Employee Ownership Trusts

Selling your company to an employee ownership trust (EOT) offers an alternative to a sale to a trade buyer or private equity house, an IPO or a management buyout.

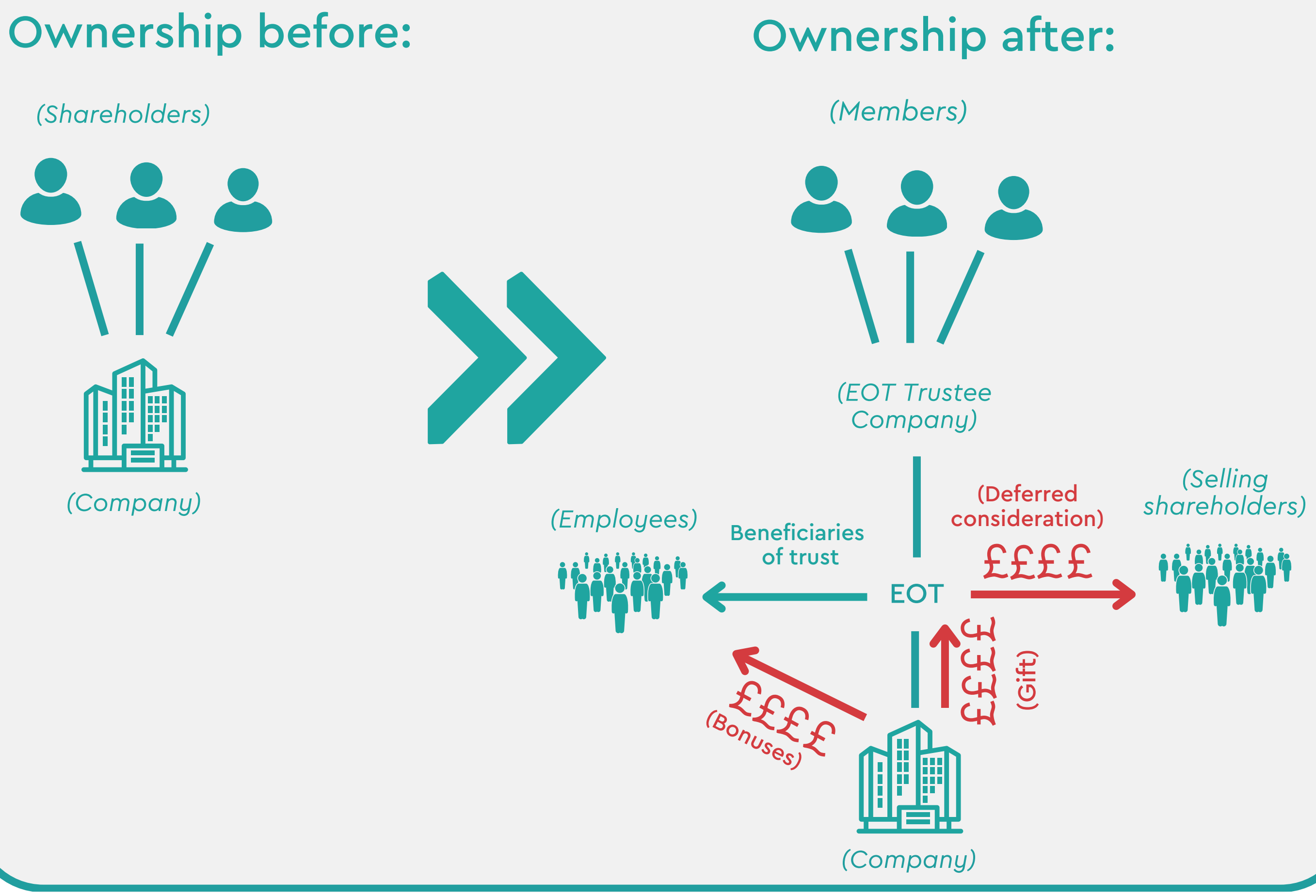
An EOT is a trust set up for the benefit of a company's employees. Following formation, the EOT buys the company. Perhaps the most famous example of an employee owned business is John Lewis.

The original shareholders of the company sell their shares to the EOT and after the sale the majority shareholder (perhaps the only shareholder) of the company is the EOT. The employees can then begin to share in the company's success as indirect owners of the company, which is a great way to incentivise them. Sale proceeds are typically funded from cash gifts by the company to the EOT, which the EOT in turn pays on to the selling shareholders.

There are significant advantages and some disadvantages for you when comparing a sale to an EOT to alternative sale structures, some of which are set out below:

Advantages	Disadvantages
If you are looking to sell, and want to pass the business to your employees, an EOT provides a way to do this. EOT sales are well regarded, can often generate positive PR and do not require management to take on personal debt (when compared to an MBO).	Selling shareholders are typically paid out over time, from company profits. This will often mean it takes several years to extract 100% of the sale proceeds, and prevents sellers making an immediate clean break (the company needs to continue to succeed while it funds the sale proceeds).
Provided certain conditions are met, selling shareholders pay no tax on sale proceeds.	Employees won't immediately see the full benefit of their ownership, because of the need to fund the share sale.
Provided certain conditions are met, the company can pay each employee a bonus (up to £3,600 each year) free of income tax.	The process is slightly more complicated compared to a standard share sale. A professional valuation is highly recommended to support the sale price. The trust needs creating and administering going forwards.
Employees are incentivised to work harder and grow the business, because the company now (largely) belongs to them (via the trust).	Control of the company shifts from selling shareholders (often the founders) to the EOT.

How does an EOT work?



If an EOT is an attractive option, there are certain qualifying conditions the company and the sale must meet, including:

- the company must be a trading company (not, for example, a property investment company).
- the EOT must obtain control of the company (typically meaning more than half the company's shares are sold to it). The EOT must retain that control.
- deferred consideration cannot be protected to the same extent it could on a standard sale.
- the trust must benefit all employees equally, subject to limited flexibility (such as allowing for a period of time before new joiners benefit).
- broadly, the company needs a reasonable number of employees unconnected to the shareholders, meaning companies with a very small number of employees (or family companies) may not always qualify.

The costs of setting up an EOT and selling your company to it will vary depending on the specifics and complexities of your transaction. Do get in touch with our expert Matt Spencer to discuss your specific requirements for an EOT, and he can provide precise information on the costs involved.

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