

ESOP 101

A Comprehensive Guide for
🇻🇳 Vietnamese Startups



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I. INTRODUCTION

Purpose of the Ebook

This eBook is designed to provide the Vietnamese startup community with a thorough understanding of Employee Stock Ownership Plans (ESOPs). As Vietnam's startup ecosystem continues to grow, it's essential for business owners and employees to grasp the significance and advantages of ESOPs.

This eBook will break down the concept, showing how ESOPs can be put into practice to align the interests of employees and shareholders, create a culture of ownership, and boost business growth

II. WHAT'S ESOP AND WHO NEEDS IT?

Definition and Basic Concepts

Employee Stock Ownership Plans (ESOPs) give employees a sense of ownership in their company, often without requiring them to pay upfront. This chapter explores what ESOPs are all about & highlights two categories of companies that can benefit from implementing ESOP.

1. Fast-growing startups for attracting top talent

Fast-growing startups thrive on innovation and agility. ESOPs serve as a powerful tool for these dynamic enterprises, giving them a competitive edge in attracting top talent. By integrating a culture of ownership, startups can appeal to ambitious professionals looking for more than just a job; they want to be part of the company's journey.

ESOPs, with their promise of shared success, attract and engage individuals who seek a sense of belonging and contribution. In this way, startups can use ESOPs to draw in top talent and foster a workforce that is deeply invested in the company's success.

2. Listed companies for retaining talent

For established listed companies in Vietnam, the focus shifts to retaining valuable talent. In this context, ESOP becomes crucial for talent management. Aligning employee interests with the organization's long-term goals, ESOP effectively retains top-tier talent. The appeal of shared ownership fosters loyalty and strengthens commitment to the company's success.

Here, ESOP acts as a dynamic force, creating a work environment where employees see themselves as stakeholders and cultivating a culture of shared prosperity and loyalty.

III. TYPES OF ESOS: PROS & CONS

In the realm of Employee Stock Option Plans (ESOPs) and Long-Term Incentive Programs (LTIPs), it is crucial for businesses in Vietnam to understand the different types and their respective pros and cons. This chapter delves into the various types of ESOPs and LTIPs, highlighting their advantages and challenges to help businesses develop effective talent management strategies.

1. ESOP / ESOS

Employee Stock Option Schemes (ESOS) or Employee Stock Option Plans (ESOP) play a crucial role in fostering a sense of ownership among employees. A percentage of the company's total shares is allocated for employees. However, ESOPs do not convert directly into shares immediately. Instead, they provide employees with the option to buy shares at a price set on the grant date.

Employees can decide whether to buy the stock (exercise) or not. If they choose not to, their entitled ESOPs may expire. ESOPs primarily serve as an employee benefit designed to align employees' interests with the company's success. Giving employees a stake in the organization can foster engagement, motivation, and loyalty, leading to increased productivity and a stronger company culture.

The pros include increased employee motivation and loyalty. However, challenges may arise with valuation complexities and potential ownership dilution.

2. RSU (Restricted Stock Units)

Companies reward their top-performing employees in various ways. While some provide cash bonuses, others prefer to give ownership rights to their employees. Offering restricted stock units (RSUs) is one way to instill a sense of ownership. RSUs provide employees with a stake in the company without requiring an upfront financial commitment.

A restricted stock unit is a form of employee compensation where employees receive company shares at a future date if they meet certain conditions. These conditions can be based on performance, time, or a combination of both.

Companies typically launch RSU programs to motivate employees to perform. If employees meet the defined targets, their units vest. Once they fulfill the obligations, they gain ownership of the shares. Unlike in an ESOP scheme, they do not need to purchase the shares after the vesting period or receive a deep discount.

Restricted stock units provide advantages for both employees and employers. Employees benefit from low or no upfront payment at the time of vesting, while employers can use them as a tool to incentivize retention and performance.

RSUs also come with some disadvantages, including no dividend payments, market standoff periods, and automatic forfeiture of unvested RSUs. After employees exercise them, RSUs convert to common shares and are subject to market risks. If the share value decreases, so does the potential profit from selling them. Additionally, RSU holders don't receive dividends or voting rights until the RSUs are vested, at which point they gain the same rights as common shareholders.

Another disadvantage is that RSUs don't vest until specific conditions or restrictions are met. If employees leave the organization or fail to achieve the target, they forfeit any unvested units.

Let's say there's a market standoff provision in the RSU policy. This means employees are unable to sell the vested RSUs for a specific period after the initial public offering, typically lasting 90 to 180 days (around 6 months). This helps stabilize the company's stock price and prevents a significant sell-off.

3. SARs/Phantom Plans (Stock Appreciation Rights)

While ESOPs are a great employee benefits scheme that has worked for many companies, some hesitate to dilute ownership rights and share equity with their employees. Many founders are wary of having employees on their cap table. They want to reward employees for their contributions to the startup's growth, but they prefer to do so primarily through monetary benefits.

SARs stand out as a practical and appealing option for both employers and employees. They let employers share the benefits of the company's value appreciation with employees, either through cash (cash-settled SARs) or equity (equity-settled SARs), without involving ownership stakes or voting rights.

The cash payout for a unit of vested Phantom stock equals the value of a stock unit in the company at the time the payout event is announced. For example, if an employee receives phantom stock when the stock is valued at \$10 and the award vests when the stock is valued at \$50, the payout will be \$50 per unit. Conversely, if the stock's value drops to \$5 at vesting, the payout would be \$5 per unit.

The pros include flexibility and reduced dilution. However, challenges can arise in effectively communicating the concept to employees and aligning their performance with the value of phantom shares.

Grasping the nuances of these ESOS and LTIP types allows Vietnam businesses to tailor their incentive programs to meet specific organizational objectives. Weighing the pros and cons helps companies select the plan that best fits their corporate culture, engages employees, and contributes to long-term success in the competitive Vietnam business landscape.

4. PSP (Performance Share Plans)

Performance Share Plans (PSPs) tie rewards directly to the company's performance, aligning employee incentives with organizational goals and motivating them to contribute to the company's success.

The benefits include a clear connection between performance and rewards, though it can be challenging to define measurable performance metrics and maintain employee morale during periods of underperformance.

IV. ESOP IMPLEMENTATION IN VIETNAM

Implementing an Employee Stock Ownership Plan (ESOP) in Vietnam involves several unique considerations, particularly around compliance with local regulations and effective administration of the plan.

Below, we detail the key considerations for implementing an ESOP in Vietnam, focusing on regulatory requirements, types of ESOPs, and the approval process.

1. Key Considerations

Vietnamese Employees Holding Shares of Foreign Parent

Vietnamese employees can hold shares of the foreign parent company under a share incentive plan. This plan must be registered with the State Bank of Vietnam (SBVN) to be effective in Vietnam

Registration with SBVN

The registration with SBVN is crucial to ensure compliance. Without registration, there is a risk of non-compliance when the parent company is publicly listed offshore.

SBVN's Role

The SBVN regulates participation in ESOPs for Vietnamese employees. Offers made to foreign employees do not require SBVN's approval.

Preferential Terms

Vietnamese employees may receive shares or purchase shares on preferential terms. The SBVN restricts remittance of monies abroad even if Vietnamese employees are willing to pay for shares.

2. Regulatory Requirements

Vietnamese employees of Vietnamese subsidiaries may hold shares of the foreign parent company ("Parent") under a share incentive plan. However, to be effective in Vietnam, an offshore share plan that awards the Parent's shares to Vietnamese employees must be registered with the State Bank of Vietnam (SBVN). This ensures compliance and avoids potential issues when the Parent company is publicly listed offshore.

The SBVN oversees participation in ESOPs for Vietnamese employees of a Vietnamese entity ("Local Entity"). The Local Entity can be a corporate entity, representative office, branch, or management office, if it is the employer and is owned directly or indirectly by the Parent company.

V.STEP BY STEP ESOP IMPLEMENTATION

To implement an Employee Stock Ownership Plan (ESOP) in Vietnam, consider the following key steps:

Understand Regulatory Requirements

Vietnamese subsidiaries can allow employees to hold shares of a foreign parent company under a share incentive plan. However, this plan must be registered with the State Bank of Vietnam (SBVN) to be effective.

Eligibility

The local entity, which can be a corporate entity, representative office, branch, or management office, must be the employer and be owned directly or indirectly by the parent company. Only Vietnamese employees of this local entity need to comply with these regulations.

Registration with SBVN

Prepare Documentation: Gather necessary documents such as the share plan details, the parent company's financial statements, and information about the local entity.

Submit Application: Submit the application to SBVN, ensuring all documentation is complete and accurate.

Address Restrictions: Resolve any restrictions related to remittance of monies abroad and other regulatory limitations.

Approval Process

The SBVN evaluates the share plan to ensure it provides clear incentives to local employees. Approval depends on whether the ESOP terms offer significant benefits, such as discounted or free shares.

Implementation of ESOP

Free Shares/Restricted Stock Units: Award employees free shares or the right to acquire free shares

Stock Options/SARs: Provide options or stock appreciation rights at a discounted or market-value exercise price, benefiting employees as the company's share value increases.

Discounted Shares: Offer shares at a discounted price with possible matching shares.

Phantom Shares: Use phantom shares where employees have a conditional right to cash linked to the share value, without holding actual shares

Ongoing Compliance

Quarterly Reporting: File quarterly reports with SBVN, detailing the list of participating employees, inbound and outbound remitted funds, and other relevant data.

Foreign Currency Account: Open and manage a foreign currency account in Vietnam for ESOP transactions.

Address Penalties

Ensure compliance to avoid fines, which can range from VND 20 million to VND 100 million for both the local entity and participating employees if regulations are not followed

Key Considerations

Tax Implications: Understand and comply with local tax laws regarding ESOPs.

Foreign Exchange Regulations: Ensure compliance with foreign exchange rules when transferring funds related to the ESOP.

VI.CONCLUSION

Final Thoughts

Implementing an ESOP in Vietnam involves navigating a complex regulatory environment, but the benefits can be substantial. ESOPs not only provide a powerful incentive for employees but also align their interests with the long-term success of the company. This alignment can drive growth and foster a committed, motivated workforce. Understanding and adhering to local regulations is crucial to leveraging the full potential of ESOPs.

Start Your ESOP Journey with Qapita

Are you ready to unlock the potential of ESOPs for your business in Vietnam? At Qapita, we specialize in helping companies design, implement, and manage ESOPs tailored to their unique needs. With our expertise, you can ensure compliance, maximize employee engagement, and drive your company's growth.

Contact us today to start your ESOP journey and transform your business landscape.