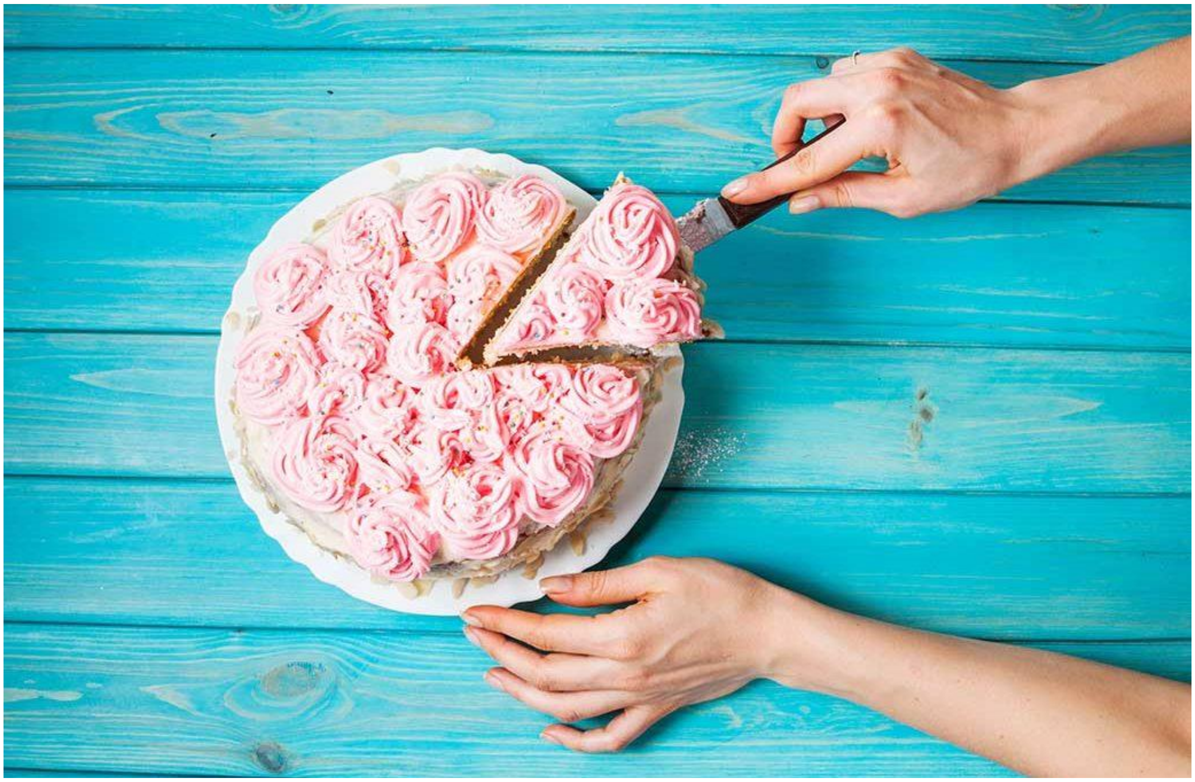
CLIENT NOTE

HOW TO AWARD SHARES TO COMPANY EMPLOYEES UNDER ARMENIAN LAW?



OVERVIEW

Back in 2021, the Armenian legislator introduced amendments in the Law on Joint Stock Companies, allowing them to award shares or options to their employees. Some companies started pondering about the opportunity. In this client note we explain how employee share or option plans can be introduced, and what considerations should be made.

Armenian law allows joint stock companies to award their employees, including managers and other executives, shares of the company. The mechanism is enshrined in Article 41 of the JSC Law, which states that a company can award its employees with company shares or share options either based on a share or share option award plan (ESO Plan) approved by the general meeting of shareholders (GMS) by a ¾ of participating votes (but not less than 2/3 of the total votes of the company) or by the company's charter.

The ESO Plan should at least foresee the acquisition, use, transfer, and sell-back/buyback processes of those shares or options by eligible employees. In case the company has a Board of

Directors/Supervisors, and the GSM authorizes the Board to take decisions regarding the ESO Plan, then the Board can make policy and technical resolutions regarding the plan.

ESO PLAN REQUIREMENTS

First, one should bear in mind that the sum of the face value of the shares being awarded directly (direct award of shares to the employee) or as a result of them exercising their share option rights (vesting) cannot exceed 25% of the charter capital (yes, in Armenia, we still have the notion of charter capital, which basically is the product of multiplying the number of shares with the face value of those shares) or the votes of the company. Moreover, the right of first refusal of non-employee shareholders does not apply to the shares subject to award to employees only.

Second, the shares or options being awarded may be free of charge or have a value less than the face value of the shares being distributed, in case the employees are required to pay for those shares. In either case, the employees have to give their consent for the acquisition of those shares.

Third, the rights attached to the shares to be distributed/awarded to employees shall be the same rights as those attached to other shares in the class of shares. The same rule applies to the face value of employee shares, which cannot be less than the face value of other shares in the same class.

TRANSFER LIMITATIONS

The JSC Law stipulates the right of the company to limit the transfer of the shares or the options to third parties, but not more than 3 years from the day the employee becomes a lawful shareholder (Transfer Limitations).

BUY-BACK/SELL-BACK ISSUES

In case the employment relations are terminated with the employee and the company has imposed Transfer Limitations, within the 3-year period, the company can, but is not obliged to mandatorily repurchase the awarded shares at market value, but not less than the face value of the shares. This right of the company does not apply when the employee is retiring, in which case the employee can keep the awarded shares.

In addition, in case the awarded shares are being forcefully sold for the fulfillment of the employee's obligations to third parties (such as on a court judgment as a result of litigation with 3rd parties), then the company can repurchase those securities at market value, but not less than face value.

Notwithstanding the above, the ESO Plan or the charter of the company may lay out cases, when the company is obliged to repurchase the awarded shares, such as in cases when the employee is incapacitated or when has to leave the company to take care of an ailing parent or another close family member. For the avoidance of doubt, it is up to the company to foresee those special cases of repurchase by the ESO Plan.

INHERITANCE ISSUES

In the event of the death of the employee who has been awarded company shares and in case the company has imposed Transfer Limitations, the heir(s) has the right to demand from the company either to repurchase those shares at market value, but not less than the face value or to swap those shares with other shares of the company is such a swap in envisaged by the charter of the company and such shares are available for swapping.

TAXATION

Unfortunately, the Armenian Tax Code does not give income tax exemptions when employees are awarded shares under Article 41 of the JSC Law. The taxmen view such award as income received by the employee. This means that the employee shall be taxed at 20% as income tax for the received shares, although it is debatable whether the employee shall be taxed for received share options.

HOW CAN WE HELP?

Our team has extensive experience in helping companies with their ESO plans both in corporate and tax matters. So please, do get in touch when you want to get sophisticated and tailored advice.

#esop #shares #options #employees #employeeshares #employeeoptions #companylaw

NOTE: This material is for general information only and is not intended to provide legal advice

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