

# How to establish an Employee Share Ownership Plan (ESOP)?

## What is an ESOP?

Employee ownership of a business can be achieved in a variety of ways namely: employees can buy stock directly, be issued shares as a bonus, can receive stock options, or obtain against payment or obtain stock through a profit-sharing plan.

Employee Share Ownership Plans (ESOPs) are very common in the US and as at to date there are more than 8 million employees involved in such plans. Mauritius as an International Financial Centre of high repute is known as a preferred domicile for International Holding Company. Mauritius can also be considered as an alternative jurisdiction for setting up of ESOPs.

## Uses of ESOP

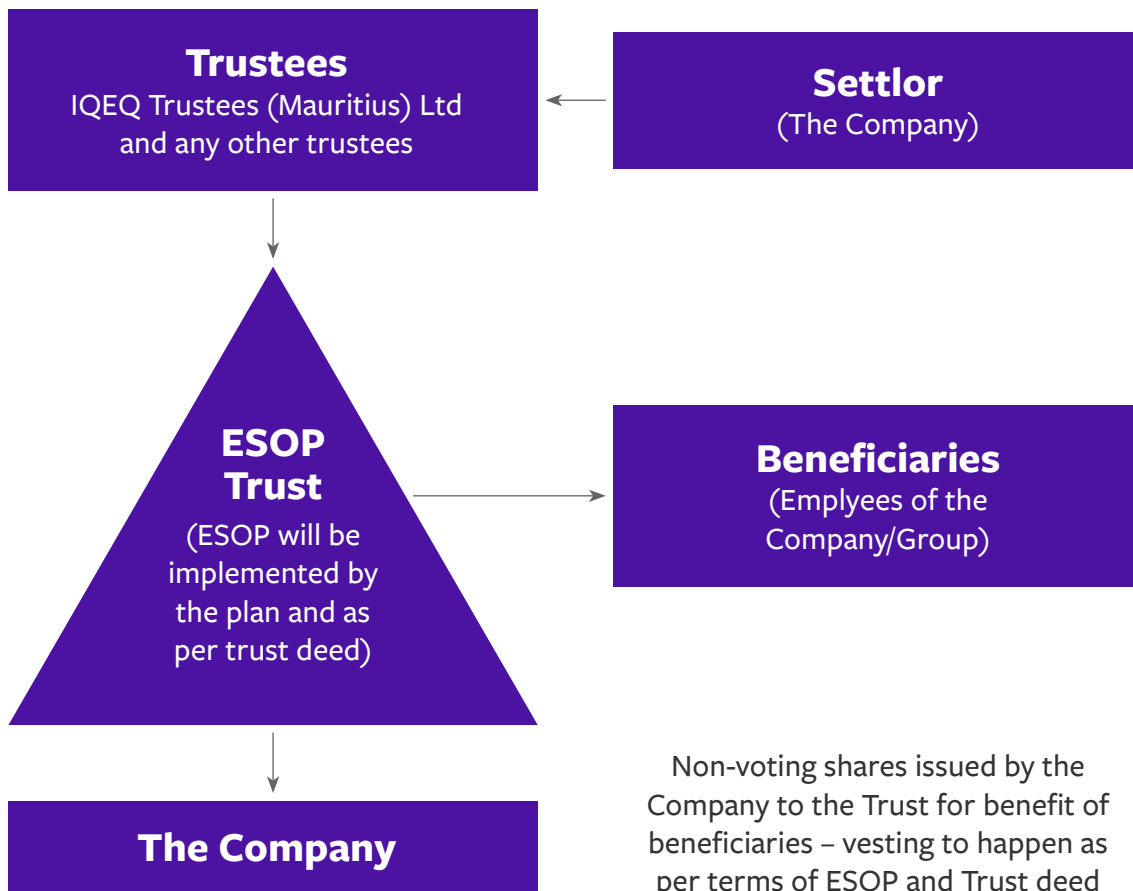
- An ESOP can provide a market for the equity of a retiring owner or any interested major shareholder of a closely held company.
- An ESOP can also provide benefit and job security for employees in the process.
- Owners of privately held companies can use an ESOP to create a ready market for their shares.
- ESOPs are often used in conjunction with employee savings plans. Rather than matching employee savings with cash, the company will match them with stock from an ESOP, often at a higher matching level.
- Other companies have used ESOPs as a technique of corporate finance for a variety of purposes: to finance expansion, make an acquisition, spin off a division, or take a company private.
- ESOP is convenient in advisory and 'people' businesses as a means to incentivise high performance by giving sweat equity.

## ESOP structure

IQ-EQ can structure ESOPs mainly through a trust structure. An ESOP is not a one size fits all product. We discuss the requirements of our clients to structure a tailor-made ESOP that meets the needs of both the employer and the employees.

Few issues that are considered by our ESOP specialist include:

- What is the legal form that best suits the operational as well as tax situation of the parties.
- The way the ESOP is established and the mechanism through which shares of the Holding Company is contributed into the plan.
- The mechanism for exercise of rights to the shares acquired or transferred under the plan.
- The formulation of benefits to employees in a clear, unambiguous manner that gives comfort to both employer and employees.
- The mechanism for admission of employees to the plan.
- The putting in place of the necessary documentation to establish the ESOP.
- Flexibility in the way and time at which the employees in the plan wish to get the benefits.
- Assistance to employees in proper management of the benefits obtained from the ESOP and tax planning thereof.



Non-voting shares issued by the Company to the Trust for benefit of beneficiaries – vesting to happen as per terms of ESOP and Trust deed

## Tax efficiency of ESOP

Tax efficiency of an ESOP plan is important. Ideally the plan is structured in such a way that:

- Employees are not taxed until the time they enjoy the final benefits from the plan, i.e., they exercise their option to acquire the shares. Foreign employees not performing their duties in Mauritius should not be taxed in Mauritius.
- Any distribution made by a trust to a beneficiary is deemed to be a dividend to the beneficiary. Dividend is exempt from tax in Mauritius.
- On disposal of the shares, there is no capital gain tax in Mauritius.
- The benefits of the plan are ideally capable of being reinvested with no or minimal tax burden.

## Regulatory environment

### Legislation

The legislation governing the law of trust in Mauritius is the Trust Act 2001. The Trust Act 2001 provides for various types of Trusts which may be set up namely: charitable, discretionary, purpose and trading trusts. Flexibility is provided under the Trust Act in determining the applicable governing law.

### Regulatory Body

The Financial Services Commission (FSC) established under the Financial Services Act 2007, act as a regulator for the financial services sector in Mauritius. Those seeking to set up a GBL1 company will have to submit their application to the FSC. The FSC consequently licenses, regulates and supervises financial institutions in Mauritius.

The Companies Division has four main functions:

- The incorporation, registration and striking-off of companies
- The registration of documents that must be filed under the Companies Act 2001
- The provision of company information to the public
- The enforcement of compliance with the legal requirements

## Why Mauritius?

Politically stable and with a booming economy, Mauritius has the prerequisite qualities to be chosen as an attractive jurisdiction to establish an ESOP for those investors having in mind the best interest of their employees. With proper expertise and assistance, implementing an ESOP can be achieved thus making an ESOP not overly complicated or expensive.

By subscribing to an ESOP Plan, employees are able to acquire wealth in an offshore trust with certain tax benefits. Through the ESOP, the Company shall encourage higher engagement from its employees and ensures participation of its employees in line with its strategies and expansion and hence may (if allowed by their domestic tax law) not be taxed thereon in their country of residence.

Thus, with adequate tax advice, the design and implementation of an ESOP can be achieved without jeopardizing the company or the employees from suffering any adverse tax consequences and in the process, the benefits of an ESOP are fully realized.

## Key contacts in Mauritius



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