, particularly those limited to an employer's workers); at placements of shares listed on Lebanese stock exchanges (rather than shares listed on foreign exchanges); and at purchases of shares (rather than shares being provided as additional compensation or a bonus to employees).

We understand that the Lebanese Capital Markets Authority has previously taken the informal view that a foreign employer's stock option plan would generally fall outside application of the local securities regulations. We have also received informal guidance to similar effect from the Central Bank of Bahrain, the Kuwaiti Capital Market Authority, and the UAE Central Bank.²

Until recently, Saudi Arabia presented a significant exception to these general conclusions. Before 2018, all securities offers (including employee stock option plans) were governed in Saudi Arabia by the Offers of Securities Regulations, which stated that such offers could only be conducted through a licensed securities firm in Saudi Arabia, by submitting a pre-offer notification to the Saudi Arabian Capital Market Authority ("CMA"), as well as a post-offer report to the Saudi CMA.³ As a result, many companies restructured their stock plans in Saudi Arabia to fall outside the literal language of the regulations. For example, some companies arranged for a cash-settled award plan, providing payments to employees based on the employer's share value but without creating any employee share ownership rights.

Starting in 2018, new Saudi Arabian securities regulations categorize employee stock option plans as "exempt offers", for which no pre-offer or post-offer filings are required.⁴ Moreover, such offers no longer need to be made through a licensed securities firm. However, the employer is required to make filings with the Saudi CMA for any quarter in which activity relating to stock awards occurs (such as when grants are made).

2. **Securities Legends/Disclaimers**

In general, there is no special securities disclaimer or written legend required in connection with stock option plans offered by a foreign employer to its employees in any country in the Arab Middle East. However, there is no harm in using such a disclaimer or legend in the award documentation. For example, disclaimers such as the following has been used in the past:

Oman

This Plan does not constitute the marketing or offering of securities in Oman and consequently has not been registered or approved by the Central Bank of Oman, the Omani Ministry of Commerce and Industry, the Omani Capital Market Authority, or any other authority in the Sultanate of Oman. Offerings under the Plan are being made only to Eligible Employees of your employer, your employer's parent company, or any other Subsidiary or Affiliate.

United Arab Emirates

This offer has not been approved or licensed by the UAE Central Bank or any other relevant licensing authorities or governmental agencies in the United Arab Emirates. This offer is strictly private and confidential and has not been reviewed by, deposited, or registered with the UAE Central Bank or any other licensing authority or governmental agencies in the United Arab Emirates. This offer is being issued from outside the United Arab Emirates to a limited number of employees of the Employer and affiliated companies and must not be provided to any person other than the original recipient and may not be reproduced or used for any other purpose. Further, the information contained in this offer is not intended to lead to the issue of any securities or the conclusion of any other contract of whatsoever nature within the territory of the United Arab Emirates.

3. **General Contract Rules**

In most countries of the Arab Middle East, foreign company stock option plans are not subject to any specific securities law or other statutory rules. Rather, such stock option plans are generally deemed a matter of contract between the parties, and therefore governed by the written terms and conditions of the relevant plan documentation.

In that light, local contract law rules would probably require that the employer obtain the acceptance or consent of each employee to the specific stock option plan. Although there is no general requirement that plan documents be in Arabic, if an employee does not read and understand English, there is a risk that the employee has not validly and knowingly consented - and thus the various rules and requirements of the documents might be deemed non-binding on that employee.

Under general contract rules in the Arab Middle East, the offer of the right to participate in the stock option plan should not be considered an on-going right or entitlement of employment, if the employer clearly states that the plan is a limited and revocable benefit extended to the employee and is not a fixed, regular and mandatory part of the employee's compensation.

However, under general principles of local law in many Arab jurisdictions, there is a possibility that a benefit could become habitual or customary, and constitute an "acquired right" of the employee.

Under the acquired rights concept, if a right or benefit is habitually bestowed upon an employee over several years, then the employee may acquire the right to treat such benefit as part of his/her employment package, despite the fact that there was no agreement or contract to that effect. Accordingly, if certain bonuses and/or fringe benefits are habitually paid, the employer runs the risk of such amounts becoming construed as part of the employee's remuneration.⁵

To become habitual or customary in the face of contrary language in the parties' written agreement, the benefit usually must be a fixed or specified amount (for example, a certain percentage of salary) and paid for a substantial length of time, probably at least three or four consecutive years.

An employer usually will seek to obtain an acknowledgement from an employee that the benefits distributed under a stock option plan are not part of the employee's regular compensation or salary, that the plan is provided on a discretionary and voluntary basis, and that it may be amended, modified, or terminated by the employer at any time. This will minimize the risk that the benefits become acquired rights and thus part of the employee's regular compensation.

4. Income Taxation

None of the countries in the Gulf Cooperation Council (i.e., Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates) currently impose any income tax on employment income, wages, or fringe benefits. As a result, there would be no income tax consequences to an employee in these countries relating to an employee stock option plan.

In those Arab countries with an individual personal tax on employment income, the stock granted to the employee would usually be deemed benefits complementary to salary, particularly if mentioned in the employer's policy, the employment offer letter and/or the employment agreement. The taxable amount would be the difference between the fair market value of the shares at vesting and the purchase price (the "discount"). Vesting would occur when the employee exercises the stock option, pays the discounted purchase price, and receives ownership of the stock.

In Lebanon, for example, local income tax law does not contain any express rules regarding awards of employee stock options, although the definition of "employment income" is certainly broad enough to encompass such compensation paid. The Head of the Tax on Salaries and Wages at the Lebanese Ministry of Finance has taken the position for many years that any benefit deriving from employment in Lebanon is subject to the tax on salaries and wages and is to be withheld/reported by the Lebanese employer, whether or not cross-charged by the foreign parent company to that local employer (or, for that matter, whether appearing in local employment-related materials).⁶

Consequently, in Lebanon, such benefits would be subject to the Tax on Salaries and Wages, to be paid by the employer in Lebanon to the Lebanese Ministry of Finance ("MoF").⁷ The Tax on Salaries and Wages is an escalating tax that could reach 25% of the employee's salary. The employer is required to report and pay online, quarterly and annually, the Tax on Salaries and Wages to the Lebanese MoF.

By way of contrast, in Jordan, we understand that a local employee would be subject to income tax on the benefit received, but the Jordanian employer would be required to report and withhold income tax from an employee only if costs and expenses of the foreign parent company's stock awards are recorded on the Jordanian employer's books and records, the Jordanian employer reimburses its parent for the cost of the awards, and/or the Jordanian employer is otherwise involved in the payment of the awards to its employee (i.e., if the operation of the plan occurs at least partially on-shore Jordan).⁸

5. Social Security Contributions

In the countries of the Gulf Cooperation Council, social insurance requirements apply only to local nationals, and even in those cases contributions are only calculated on basic salary that typically does not include fringe benefits such as employee stock option plans.

By way of contrast, in Lebanon, pursuant to Article 68 of the National Social Security Law, earnings subject to payment of contributions are gross salary in addition to benefits in kind. Pursuant to Article 1 and 2 of Regulation No. 11 - Contributions Regulation, the earnings that are subject to payment of contributions includes benefits in kind. In that light, we believe that vested stock options would be subject to payment of social security contributions to the National Social Security Fund ("NSSF").⁹ As with the income tax, the contribution amount would be based on the difference between the fair market value of the shares at purchase and the purchase price.

The local employer in Lebanon must withhold its employee's social security contribution from gross wages, and remit to the NSSF either monthly (if 10 or more employees are employed by the employer) or quarterly (if fewer than 10 employees are employed by the employer).¹⁰

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Many foreign companies are offering stock option plans to their employees working in the Arab Middle East. In general, employers will not face any significant obstacles to the offering of such plans in Arab countries, as such plans are largely governed as a matter of contract between the parties. Carefully drafted and thorough plan documentation, agreed upon by the parties, should ensure the smooth administration of such employee benefits.

HLS/ah
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E N D N O T E S

1. For example, in offering the stock option plan to employees in Libya, the employer is unlikely to be deemed conducting financial promotion and marketing within the meaning of Article 32 of Libyan Law No.11 of 2010 regarding the Financial Market, and thus would not be subject to the prohibition on such activity by unauthorized persons. Notably, for companies licensed in the off-shore Qatar Financial Centre, the Financial Services Regulations (2010) contain an Employee Share Scheme Exemption from those "Regulated Activities" that are otherwise subject to the Regulations, thereby formally exempting share plans operated by an entity (or an entity in its corporate group) to facilitate participation in employee share plans.

2. The Iraq Securities Commission ("ISC") is only concerned with offers of securities inside Iraq, i.e., in relation to securities in a company which is incorporated in Iraq and/or listed on the Iraq Stock Exchange or other local exchanges licensed by the ISC. The ISC does not regulate offers of foreign securities. In addition, Egyptian securities law restrictions should not apply to a non-Egyptian company's stock option plan if the relevant stock is not listed on an Egyptian stock exchange.

3. Saudi Arabian Offer of Securities Regulations, approved by CMA Board Resolution No. 2-11-2004 dated 20/8/1425H (4 October 2004) as amended.

4. Saudi Arabian Rules on the Offer of Securities and Continuing Obligations, approved by CMA Board Resolution No. 3-123-2017 dated 9/4/1439H (27 December 2017).

5. See Baker & McKenzie, The Global Employer Focus on Egypt (24 December 2014), accessed at https://www.bakermckenzie.com/-/media/files/insight/publications/2015/09/the-global-employer-egypt/bk_employment_globalemployeregypt_2015.pdf?la=en .

6. Over a decade ago, the Lebanese government's position may have been different, i.e., that benefits paid off-shore Lebanon with no involvement by the local employer might not require local withholding/reporting. Rather, the employee in Lebanon would be personally responsible for reporting the income and paying the taxes. A letter dated July 2009, from the Lebanese Minister of Finance, concluded that a Lebanese employer would not need to withhold or report tax if it is not bearing the cost of the employee equity awards.

7. There is another view at the Lebanese MoF, pursuant to which stock options would be subject to the Tax on Movable Capital amounting to 10% (Chapter III of the Income Tax Law governing Movable Capital), similarly to the stock options granted to a bank's employees which are subject to the Tax on Movable Capital, pursuant to Lebanese Law No. 308 (3 April 2001) on "Issuing Banks' Shares, Trading in them, Issuing debt bonds, and Owning Real Estate by Banks". The better view is that non-bank corporate stock options are benefits deriving from a local employment agreement and should, as such, be subject to the Tax on Salaries and Wages. In addition, Lebanese Law No. 308 is addressed to banks, and should accordingly apply to banks only.

8. There are somewhat different income tax results if a company were to operate in Jordan through a so-called regional headquarters office. The income of a regional headquarters office is not generally subject to Jordanian income tax. Assuming a company treated the stock option benefit as an expense of the regional headquarters office, only Jordanian national employees of the regional headquarters office are subject to tax on this benefit. Non-Jordanian employees are not subject to income tax in Jordan when working for such a regional headquarters office.

9. There is another view, pursuant to which the stock options would not be subject to payment of contributions to the Lebanese NSSF, on the basis that the National Social Security legal texts do not specifically subject them to payment of contributions (contrary to other benefits, such as transportation, bonuses and allowances that are explicitly subject to said contributions). The better view is that vested stock options are benefits deriving from a local employment agreement and should, as such, be subject to the Lebanese NSSF contributions, just as they are subject to the Tax on Salaries and Wages.

10. In Jordan, an employer would not be required to withhold social security contributions from the stock option benefit if the benefit is not a regular and usual form of employee compensation.