Extending Stock Incentives to Chinese Employees

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Many multinational companies with operations in China recognize the benefit of extending their stock incentive plans to employees of their subsidiaries in China. Doing so requires that they register the plan with the State Administration of Foreign Exchange (SAFE) under the Operating Procedures for the Administration of Participation by Domestic Individuals in Employee Stock Ownership Plans and Stock Option Plans of Overseas Listed Companies. The regulations impose a registration obligation on listed or public multinationals, but lack clear guidance on the registration obligation of non-public companies. The registration requirement applies to options, restricted stock, RSUs, SARs, ESPPs and other forms of employee stock incentive programs. In order to obtain approval, the multinational must (i) appoint a "Domestic Agent" (typically a subsidiary/affiliate in China) for participating Chinese employees; (ii) establish a special onshore bank account approved by SAFE through which all proceeds towards the purchases and from the sale of shares must be deposited; and (iii) forecast the amount of proceeds to pass through such account each year (there are ongoing reporting requirements).

A registration application is filed with the SAFE office in the location where the multinational wants the plan to be administered for all participating employees of its Chinese subsidiaries. The local SAFE office reviews the application, which may result in requests for clarification and supplementation, before forwarding it to the central SAFE office in Beijing for formal review. It is not unusual for several months to elapse between the filing of the application and the receipt of approval.

Piloting the application through the SAFE registration process requires preparation of a complete and persuasive application (including extensive and accurate translations of documents into Chinese), clear explanations of the issues of particular concern to SAFE (*e.g.*, means of exercise, amounts involved and mechanics of inbound and outbound fund flows), and ongoing liaison with the typically overburdened case officer handling the application in the local SAFE office.

WilmerHale is fully familiar with the application procedure and has guided clients successfully through the registration process, enabling clients' Chinese employees to participate in stock incentive plans in compliance with Chinese government regulations. Failure to register a covered stock incentive plan with SAFE can result in difficulties with respect to the remittance of funds associated with the plan in and out of China.

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