Institution **CIOT - CTA**
Course **APS VAT and Other Indirect Tax**

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Answer-to-Question-_1_

From: BFR TAX LLP

To: Board of Coua Ltd

Subject: DRAFT Report regarding the sale of shares in Eggton Ltd and the tax and commercial implications of two potential investment opportunties

Date: 08 May 2025

This report is currently in draft format and is not to be distributed until reviewed.

Introduction

This report has been prepared based upon the information provided to us by Manny Singh, under our Letter of Engagement dated 1 May 2025. This report has been prepared exclusively for the Board of Directors of Coua Ltd and cannot be relied upon by any third party.

We understand that Coua Ltd is currently in the process of selling its subsidiary entity, Eggton Ltd, which is owns 100% of the shares in. Following receipt of proceeds from this sale of shares and further investment, the business is considering two potential new business ventures and would like to understand the tax and commercial issues arising from both.

Our report has considered the following factors:

1. The sale of shares in Eggton Ltd and estimated net proceeds
2. Option 1: Construction of a new factory
3. Option 2: Purchase of a wholesale clothing business

Executive Summary

- We estimate the proceeds of sale from the sale of Eggton to be £33,991,553, leading to a small shortfall compare to the projected costs of each option. This option was identified as easy to fund so we do not think funding will be a concern.
- We would recommend proceeding with Option 1 due to the costs being lower than you have projected (explained below) but also as a commercial decision, as Option 1 would involve you expanding in your sector and potentially creating new products that you can sell to further grow the business.
- We note that the costs will be lower than forecasted due to the increased capital allowances available, as R&D consturction can get 100% FYAs rather than 3% SBA so the construction costs are substantially reduced by 25% CT. We note that SDLT of £469,500 is also due.
- The R&D work within option 1 could lead to developments that you are able to trademark and guaruntee future income. In the first year, R&D relief on the £28m expenditure would be £11.2m, which is significant and further reliefs would arise each year providing the R&D continued, although no R&D relief is avaialble on the commercial goods then sold.
- Option 2 is attractive due to the acquisition of an established business with exclusivity and a trained management team. However, you would have less day to day control of this enterprise.
- Stamp duty is also a factor that has not yet been considered, and holding the company outside the VAT group would mean that you would need to charge VAT on any supplies between Coua LTd and the new business. VAT incurred on lender's fees would not be recoverable and as such this forms an additional cost of this route. No new capital allowances would arise so there is no immediate signficant relief as there is under option 1.
- We would therefore recommend option 1. Essentially the possiblities under this option

appear to be more in line with your commercial ventures and the up front cost, although slightly increased by SDLT, will be reduced by the CAs available and therefore costs will be lower than you have budgeted for but could lead to substantial future profits.

(1) Net proceeds of the sale of Eggton shares

Net proceeds of sale

We have provided a breakdown of the capital gain arising from the sale of shares in Appendix A, together with a calculation for the VAT recovery. We estimate a gain of £34,148,553 will arise from the share sale; however, providing the substantial shareholding exemption applies, the Corporation Tax on this gain will be nil.

Substantial Shareholding Exemption

This exemption allows companies that sell shares in businesses for which they hold more than 10% of the ordinary shares and distributable profits to pay no corporation tax on the disposal of these shares. As a holding company, Coua Ltd will meet the 10% shareholding condition.

There is also a condition concerning the entity sold which states it must be trading for at least 12 months out of the 6 years preceding its sale. As Eggton is a trading entity incorporated in 2005, this condition is met.

The proceeds will therefore be exempt from Corporation Tax.

VAT on professional costs relating to share sale

A sale of shares to UK businesses or individuals is exempt for VAT purposes. Therefore, the general rule is that any costs you have incurred that can be directly attributed to selling shares would not allow for input recovery. This is the case with the commission paid to Melanie, as this is related to the sale of shares in the UK, therefore the VAT cost should be factored in when considering your overall proceeds.

Commission to Teddy Wu

The costs paid to Teddy Wu are a service provided by an overseas business to Coua Ltd so, as you know, the reverse charge obligation will arise. This supply may allow for input recovery under the specified services rules.

Specified services

Where shares are sold to a non-UK company, this is a specified supply for VAT purposes. Essentially, a specified supply is still exempt (as a sale of shares) but gives rise to a special concession that allows input tax directly attributed to it to be recovered. As a proportion of the sales of shares was to a non-UK business and this cost can be directly attributed to that cost only, this will allow you to recover this input tax in full.

Overheads of the deal fees

Fees such as legal fees and accountancy should be considered carefully to determine if they are wholly attributable to either the 80% sale to UK buyers or the 20% to overseas buyers. Assuming that neither are directly attributable to one, a proportion of the VAT incurred of 20% could be recovered to reflect the proportion of sales that give rise to input tax recovery.

Losing the Management Services fees from Eggton

We note that you raised the point that you will no longer be receiving management services charges from Eggton due to its disposal. This could be significant for the VAT recovery position of Coua Ltd if it were a 'bare' holding company where its only activity was a management services agreement with Eggton. However, as Coua Ltd is also undertaking trading activity (as per the information provided by you), it will not cease to have an economic activity once Eggton has been sold and we would therefore not flag any risk from this.

Eggton leaving the VAT group
We note that HMRC must be informed within 30 days of the change in membership of the VAT group. As your VAT payment will still exceed £2.3 million per annum you will still be within the payment on account regime but may wish to request a reduction in payments if you believe they will fall significantly.

Eggton leaving- general implications
Eggton will cease to be a member of the relevant group relief group post disposal and any losses would be transferred with it, we note there do not appear to be trading losses so do not consider any action necessary on this point.

Conclusion
Due to the SSE, no CT will be due and your proceeds should be circa £34,148,553, although we note that £157,000 of VAT will be irrecoverable, leading to a total of £33,991,553.

(2) Option 1: Construction of new factory

Expected costs of construction

Land
Land is capital in nature and is therefore not deductible for CT purposes.

Stamp Duty Land Tax

We note that the land cost of £8,000,000 will also incur Stamp Duty Land tax ("SDLT"). SDLT is charged on the VAT inclusive value, as the landlord has opted to tax, SDLT will apply to £9,600,000. The non-residential rates will apply as this is bare commercial land, therefore SDLT will be:

£
0- 150,000 @ nil
150,001-250,000 @ 2% = 2,000
250,001 - 9,600,000 @ 5% = 467,500
=£469,500 extra cost

You will also be required to make an SDLT return, together with the payment, 14 days post completion.

VAT on expected costs of construction

The VAT of £1,600,000 on the land should be recoverable in full as the use you have outlined is fully taxable for VAT purposes.

As a commercial business, you will incur standard rate VAT on the construction costs you incur, which will be recoverable as the entire site will be used to undertake taxable activities.

Similarly, the equipment and other costs, where VAT is applied, will be recoverable as related to a fuly taxable business activity.

The research you are undertaking would not be considered 'non-business' for VAT purposes on the basis that you are undertaking it in order to be able to exploit the findings for commercial sale. VAT case law concerning a charity found that crash test simulations provided for free to lead to future taxable work were related to that future work, therefore even research performed before production will be a business activity.

It should however be noted that the expenditure on land and construction will create a Capital Goods Scheme asset for the business, this will not give rise to any clawback of VAT providing you continue taxable use for a minimum of ten years , but should be considered if you were to change use or decide to rent or sell the property within 10 years.

Making the option to tax may be beneficial so that any future sale is taxable for VAT purposes, this can be done by documenting your intention somewhere such as meeting minutes and emailing HMRC, we can support with this if required.

Research and Development

There are special reliefs provided to business that undertake research and development in a field of science or technology. In order to qualify, the work must either create something new or appreciably improve/find a new way of doing something existing. The work you have outlined to produce electric vehicle batteries more efficiently and safely will qualify as Research & Development("R&D") expenditure for these purposes as it is leading to a substantial improvement in a scientific field.

The reliefs provided for research and development should be factored in to your decision making, as a credit called the 'RDEC' is available against the qualifying R&D revenue expenditure each accounting period, allowing to ongoing savings. There is also a First Year Allowance of 100% on R&D expendtiture that is more generous than the general FYAs available.

RDEC

The RDEC is a 20% credit that can be deducted from the CT payable for the accounting period. The way that it is calculated is that the RDEC is treated as a taxable receipt (meaning you pay CT on it) but then also a tax deduction, the net benefit after adding in and deducting the RDEC is therefore 15%, which is on top of the usual 25% relief for business expenses, this totals 40% relief against the R&D expenditure cost.

The £28,000,000 R&D expenditure therefore would give rise to relief of £11,200,000. If R&D was not undertaken and this was a general business expense, relief would be only £7,000,000.

This leads to an additional £4,000,000 relief for option 1 due to the R&D expenditure.

R&D Capital expenditure

Land does not qualify for any Capital allowances either under the R&D rules or general rules, as such we have outlined the relevant additional costs to considered for land above, but will now consider the potential savings for R&D expenditure on your remaining costs.

Capital allowances

Building

The building costs would generally allow for a 3% structures and building allowance per annum across a 33 1/3 year period. However, the proportion of the building that relates to the R&D activity (the R&D lab) would qualify for 100% FYA.

Equipment

Provided the equipment is new, this would qualify for 100% FYAs for both the R&D and the factory. Otherwise, second hand goods for the factory could make use of the £1m annual investment allowance ("AIA"). Integral features (which is generally items incorporated into the building such as air conditioning) have a lower rate of FYA at 50%, therefore you should ensure that the AIA is allocated towards these in priority.

Specialised Equipment

The specialised equipment imported will incur import duties. Import VAT will be recoverable, although we note that you will need to have a GB EORI and PIVA account to be the importer on record- we assume due to the size and nature of your business that you will be utilising a PIVA account, if not it may be possible to use the freight forwarder's duty deferment account if needed.

The customs duty due on import (as there is no free trade agreement between Sayonara and the UK) will increase your costs as it is not recoverable. There is a relief available for import of some specialised equipments for commercial use but we would require further details to confirm if this applies. Alternatively, you could request your supplier imports the goods under DDP incoterms to bear the associated administration and costs; however this will be a commercial decision based upon your relationship with the supplier. We have therefore flagged this cost as an additional cost on the basis you may be required to incur duties.

Conclusion

Purhcasing a business should be, on the whole, a commercial decision. Option 1 would involve you expanding in your sector and potentially creating new products that you can sell to further grow the business. We note that this option may appear to be cash negative (although given the reliefs outlined above, this may no longer be the case)however the business is in a strong financial position and as such a new venture in a relevant field appears to have a clearer long term benefit than option 2.

The R&D work within option 1 could lead to developments that you are able to trademark and guaruntee future income; however, it also involves considerable up front costs and there is the need to ensure that you qualify for the conditions for HMRC's R&D relief to be in point. However, based on the information provided to us we believe you will meet these conditions.

Although there is a small up front Stamp duty land tax liability you had not factored in of £469,500, the long term cost of this route is likely to be lower due to the R&D relief outlined. Based on the figures provided, CT relief of £11,200,000 is available in year 1 via the RDEC. There is also relief on 100% of the proportion of construction that relates to R&D expenditure and any plant and machinery used for the R&D work.

You hvae also indicated that funding would be easy under this option, which would help to make up the small shortfall outlined.

Essentially the possiblities under this option appear to be more in line with your commercial ventures and the up front cost, although slightly increased by SDLT, will be reduced by the CAs available and therefore costs will be lower than you have budgeted for but could lead to substantial future profits.

(3) Option 2: Purchase of a Wholesale clothing business

VAT on purchase of shares and related costs

As outlined above, the purchase of shares is exempt from VAT and as such you will not incur VAT on the shares themselves. VAT on your professional costs totals £150,000. The acqusition of a business is considered to be a business activity for VAT purposes and allows for input tax recovery, therefore this VAT should be recoverable in full. We note there is no intention to add Unumiota to the VAT group, we note that it does not need to be within the VAT group in order for input recovery to be possible but Coua Ltd should ensure it enters into a management services agreeement with the the new entity so that there is a direct link between its taxable activities and acquiring the new business.

The professional costs you are satisfying on behalf of Rag Tag Trade Plc require further review. There has been a number of VAT cases concerning input tax recovery on deal fees where there are two parties who could be seen to benefit from the service, we call these 'tripartite agreements'. If you could be seen to have instructed the service provider and benefitted from the service, you could potentially recover the input. However, unfortunately in this instance it appears that your lender is unequivocally the recipient as it will instruct the advisors and receive the advice and you will simply remunerate the cost it has suffered. Therefore, under the principle set by the 'Airtours' VAT case, this VAT will be an irrecoverable cost for you.

Corporation Tax
The purchase of shares is capital in nature and is therefore not deductible for CT purposes.

Stamp Duty
Stamp Duty of 0.5% will be due on the purchase price for the shares, this is also not CT deductible as it will be an allowable cost in the gain calculation on future disposal. Stamp Duty on £41,000,000 will be £205,000.

Capital Allowances

The capital assets acquired will be inherited at their tax written down value and there is therefore no AIA / FYAs, you will just continue with the future allowances.

Buiness history

A signficant risk we would flag with the acquisition of shares is that you will incur all of the history of the business. We would not recommend this option without recommending that a full due diligence is undertaken and warranties are drawn up to indeminify you against any liabilities that may exist in any tax before acqusition. You will also inherit the commercial reputation of the business as well as any customer liabilities already existing, so these must be evaluated before considering purchase also. If any losses are available, these will be bought with the business.

Exclusivity

Exclusivity in key markets for 5 years is a very attractive offer from a commercial perspective. This could allow the business to establish a powerful position on the market; however, as this is limited to 5 years it should be considered whether the forecasted figures are heavily dependent on this, and whether the future value after this could dip once it no longer monopolises the market.

Management

We also note that the management will be run by the existing team, whilst this is helpful to rely upon their commercial expertise in the sector, it also means that less control will be orchestrated by your board of Directors, which may impact their preference.

Conclusion

Option 2 is attractive due to the acquisition of an established business with exclusivity and a trained management team.

However, you would have less day to day control of this enterprise and, as outlined you inherit any previous history and liabilities alongside the business and this should be factored in to your decision making also.

Stamp duty is also a factor that has not yet been considered and adds a small cost. Furthermore, holding the company outside the VAT group would mean that you would need to charge VAT on any supplies between Coua LTd and the new business.

VAT incurred on lender's fees would not be recoverable and as such this forms an additional cost of this route.

No new capital allowances would arise so there is no immediate signficant relief as there is under option 1. There could also be some complexities in the new business such as retail schemes for VAT, which you do not currently have the expertise to deal with. The risk that the profits may drop following the exclusivity period are also concerning for this option. Therefore, on the whole option 1 appears preferable.

Appendix A: Sale of shares in Eggton

Capital Gain on Shares

		£	Notes		
Proceeds		35,000,000			
Less: Costs of sale					
Commission to Melanie		(350,000)			
Commission to Teddy Wu Associates		(175,000)			

Accountancy fees		(125,000)			
Legal Fees		(200,000)			
Less: Cost of shares		(1,000)			
Less: indexation allowance		(447)	N1		
Gain:		34,148,553			
CT due @ 25%		nil	N2		

N1: Indexation allowance = from 1 June 2005 278.1-192.2/192.2 x 1,000 = 447

N2: Substantial shareholding exemption applies so exempt from CT

VAT recovery on professional fees

VAT on		**Value £**	**Recovery**			
Commission to Melanie		70,000	nil			
Commission to Teddy Wu		35,000	35,000			
Legal fees		40,000	8,000	20%		
Accountancy Fees		25,000	5,000	20%		
		Total	**48,000**			

Irrecoverable VAT of **£157,000**should be factored into costs

Note: explanation for the VAT recovery is in the narrative of the report