BAXENDALE

QUICK GUIDE TO LENDING TO AN EMPLOYEE OWNED BUSINESS

Glossary of Terms:

Employee Trust:
Usually Employee Ownership Trusts (EOTs) or for older businesses Employee Benefit Trusts (EBTs) where ownership over some or all of the shares in the business is held in trust.

EOB:
Employee Owned Business, owned wholly or materially by the employees of the company.

Trustees:
The trustees of the employee trusts. Usually a corporate trustee controlled by a group of trustee directors. The entity is usually dormant, holding no assets on its own behalf.

Purpose of Borrowing:

EOBs will usually borrow for the same reasons as other businesses:

- to grow the business
- to invest in / acquire key assets
- to increase working capital
- to fund an exit

The latter in particular will have some details that are likely to vary from other forms of borrowing.

Who is the borrower?:

The borrower will usually be either the EOB itself or the Employee Trust.

For the borrower, the main benefit of the EOB being the borrower is that the interest and similar costs can usually be treated as a cost when calculating the EOB's corporation tax liabilities.

If the Employee Trust is the borrower, this has the benefit of the debt not usually being on the EOB's balance sheet.

Key Differences:

There are a handful of factors that may be different from a loan to a non-EOB:

- The corporate trustee does not hold the trust assets on its own behalf: Assets are held in trust for the benefit of the employees. This means that a debenture / floating charge granted by the corporate trustee may not cover the assets in the trust. If a bank wants security over these assets, taking a share pledge or charge over the shares held in the trust is usually a better option (although the bank may still want the debenture).

Key Differences (cont.):

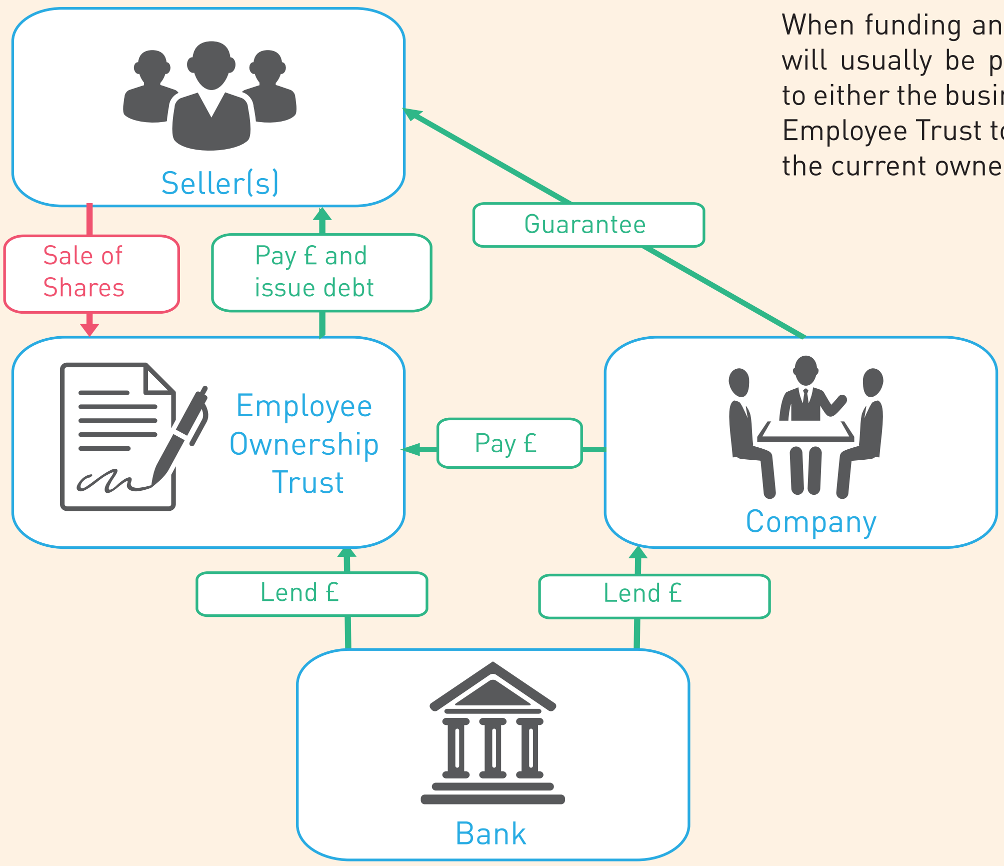
- The Employee Trust is not a trading entity: Any financial covenants or obligations to produce financial information are unlikely to be appropriate. These should usually be restricted to the EOB itself

- No Personal Guarantees: It is extremely unlikely that an EOB that is wholly owned by an Employee Trust will have any employees willing to provide a personal guarantee for any debts of the EOB.

- Status of the former owner(s): In an exit situation, the former shareholders will often remain significant creditors with various creditor protections. The bank will usually want to be clear on the nature of these protections and powers and the extent to which they should be postponed behind their own position (for example, through the use of an intercreditor agreement).

Funding an Exit:

When funding an exit, the funder will usually be providing finance to either the business itself or the Employee Trust to fund the exit of the current owners:



Baxendale are specialist advisers on employee ownership. We have been advising businesses on employee ownership for almost twenty years and have been employee owned ourselves for thirty years. During this time we have helped over 100 businesses become employee owned.