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Welcome to this monthly series for business owners, where I aim to demystify the corporate market and highlight trends in a non-technical manner.

For a further discussion on any of these topics, please contact me on:

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Alternative Exits for Business Owners

Many business owners are keen to move on with their lives, after a tough few years. Sale or Private Equity (PE) can be the answer, but if your business is not in a “hot” sector, or the growth profile does not attract investors, what are the options?

EOTs (Employee Ownership Trusts)

Increasingly popular, replacing the more traditional management buyout.

Two main reasons these are popular:

- (i) builds loyalty, giving employees a long-term ownership stake (through an employee trust).
- (ii) allows founder(s) to de-risk/exit, with zero rate Capital Gains Tax (CGT).

EOT's can use borrowed money, but are often financed with profits/cash reserves, combined with future profits (deferred consideration). A founder could sell 50% to an EOT, then if the business continues to grow, seek a full exit in due course. It is not certain though whether the currently attractive tax rate will survive an election. The risk with an EOT is that it will often include an extended deferred consideration period; if the business slows down, or loses momentum, the company may be unable to pay. Whilst payment arrangements can be adjusted, this may be one reason for founders to retain a controlling interest, until satisfied that the management team is ready to take the reins.

MBOs (Management Buyouts)

Financed by a founder selling some/all shares to a key leadership team, with the price paid from retained profits/borrowing.

Founders will typically sell all/some shares, supported by bank debt, and sometimes a deferred payment. Key managers are normally asked to invest personally (“skin in the game”), with the rule of thumb being one year’s salary.

Sellers will receive CGT tax relief, through Business Asset Disposal Relief (10% first £1m, and 20% thereafter). So, MBO's may be less attractive than an EOT from a CGT perspective, but achieving CGT treatment at these rates, remains much more attractive than the other options of extracting reserves from a business (as income).

In Issues 1 and 2 of Corporate Commentary, I covered Current Trends in the M&A Market and Sale or PE? Which will Deliver Best Value, respectively. Both can be found at: <https://www.dmhstallard.com/news-insights>

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