



Employee Ownership Trusts (EOTs)

Employee Ownership Trusts (EOTs) allow business owners to transfer a controlling interest in their businesses to the employees in return for paying lower amounts of capital gains tax (CGT). Significant changes to the EOT rules were announced in both the Autumn Budget 2024 (taking effect from 30 October 2024) and the Autumn Budget 2025 (taking effect from 26 November 2025). The updated rules are outlined below.

What is an Employee Ownership Trust (EOT)?

An Employee Ownership Trust is a specific type of Employee Benefit Trust (EBT) used to reward employees and encourage employee engagement. An EOT provides an indirect form of employee ownership whereby the trust holds a controlling stake in a company on behalf of all the company's employees.

Where a shareholder sells a controlling stake in their business to an EOT and qualifying conditions are met there can be significant tax advantages. For disposals to an EOT made on or after 26 November 2025, 50% of the gain is potentially exempt from CGT and 50% is chargeable. The chargeable part doesn't qualify for [Business Asset Disposal Relief \(BADR\)](#) or [Investors' Relief](#). The exempt 50% is deducted from the trustees' tax acquisition cost of the shares. With the main rate of CGT currently being 24%, the current effective rate of CGT on a gain arising from a qualifying sale of shares to an EOT would be 12%.

For disposals completed before 26 November 2025, 100% of the gain was potentially exempt from CGT. This can make EOTs useful in succession planning as an alternative to an external sale, a private equity backed buy-out or a management buy-out (MBO).

How do Employee Ownership Trusts work?

1. A qualifying EOT is set up.
2. The business owners sell more than 50% of the current share capital to the EOT for market value (using an independent valuation). Part of the purchase price might be left outstanding as a debt owed by the EOT to the selling shareholders (or an initial payment may be made using third-party debt finance).

3. The company uses future profits to make contributions to the EOT and the EOT uses these payments to repay the outstanding purchase price and associated costs. As with any deferred consideration structure, repayment depends on the company continuing to generate sufficient profits.

Updated EOT rules: Autumn Budget 2024

From 30 October 2024, HMRC has taken the view that contributions a company makes to an EOT are to be treated as distributions. This represents a change from HMRC's previous approach and the correct tax treatment is not free from doubt.

There is however a specific claimable tax relief for EOTs. Where contributions are made by a company to fund an EOT's qualifying acquisition costs (for example, payments for the shares, repayment of acquisition borrowing, interest at a reasonable commercial rate, valuation fees, stamp duty, stamp duty reserve tax and other reasonable expenses directly connected with the acquisition), those contributions should not be brought into tax. Contributions made by companies to EOTs to fund other costs (such as ongoing ownership costs) are outside this relief and may therefore be treated as taxable distributions in line with HMRC's stated view. Given the degree of uncertainty and HMRC's current stance, it's important to document the purpose of each payment carefully and ensure terms (including any interest) are commercial. Specific advice may be required to support the position taken and any claim for relief. It should be noted that this relief does not apply automatically and must be claimed by the EOT.

Qualifying conditions for EOT tax relief

Determining the price the EOT must pay for the shares is important – setting this too high risks the trustees being found to be in breach of their duty of care towards the employees as beneficiaries of the trust and might result in failure to meet the key conditions for the CGT exemption to apply.

These are the key conditions that must be met for the selling shareholders to benefit from the EOT CGT exemption:

1. The trustees of the EOT must be UK tax resident.
2. The company must be a trading company or the principal company of a trading group.

3. All employees must be entitled to be beneficiaries of the EOT, subject to a qualifying period of up to one year and any benefits must be provided on the same terms to all eligible employees (amounts can differ by objective factors such as pay, length of service or hours worked).
4. The EOT must not hold a controlling interest in the company (ie more than 50% of ordinary share capital and voting rights, profits available for distribution and 50% of the assets on winding up) before the tax year of the transfer and must hold a controlling interest at the end of the tax year in which the transfer takes place.
5. The trustees of the EOT must take reasonable steps to ensure the consideration doesn't exceed market value, typically by obtaining an independent professional valuation they can rely on.
6. The number of continuing shareholders (and any other 5% participators) who are directors, employees or persons connected with them must not be more than 40% of the total number of employees of the company or group.
7. Exiting shareholders (or persons connected with them) must not retain control of the company post-sale by controlling the EOT.

If the EOT conditions are breached within four years of the end of the tax year in which the disposal was made, relief will be withdrawn and the exiting shareholders will be assessed to CGT as if the claim hadn't been made.

Advantages of selling your business to an EOT

Shares can be sold to the EOT at their full market value. For disposals on or after 26 November 2025, 50% of the gain is potentially exempt and 50% is chargeable to CGT (with no BADR or Investors' Relief on the chargeable part), and the exempt portion reduces the trustees' tax acquisition cost. For earlier disposals, 100% relief may apply. This effective CGT rate of 12% compares to paying CGT at 18% from 6 April 2026 (14% for the 2025-26 tax year) on the first £1 million of lifetime capital gains that qualify for BADR or 24% on gains that do not qualify for BADR.

The sale should also be free of income tax and inheritance tax, subject to certain conditions being met. It is recommended that advance statutory HMRC tax clearance is sought to obtain certainty that HMRC would not invoke the transactions in securities anti-avoidance rules (although, following HMRC's change of view from 30 October 2024, it is no longer necessary to seek separate non-statutory HMRC tax clearance in relation to whether EOT contributions are taxable distributions).

The EOT only needs to buy a controlling interest, so not all shareholders have to sell their shares to the EOT. While shareholders could, in theory, dispose of only enough of their shareholding for the EOT to obtain control, this might be unlikely to occur in practice as the CGT exemption

might not apply to any later disposal. The directors who have sold their shareholding can stay in post after the sale and can continue to receive a salary for their director's duties (but can no longer control the company).

By selling internally, the shareholders don't need to find an external investor and time and fees can often be saved on the transaction (albeit the business must be suited to employee ownership).

Advantages of an EOT for employees

Employees can gain an interest in the company without using their own funds. The employees might feel more engaged as they have a stake in the business they're working for.

Employees can be paid tax-free bonuses of up to £3,600 a year provided these are paid to all qualifying employees on the same terms. This bonus is, however, subject to NIC. These are cash bonuses, not dividends, so they can be paid without the company having to make a profit or have distributable reserves. The only factors that may be used to determine the award are:

- The employee's remuneration
- The employee's length of service
- Hours worked by the employee

This allows full-time employees to receive more than part-time employees, for example, without losing the tax-free nature of the payment.

How we can help

Using an Employee Ownership Trust is one of several ways a business owner can exit their business. This route is becoming more popular, not least because of the tax advantages available given the reduction in the lifetime allowance for Business Asset Disposal Relief. Whether it's the right option for you will depend on several factors, including whether your business is suited to employee ownership. For more on the options available to you for exiting your business, see [Business succession planning](#)

We can help you decide whether using an Employee Ownership Trust is the right option for you and can advise on all aspects of implementing such a sale. To find out more, please get in touch with your usual Saffery contact, or get in touch with Sean Watts.



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