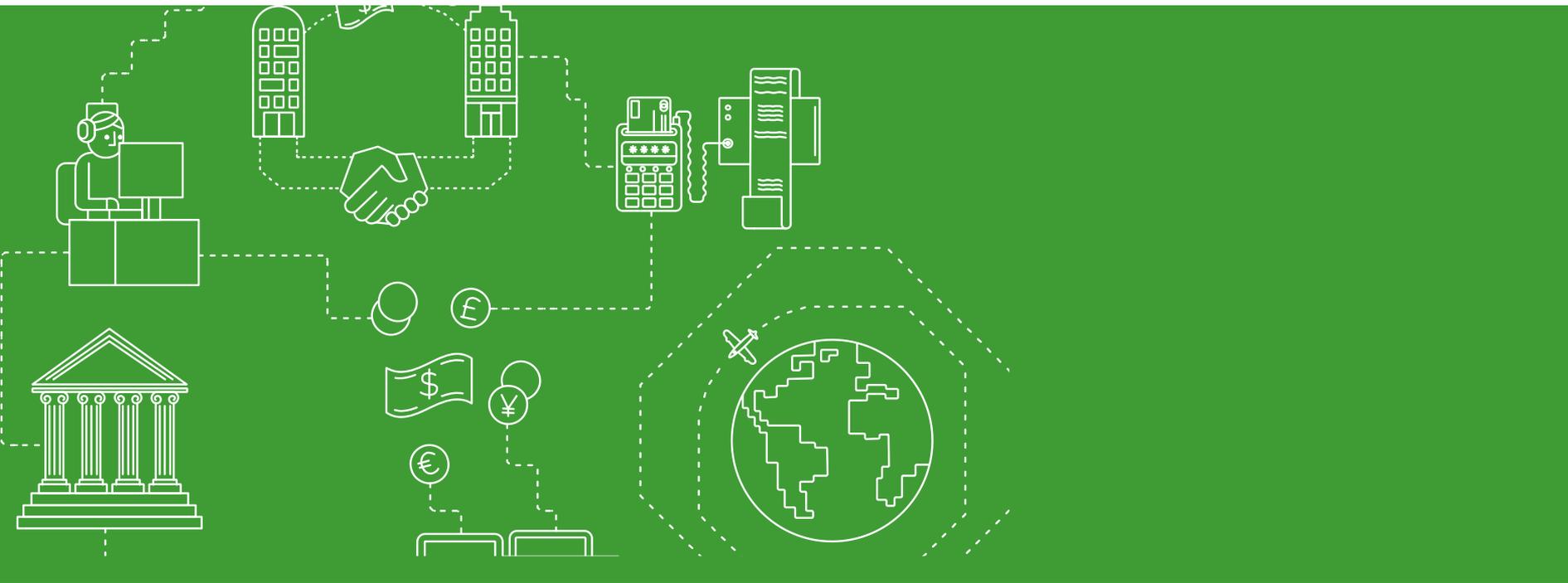


THE POWER OF BEING UNDERSTOOD

AUDIT | TAX | CONSULTING



EMPLOYEE OWNERSHIP TRUSTS (EOTS): STRUCTURING, FUNDING - OVERCOMING SOME OF THE DIFFICULTIES



Boards too should remain open to potential changes of corporate form – the choice should not simply be a binary one of going public through a listing on the stock market or remaining private..... A recent example of what can be done is that of Julian Richer, founder of the audio and entertainment chain Richer Sounds, who has handed control of the business to staff

Opinion The FT View
The Editorial Board

The Basics - set up

Company establishes EOT, appointing trustees, amending articles of association to match and creating governance structure (Employee Council or similar).

Trustee agrees in principle to buy shares (valuation agreed, terms of SPA, structures funding arrangements).

Sale completes and EOT trustees acquire shares and control of the Company and vendor(s) receive consideration.

The Basics – on going

EOT trustees pay vendors for consideration in instalments funded by contributions from the company.

Company repays any third party debt.

Surplus profits used to build up working capital/reserves, reinvestment, distributions to employees through bonus.

The Basics – future sale

EOT trustees may receive an offer for all the shares in the Company.

If the sale is during the tax year of original transfers or the following tax year, a sale removes tax relief for the vendors. If in subsequent tax years, capital gains fall on the EOT trustees.

If the sale happens, EOT makes a capital gain and distributions to eligible employees are taxed as employment income.

Qualifying as an EOT



Employee Ownership Trust Requirements

Trading Requirement section 236I TCGA

- Company or Group – taken together – trading activities ‘to a substantial extent’
- Cash and non-trading assets on the balance sheet – clearance but ‘at the time of disposal and continues to meet that requirement for the remainder of the tax year in which that time falls’
- Pre-transaction restructuring

Employee Ownership Trust Requirements

All Employee Benefit Requirement section 236J

- All employees – all employees and officeholders
- Except ‘excluded participator’ – 5% or more during 10 years before EOT
 - Family members...direct ownership – domestic, family or personal – s421B(3)(b)?
 - EMI/SIP
- No loans or sub-trusts
- ‘same terms’

Employee Ownership Trust Requirements

Equality Requirement section 236K

- All employees – but can effectively exclude those without 12 months continuous service
- Technically a discretionary trust but minimal discretion
- ‘same terms’ – length of service, remuneration, hours worked
- Only really relevant if there is a distribution – why distribute?

Employee Ownership Trust Requirements

Controlling Interest Requirement section 236M

- Trustees
 - hold >50% ordinary share capital and have majority of votes
 - What about golden share retained by vendor to stop inappropriate sale?
 - entitled to > 50% of profits available for distribution
 - What if profits used to repay loans or pay off vendors?
 - Waive dividends – no problem section 236T(3)

Employee Ownership Trust Requirements

Controlling Interest Requirement section 236M

- Trustees
 - entitled to >50% on a winding up
 - What about charges – probably ok section 236T(4)?
- No agreements, instruments affecting constitution/management to prevent control
 - Board still has management responsibilities but corporate governance structure vital
- Terms of loan notes – Deferred consideration

Employee Ownership Trust Requirements

Controlling Interest Requirement section 236M

- Interaction with Accounting Principles:
 - Do the trustees control the company or does the company control the trustees?
 - Who has the power to appoint the trustees?
 - If trustee is a company – limited by guarantee – who are the members?
 - Accounting requirement to consolidate

Employee Ownership Trust Requirements

Limited Participation Requirements s 236N and s 454 CTA 2010

- At no time in the 12 months ending with the 'disposal'
 - When the claimant was a participator did the participation fraction exceed $2/5$
 - And did not exceed $2/5$ in the remainder of the tax year of disposal

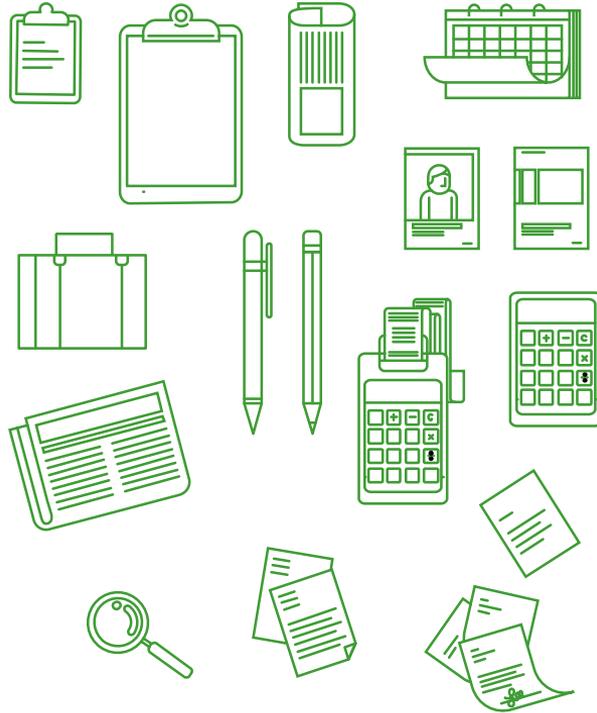
Participation fraction is

$$\frac{\text{Persons both (1) 5\% participators and (2) employees* (plus connected employees*)}}{\text{Employees in Group}}$$

Disregard if no more than 6 months for reasons outside the control of the trustees

* Including officeholders.

Running the EOT



Employee Ownership Trust Bonus

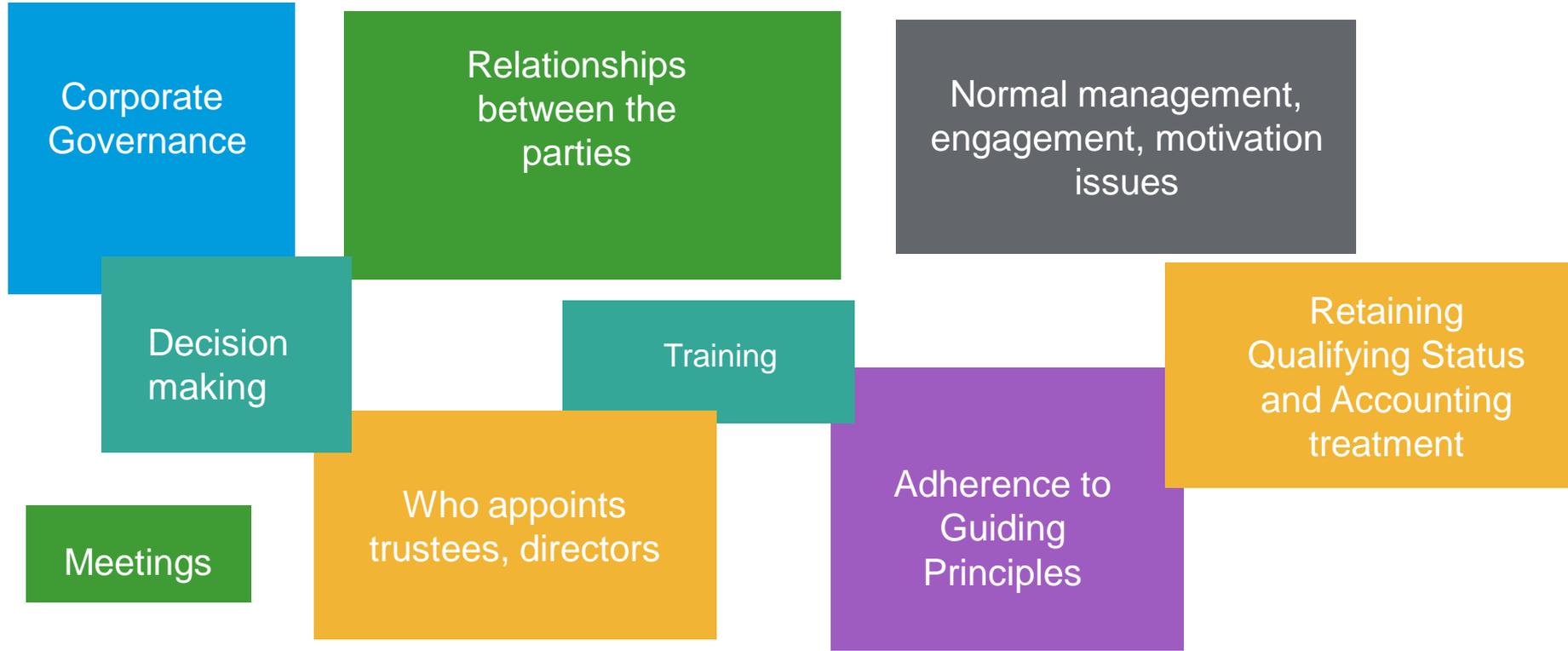
Section 412A ITEPA

- Need a plan
- Paid by the employer
- All employee requirement and equality principle
- Limited Participation Requirement

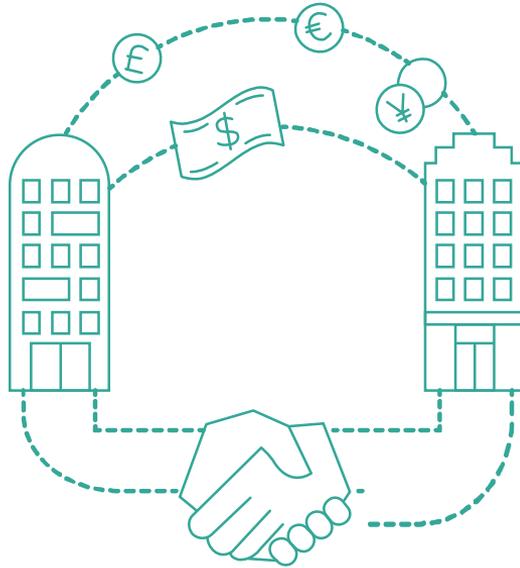
BUT

- No Excluded Participator provision
- Cannot reference a period before an EOT

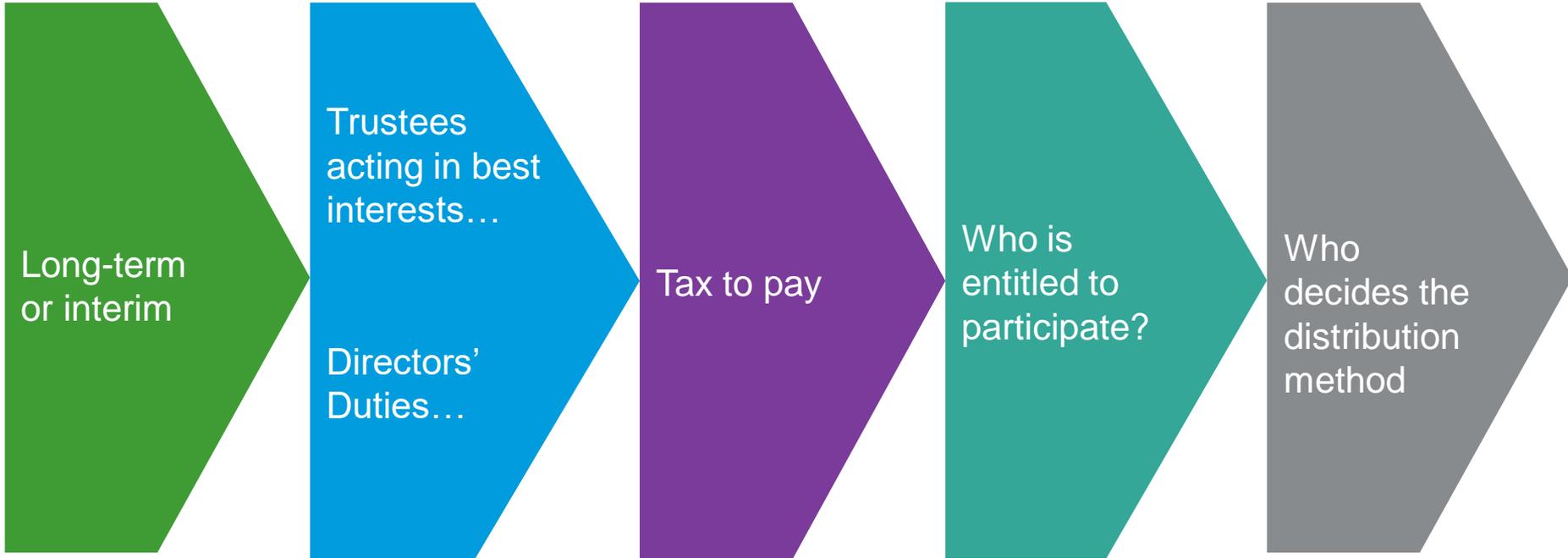
Corporate Governance



Winding up the EOT



Winding up the EOT



THANK YOU