Spotlight on the Employee-Ownership Trusts Working Group

Briefings



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The Employee-Ownership Trusts (EOT) Working Group is made up of CIOT members who have an interest in this fairly niche area of practice.

With nearly 1,800 employee-owned businesses in the UK, more and more are utilising EOTs as a way of giving their employees an indirect stake in the business, whether it be for retention, motivation or both. It is also a useful way for an owner to retire from the business safe in the knowledge that it will continue as a going concern in the hands of their employees and trustees, rather than those of an unknown third party.

John Lewis is perhaps the best known example of an EOT-owned business, but others include Go Ape, Riverford Organic Farmers, Richer Sounds, Stephens Scown Solicitors and Aardman Animations.

The working group is in regular contact with the Employee Ownership Association, which provides a valuable insight into the sentiments and concerns of EOT-owned businesses. However, there have been some concerns over the years that the tax benefits for business owners might be the primary motive for an EOT's use, rather than any benevolence towards employees.

When a business owner transfers at least 51% of their company's shareholding into an EOT, the disposal is treated as being 'no-gain/no-loss'; i.e. it is a tax-free and tax-neutral transfer, which would otherwise be fully chargeable to capital gains tax (CGT). Only when the trustees subsequently sell the business to a third party would CGT become an issue – unless the EOT were located outside the UK, in which case the disposal would be outside the scope of UK CGT.

HMRC believes that this is a significant loophole. In a 2023 consultation, 'Taxation of Employee Ownership Trusts and Employee Benefit Trusts' (July to September 2023), it proposed that only UK-based EOTs can attract the CGT relief for business owners. This follows on from a submission made by the CIOT in 'Autumn Budget 2021 representation on enhancement and anti-abuse measures, funding and other tax issues' (see www.tax.org.uk/ref833).

The 2023 consultation comprehensively addresses the tax rules concerning EOTs for the first time since their introduction in 2014. Much of the working group's time of late has been taken up with this consultation. Besides the use of offshore EOTs, the consultation also addressed the issue of former business owners subsequently controlling the EOT trustee board – thus effectively placing themselves back in charge of the business after benefiting from tax relief upon disposal.

Despite warning against new rules being over-prescriptive and burdensome, the CIOT does support further moves to ensure that EOTs are being used for what they were intended (i.e. as vehicles for long-term employee participation with tax reliefs as an incentive), rather than as an instrument for short-term tax savings.

The CIOT also expressed support for other changes such as:

- removing the need for HMRC clearances upon the establishment and funding of an EOT;
- increasing the £3,600 employee tax-free bonus limit to take account of ten years' inflation and to make those payments free from National Insurance, as well as income tax; and

- more ongoing checks to ensure that EOTs are being operated in accordance with the rules providing the tax relief.

We are still awaiting the release of draft legislation following the consultation’s conclusion.