Navigating the complexity of **employee benefit trusts**

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Introduction

Retention and recruitment of key staff remain major challenges for many businesses.

For that reason, effective employee incentive plans – commonly linked to the employing company's shares – are used to engage and reward staff for strong performance, longevity of service and loyalty. Share based incentives are intended to align the interests of employees with those of shareholders – essentially, employees are less likely to leave a business they own a part of.

Incentive plans are a key element of an employer's reward package, so companies should have a handle on how to manage them properly – this is often where employee benefit trusts (EBTs) come in.

An EBT isn't an incentive plan; it is commonly the vehicle that holds assets to satisfy incentive awards. A well-run EBT ensures that shares, cash or other assets can be independently held, administered and distributed to plan participants. EBTs are a tax-efficient way of ensuring that incentive plans provide maximum value for employees and businesses.

EBTs, however, need to be set up and administered professionally to ensure they continue to meet the needs of businesses and beneficiaries. Companies with an established EBT need to ensure it still does everything they want it to do.

Considerations when establishing or reviewing an EBT

In this guide, we'll describe what EBTs are, what they do and how you can make the best of them, whether you're thinking of setting one up or you have one already. We'll cover:

EBT basics

What they are and their advantages when it comes to facilitating employee incentive plans.

EBT use cases

Three company types and how they tend to use EBTs.

Setting up an EBT

What to consider before committing to an EBT, how to choose a trustee and what the setup process involves.

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How to make sure your EBT is meeting your needs.

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The importance of location and automation on EBT performance.

EBT partnerships

How to choose a third party trustee for your EBT.

SECTION 1

Employee benefit trusts: the basics

What is an employee benefit trust (EBT)?

An EBT is a discretionary trust, usually set up by a corporate settlor in conjunction with employee incentive plans, to deliver reward to the beneficiaries of the trust – namely the company's employees. The trust is funded by the company to hold and distribute assets to satisfy awards granted to employees. The beneficial class of the trust usually includes employees of the settlor company's group, as well as former employees and their relatives or dependents. The settlor company is excluded from the beneficial class, ensuring that assets are applied for the benefit of employees, independent of the company.

What's the main purpose of an EBT?

The main purpose of the EBT is to provide benefit to the underlying beneficiaries – to reward, and incentivise employees of the company's group – usually by delivering shares or other assets as part of an employee incentive plan. The exact nature of the incentive plan will differ according to the type of business setting it up, who it wants to reward and how. Here are some questions to ask:

- Is the plan intended to reward all staff, a particular tier of staff, or a smaller number of founders or key executives?
- Is it intended to reward performance or longevity – or both?
- Will participants be required to invest personally, or is the plan intended to supply reward?
- Will the plan be linked to the company's shares, funds or perhaps cash?
- Do specific shareholding or share retention requirements apply to the company's employees?

Regardless of the plan requirements, an EBT is a flexible way to administer an employee incentive plan – or several plans at once. An EBT is fundamentally an efficient vehicle for the smooth operation of incentive plans designed to motivate and engage staff, helping a company's recruitment, retention and incentivisation.

What are the benefits of an EBT?

- EBTs are flexible. An EBT can be used to manage many kinds of employee incentive plan, tailored to the needs of the company. It can be used to fund and administer several plans at once.
- A properly administered EBT can be a tax-efficient way of rewarding employees – assets held in an offshore trust are usually sheltered from UK capital gains tax.
- An EBT is distinct from the settlor company, giving peace of mind to beneficiaries that assets are held securely for their benefit.
- Most EBTs are administered by an independent, third-party trustee who has a fiduciary duty to act in the best interests of beneficiaries – giving comfort to beneficiaries that their interests are looked after, further enhancing the attractiveness of the incentive plan.

SECTION 2

EBT use cases

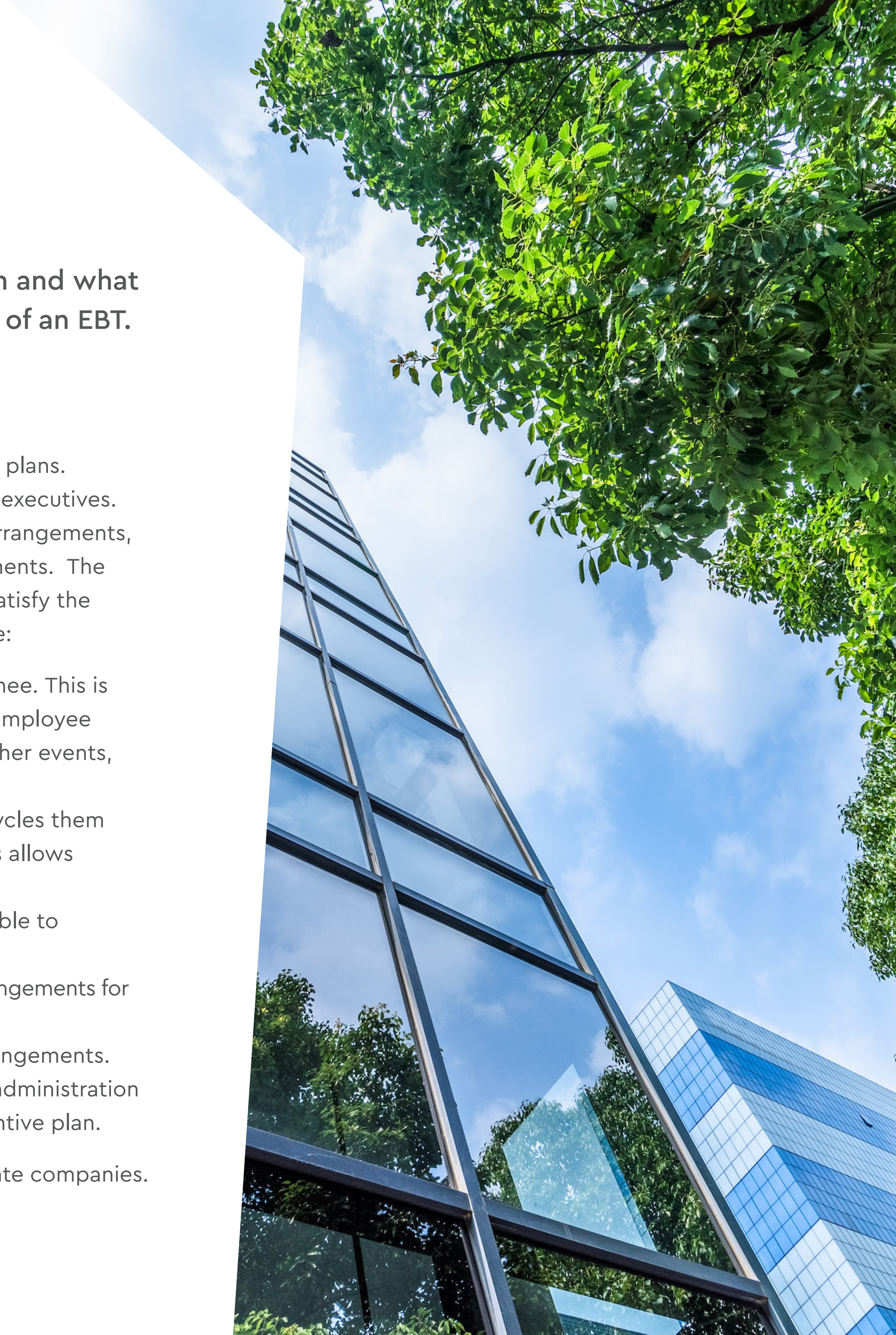
The benefits and common uses of EBTs depend on who is using them and what they're using them for. In this section we'll look at three typical uses of an EBT.

Private companies

A private company might operate one of several types of employee incentive plans. The plan(s) might reward everyone in the business, or a select number of key executives. The EBT might be used in conjunction with joint ownership or fund deferral arrangements, revenue approved incentive plans, bespoke share rewards or bonus arrangements. The trustee of an EBT holds the relevant assets in trust until they are required to satisfy the incentive awards. Additional benefits of an EBT for a private company include:

- Nominee arrangements. The trustee holds assets for employees as a nominee. This is potentially cost and tax efficient, and also ensures confidentiality around employee holdings. As the trustee is the sole legal titleholder for transactions and other events, nominee arrangements can also make for simpler administration.
- Creating an internal market. The EBT buys shares from employees and recycles them to others. For private companies with no other market for their shares, this allows beneficiaries to realise the value of their rewards.
- Warehousing unallocated assets – ensuring that sufficient assets are available to satisfy future obligations.
- Administering bespoke arrangements. The trustee can facilitate bespoke arrangements for key hires.
- Trustees can also assist in exit events, restructuring, listing and lock-in arrangements.
- Administration support – many EBT trustees can also provide outsourced administration and data management solutions, easing the administration of a share incentive plan.

Ocorian looks after the employee incentive arrangements of around 300 private companies. Many operate bespoke and varied plans, in conjunction with an EBT.



Private equity-backed companies

Private equity-backed companies commonly operate an EBT in conjunction with a Management Incentive Plan (MIP). MIPs are designed to incentivise leadership teams and employees to maximise performance during the term of the equity investment. Often, employee equity is held by an EBT trustee as nominee until an exit event.

Benefits include:

- The trustee holds assets for employees as nominee enabling tax and cost-efficient incentive plans and ensuring confidentiality of employee holdings.
- The trustee is the sole legal titleholder for transactions and other events, making for smoother administration.
- The trustee holds reserved but unallocated (or leaver) equity securely in the trust fund for future allocation.
- The trustee can facilitate bespoke arrangements, e.g. for key hires, and provides processing for those leaving or joining the MIP.
- An EBT trustee can assist with exit, restructuring, listing and lock-in arrangements.
- Administration support – many EBT trustees can also provide outsourced administration and data management solutions, easing the administration of a share incentive plan.

Ocorian looks after the MIPs of around 200 private equity-backed businesses, usually in conjunction with an EBT. Clients include private equity firms who use Ocorian's services for each new company they acquire to help incentivise management performance for the term of the investment.

Public limited companies (PLCs)

Many listed companies operate different incentive plans at different tiers of the business – from all-employee arrangements to plans for key executives. Many also operate legacy schemes, which can be complex to administer. An EBT will often be used to hold shares to satisfy incentive awards across a number of plans, hedging the company's obligation to provide the required shares when awards vest.

Benefits include:

- The trustee holds the assets to satisfy awards – these arrangements might include long-term incentive plans, all-employee plans, Inland Revenue tax approved plans, and fund deferral arrangements.
- The trustee might also hold vested assets for employees as a nominee – encouraging employee share retention and easing administration and reporting (e.g., FATCA and CRS reporting). The trustee also facilitates dividend and voting processing under a nominee arrangement.
- The trustee might assist with hedging strategies for PLC clients.
- Administration support – many EBT trustees can provide outsourced administration and data management solutions, easing the administration of share incentive plans.

Ocorian looks after the EBT arrangements of over 100 listed companies, including c.20% of the FTSE 100. We tailor our service to the precise needs of our clients.

SECTION 3

Setting up and reviewing an EBT

New to employee benefits trusts?

EBTs are an effective and efficient way to manage incentive plans for your employees. So how do you set one up?

We recommend that clients work with their tax and legal advisors to decide on the structure that best suits their business priorities and circumstances. These advisers can help your business create a tax-efficient and compliant reward strategy tailored to your needs.

Your EBT trustee should work with you and your tax and legal advisors to put their guidance into practice. Most businesses choose to appoint a third-party trustee, operating in a regulated environment.

Five key steps in setting up an EBT

1 Determine the purpose of your incentive plan

Agree the purpose and structure of the company's reward strategy in conjunction with your relevant advisors.

2 Choose a trustee

The trustee role is crucial. Acting in the best interests of beneficiaries at all times, a third party trustee ensures the independence of your employee incentive plan and EBT, provides professional technical experience, transparency and operates in a regulated environment.

3 Settle a trust deed and ancillary documents

The trust deed sets out the powers and duties of the trustee and governs the operation of the trust. It records the relationship of the parties involved in the trust: the settlor company, the trustee and the beneficiaries who may benefit from the assets held in the trust.

The trust deed will usually include wide discretionary investment powers, and the trustee will look to the company for recommendations relating to the acquisition of assets and their application for the benefit of beneficiaries.

There may also be a separate operating agreement that prescribes how the trustee and company will work together to provide reward, alongside funding and plan documentation.

4 Fund the trust

Like most trusts, an EBT can be set up with a nominal sum. After that, an employer will fund the trust by either giving or lending capital to acquire shares or other assets to be used for satisfying awards made under the plan(s).

5 Administer the trust

With set-up complete, the trustee will hold and manage assets according to the terms of the trust deed, incentive plan(s) and operating agreements.

Reviewing existing reward arrangements and EBTs

Once established, an EBT may remain in place for many years. In some cases, a company may benefit from reviewing their EBT and incentive arrangements to ensure that they provide appropriate, effective and cost-efficient reward.

Four reasons to review your incentive arrangements

1 Your arrangements have never been reviewed

If your incentive arrangements were set up several years ago, the incentive plan may not meet employee expectations. Trends in incentives are evolving with our approach to careers and reward. Legacy awards may be "underwater", or a plan may not offer effective reward and retention.

2 Your arrangements may no longer be compliant

The regulatory, legal and tax landscape is continually evolving and arrangements should be subject to relevant review and advice.

3 Your arrangements may no longer be efficient

Do you and your service providers have the processes and technology to create administrative simplicity, reduce risk and increase efficiency?

4 Your company has changed

Has your organisation changed significantly since the establishment of your incentive arrangements? Maybe you've grown, acquired another company or merged. You may be able to review costs, administration and effectiveness of rewards.

Companies with an existing incentive plan should make sure it reflects their requirements, and employee expectations.

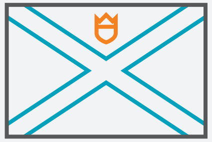
SECTION 4

Best-practice EBT administration

Where should you set up an EBT?

The jurisdiction of your EBT has tax and legal implications and your advisors will guide you on the best approach. It's also true that some locations have developed reputations as hubs for the efficient management of employee incentive plans and administration of EBTs – this long standing reputation and experience is invaluable.

Many UK and international businesses look to Jersey and Guernsey to administer offshore EBTs – benefiting from CGT sheltering but also significant experience and technical expertise, provided in a highly regulated jurisdiction.



Three reasons to administer your EBT in Jersey

1. **Tax-efficiency**

   Establishing an EBT in Jersey makes it resident outside the UK for tax purposes. In particular, this shelters the trust's assets from capital gains tax.

2. **Experience**

   Jersey has a long history of providing trustee services for EBT structures. Many trustees on the island are hugely experienced in setting up and administering EBTs, even in more complex and bespoke situations.

3. **Regulatory environment**

   Jersey is a highly regulated jurisdiction and trustees face annual external audits, and capital adequacy and insurance requirements. A compliance culture helps safeguard EBT assets and reassure beneficiaries.

Automation is key to efficiency

Location is one issue, technology another. Many businesses still manage employee incentive plans using spreadsheets. As plan populations and legacy awards grow, manual processes may become increasingly inefficient, error-prone and opaque, making valuable large-scale data analysis impossible.

Cloud-based solutions hugely simplify the management and tracking of incentive arrangements. Platforms provide a single virtual folder for your reward arrangements and a self-serve portal for employees. They automate repeating tasks and make sure the administration of plans is accurate, efficient and transparent.

Technology is used to guarantee accuracy and administrative efficiency, while providing businesses and employees with 24/7 access to relevant data.

Four ways technology simplifies employee incentive plan administration

1 Accurate audit trails

Any changes made to equity ownership and awards are recorded, authenticated and immutably stored.

2 Visibility

Software makes trust transactions, trustee shareholdings and award commitments visible, and provides 24/7 access to relevant tax and accounting information.

3 Employee awards tracking

Employee incentive plans can become increasingly complex as your business grows. An automated system can track employee incentive plans efficiently, using data analysis and, increasingly, artificial intelligence to help you create the most beneficial timetable around equity release and vesting schedules.

4 Employee information

Your people want to know what they have been granted, when it will vest and what they have already received. Where relevant they will want to keep track of valuations over time. Cloud-based systems make this information easily accessible. Employees can see their holdings, check vesting schedules and see models of the potential value of their shares.

Software makes incentive plan administration easier and keeps employees engaged with the reward process – reinforcing the message that loyalty and performance are valued and rewarded.

Ocorian work with different providers to ensure we have access to the right partners for our clients and that we can provide a holistic service to all clients whether they are FTSE100/All share, AIM listed or private equity backed companies.

Choosing a trustee

An efficient employee benefit trust relies on an effective trustee. The trustee looks after the trust's assets and supports the provision of reward to beneficiaries. A trustee can also remove a significant administrative burden from in-house teams.

With that in mind, choosing the right trustee is clearly an important decision. Here's what you need to look for in a potential EBT partner:

Tailored services

As well as acting as trustee, holding trust assets, your trustee will assist with the operation of your incentive plans and may provide digital platforms easing administration and reporting and increasing employee engagement.

Expertise and experience

EBT administration takes expertise, experience and a dedicated team. Many reward arrangements are bespoke and some are quite complex. Your trustee should have a history of running a wide spectrum of reward types for a wide range of clients.

Systems and processes

Ask a prospective partner about the systems and processes they have for managing employee benefit trusts and incentive plans. Can they offer you a technology platform and portal? Do they automate as many processes as possible? As you grow and your scheme expands, can they scale their service accordingly?

Location

Your tax and legal advisors will guide you on the best jurisdiction and regulatory environment for your EBT.

The most crucial test? Meet them. Let any potential provider demonstrate the experience of their people and the sophistication of their technology. Ask for case studies of companies with similar requirements. In a tough time for recruitment and retention, employee reward should not be left to chance.

Ocorian is the perfect partner for your EBT needs

We are proud to be a leading and well-established provider of trustee, administration, and system solutions for employee incentives arrangements. But why trust us?

C. 20% of the FTSE 100 use our Employee Incentive Services, in addition to scores of FTSE 250, FTSE 350, AIM listed and private companies.

We strive to deliver excellent service regardless of size or complexity.

Our Jersey-based team has an exceptional reputation with decades of experience in the employee benefits industry.

We can seamlessly set up and mange a spectrum of incentive schemes from bespoke arrangements for a handful of senior staff to all-employee packages covering hundreds or thousands of employees.

We offer an end-to-end service for EBTs, backed by the latest administration software and a powerful client portal so you get information at your fingertips.

Get in touch with us

For more information on employee incentives services from Ocorian, and to start a conversation about your bespoke needs, please visit our website or get in touch.

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