TRIDENT TAX

Our advice is defined by our knowledge and refined by our experience.

Factsheet

September 2024

Understanding Employee Ownership Trusts (EOTs): Unlocking Benefits

This factsheet provides an overview of Employee Ownership Trusts (EOTs), designed to inform business owners' considering selling their company to benefit their employees. Compiled by Trident Tax's experts, it covers key aspects of EOTs, their tax implications, and practical considerations.

For tailored UK tax advice specific to your circumstances, we strongly recommend consulting our experts.

EOT Overview

Definition: An EOT is a legal entity set up to allow a business to be owned and run for the benefit of its employees.

Purpose: EOTs are often used when an owner-manager of a private trading company wants to retire and transfer ownership to the employees rather than a trade purchaser.

Tax Implications: Specific tax reliefs are available to encourage employee ownership through EOTs.

When Would an EOT Be Used?

Retirement	When an owner wants to retire and sell a controlling shareholding but does not want to give the shares to family or sell to a trade buyer.
Funding Challenges	EOTs can address difficulties in management borrowing enough to pay for the shares upfront and cover the seller's tax liability.
Deferred Payments	The EOT can buy shares at market value, with payments funded over time by the business's cash and profits.

The Owners Position

Continued Involvement: The seller can remain a shareholder and director, although not as a controlling shareholder.

Trustee Restrictions: Proposed legislation prevents the seller from being the sole or majority trustee of the EOT.

Capital Gains Tax Relief on EOT Sales

- **Tax-Free Disposal**: If legislative conditions are met, the gain realised from the sale to an EOT is taxed at 0%, making the disposal tax-free.
- **Deferred Payments**: Payments over a long period can be documented as loan notes issued by the trustees, mitigating cash flow issues.

Income Tax Considerations

Trading Company Requirement	The company must be a trading company or the holding company of a trading group. This means that there is a restriction on the amount of cash (other than working capital) that can be held by the company.
Pre-Sale Dividend	A pre-sale dividend may need to be paid, on which the owner would pay income tax.
Director's Loan	If the seller has a director's loan from the company, it must be cleared, possibly via a taxable dividend.
HMRC Clearance	It is usual to seek HMRC clearance to ensure none of the sale consideration is taxed as dividends.
Interest on Deferred Payments	Trustees can pay interest on deferred payments, which is subject to income tax.

Funding Payments to the Seller

Trustees' Obligations: Trustees owe money to the seller and hold shares in the trading company.

Funding Source: Payments to the seller are funded by the company's contributions to the trust, which are not deductible for corporation tax purposes.

Market Value Condition: Payments must not exceed the open market value of the shares for the tax treatment to apply.

Practicalities of the Sale

- **Share Valuation**: Establishing the value of the shares to be acquired by the EOT is crucial.
- **Documentation**: The sale process should be straightforward, avoiding complex documentation.
- **Trustee Appointment**: Trustees need to be appointed, and professional co-trustees may be preferred to ensure legal responsibilities are met.
- **Sale Process Efficiency**: The process is typically quick and non-adversarial, as involved parties already know the business.

Inheritance Tax Considerations

Exposure: The seller may face new inheritance tax exposure, as loan notes do not qualify for 100% relief.

Family Trusts: Transfers of shares into family trusts prior to the sale may be considered to manage this exposure.

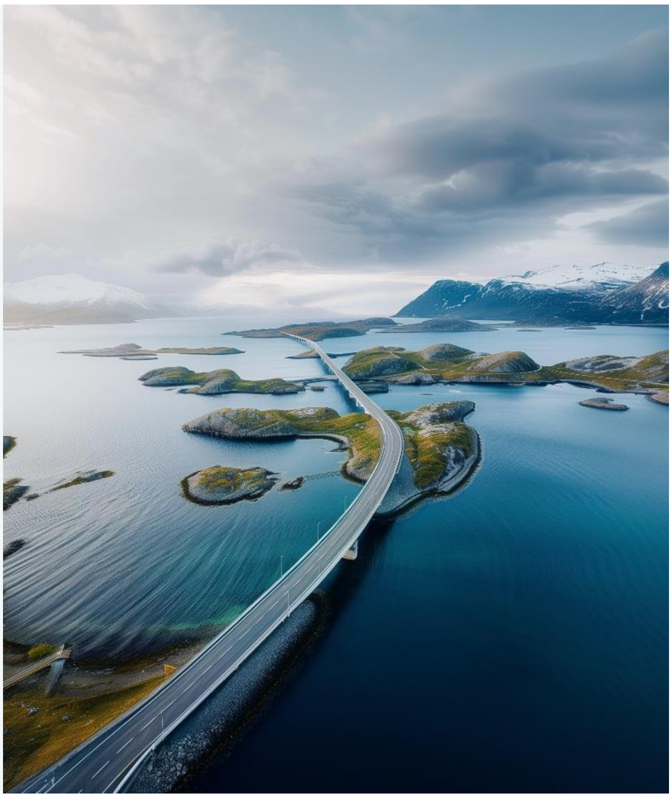
Payments to Employees

- **Equal Benefit**: The EOT must benefit all employees equally.
- **Tax-Free Payments**: The EOT can make tax-free payments of up to £3,600 per year to each employee.

Achieve Your Goals with Trident Tax's Expert EOT Guidance

At Trident Tax, we specialise in providing tailored UK tax advice on EOTs, helping you navigate the complexities and unlock the benefits of employee ownership.

Whether you need assistance with the implementation, compliance, or strategic planning for your EOT, our experts are here to guide you.



TRIDENT TAX

Simplify your taxes, amplify your success with Trident Tax's expert guidance and trusted resolutions.

+44 (0)207 952 2921
admin@tridenttax.com
www.tridenttax.com