

The Benefits of an Employee Ownership Trust (EOT)

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By **Paul Webb**, 11th July 2023

We are frequently asked by our clients about the often-difficult topic of exit and succession planning.

This gives rise to several practical issues, especially where a trade sale is not likely, or the existing management team are perhaps not in a position to be able to raise sufficient funds to affect a traditional "Management Buy Out".

One Solution that is often overlooked is an Employee Ownership Trust (EOT)

An EOT can be used to acquire between 51% and 100% of a trading company's shares which are then held on trust for the benefit of all the company's employees, on the same terms.

Unlike traditional employee share schemes, which give rise to direct employee ownership, the EOT allows for indirect employee ownership overseen by selected employee Trustees.

EOT's have been shown to promote better business performance, greater commitment, and productivity from employees with increased staff loyalty, lower staff turnover and absenteeism. They also allow staff members to benefit from being involved in the management and future direction of the business.

Benefits to the Shareholder

- The sale by the existing business owner of over 51% of his/her shares in the company to a qualifying EOT, would be Capital Gains Tax (CGT) and Inheritance Tax (IHT) free. This can prove to be a valuable relief given that the Business Asset Disposal relief limit for the reduced 10% rate of CGT is only £1 million;
- A market is created for the shares that might not otherwise exist;
- Unlike in a liquidation situation (which is often the only choice for small business owners to realise the value of the business), the company can continue to operate, and the shareholders and employees can still be part of that business;

- Typically, the sale of shares in a company to an EOT is funded by a mixture of existing cash, from within the company, and external loan instruments;
- It avoids the need for often complex and expensive negotiations when selling to a third party.

Benefits to the Company and Employees

- A trading company owned by an EOT is able to pay cash bonuses of up to £3,600 per annum to all employees (on a 'same terms' basis);
- These bonuses will be tax-free but will be subject to National Insurance Contributions (NIC's);
- The company gets corporation tax relief on these tax-free bonuses;
- There are benefits in terms of increased staff motivation and job retention, as set out above.

Summary and Additional Information

An EOT can provide a tax-beneficial way for shareholders to realise value and to involve employees in the company that they work for, although the structuring and funding of an EOT requires careful consideration.

If you would like to find out more about how an EOT may benefit you and your business, please contact us: advice.uk@dixcart.com.