



Finance Act 1996

1996 CHAPTER 8

PART IV

INCOME TAX, CORPORATION TAX AND CAPITAL GAINS TAX

CHAPTER II

LOAN RELATIONSHIPS

Introductory provisions

80 Taxation of loan relationships

- (1) For the purposes of corporation tax all profits and gains arising to a company from its loan relationships shall be chargeable to tax as income in accordance with this Chapter.
- (2) To the extent that a company is a party to a loan relationship for the purposes of a trade carried on by the company, profits and gains arising from the relationship shall be brought into account in computing the profits and gains of the trade.
- (3) Profits and gains arising from a loan relationship of a company that are not brought into account under subsection (2) above shall be brought into account as profits and gains chargeable to tax under Case III of Schedule D.
- (4) This Chapter shall also have effect for the purposes of corporation tax for determining how any deficit on a company's loan relationships is to be brought into account in any case, including a case where none of the company's loan relationships falls by virtue of this Chapter to be regarded as a source of income.
- (5) Subject to any express provision to the contrary, the amounts which in the case of any company are brought into account in accordance with this Chapter as respects any matter shall be the only amounts brought into account for the purposes of corporation tax as respects that matter.

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81 Meaning of “loan relationship” etc

- (1) Subject to the following provisions of this section, a company has a loan relationship for the purposes of the Corporation Tax Acts wherever—
 - (a) the company stands (whether by reference to a security or otherwise) in the position of a creditor or debtor as respects any money debt; and
 - (b) that debt is one arising from a transaction for the lending of money;
 and references to a loan relationship and to a company’s being a party to a loan relationship shall be construed accordingly.
- (2) For the purposes of this Chapter a money debt is a debt which falls to be settled—
 - (a) by the payment of money; or
 - (b) by the transfer of a right to settlement under a debt which is itself a money debt.
- (3) Subject to subsection (4) below, where an instrument is issued by any person for the purpose of representing security for, or the rights of a creditor in respect of, any money debt, then (whatever the circumstances of the issue of the instrument) that debt shall be taken for the purposes of this Chapter to be a debt arising from a transaction for the lending of money.
- (4) For the purposes of this Chapter a debt shall not be taken to arise from a transaction for the lending of money to the extent that it is a debt arising from rights conferred by shares in a company.
- (5) For the purposes of this Chapter—
 - (a) references to payments or interest under a loan relationship are references to payments or interest made or payable in pursuance of any of the rights or liabilities under that relationship; and
 - (b) references to rights or liabilities under a loan relationship are references to any of the rights or liabilities under the agreement or arrangements by virtue of which that relationship subsists;
 and those rights or liabilities shall be taken to include the rights or liabilities attached to any security which, being a security issued in relation to the money debt in question, is a security representing that relationship.
- (6) In this Chapter “money” includes money expressed in a currency other than sterling.

Taxation of profits and gains and relief for deficits

82 Method of bringing amounts into account

- (1) For the purposes of corporation tax—
 - (a) the profits and gains arising from the loan relationships of a company, and
 - (b) any deficit on a company’s loan relationships,
 shall be computed in accordance with this section using the credits and debits given for the accounting period in question by the following provisions of this Chapter.
- (2) To the extent that, in any accounting period, a loan relationship of a company is one to which it is a party for the purposes of a trade carried on by it, the credits and debits given in respect of that relationship for that period shall be treated (according to whether they are credits or debits) either—

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- (a) as receipts of that trade falling to be brought into account in computing the profits and gains of that trade for that period; or
 - (b) as expenses of that trade which are deductible in computing those profits and gains.
- (3) Where for any accounting period there are, in respect of the loan relationships of a company, both—
- (a) credits that are not brought into account under subsection (2) above (“non-trading credits”), and
 - (b) debits that are not so brought into account (“non-trading debits”),
- the aggregate of the non-trading debits shall be subtracted from the aggregate of the non-trading credits to give the amount to be brought into account under subsection (4) below.
- (4) That amount is the amount which for any accounting period is to be taken (according to whether the aggregate of the non-trading credits or the aggregate of the non-trading debits is the greater) to be either—
- (a) the amount of the company’s profits and gains for that period that are chargeable under Case III of Schedule D as profits and gains arising from the company’s loan relationships; or
 - (b) the amount of the company’s non-trading deficit for that period on its loan relationships.
- (5) Where for any accounting period a company has non-trading credits but no non-trading debits in respect of its loan relationships, the aggregate amount of the credits shall be the amount of the company’s profits and gains for that period that are chargeable under Case III of Schedule D as profits and gains arising from those relationships.
- (6) Where for any accounting period a company has non-trading debits but no non-trading credits in respect of its loan relationships, that company shall have a non-trading deficit on its loan relationships for that period equal to the aggregate of the debits.
- (7) Subsection (2) above, so far as it provides for any amount to be deductible as mentioned in paragraph (b) of that subsection, shall have effect notwithstanding anything in section 74 of the Taxes Act 1988 (allowable deductions).

83 Non-trading deficit on loan relationships

- (1) This section applies for the purposes of corporation tax where for any accounting period (“the deficit period”) there is a non-trading deficit on a company’s loan relationships.
- (2) The company may make a claim for the whole or any part of the deficit to be treated in any of the following ways, that is to say—
- (a) to be set off against any profits of the company (of whatever description) for the deficit period;
 - (b) to be treated as eligible for group relief;
 - (c) to be carried back to be set off against profits for earlier accounting periods; or
 - (d) to be carried forward and set against non-trading profits for the next accounting period.
- (3) So much of the deficit for the deficit period as is not the subject of a claim under subsection (2) above shall be carried forward so as to be brought into account for

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the purposes of this Chapter as a non-trading debit (“a carried-forward debit”) for the accounting period immediately following the deficit period.

- (4) No claim shall be made under subsection (2)(a) to (c) above in respect of so much (if any) of the non-trading deficit of a company for any accounting period as is equal to the amount by which that deficit is greater than it would have been if any carried-forward debit for that period had been disregarded.
- (5) No part of any non-trading deficit of a company established for charitable purposes only shall be set off against the profits of that or any other company in pursuance of a claim under subsection (2) above.
- (6) A claim under subsection (2) above must be made within the period of two years immediately following the end of the relevant period, or within such further period as the Board may allow.
- (7) In subsection (6) above “the relevant period”—
 - (a) in relation to a claim under subsection (2)(a), (b) or (c) above, means the deficit period; and
 - (b) in relation to a claim under subsection (2)(d) above, means the accounting period immediately following the deficit period.
- (8) Different claims may be made under subsection (2) above as respects different parts of a non-trading deficit for any period, but no claim may be made as respects any part of a deficit to which another claim made under that subsection relates.
- (9) Schedule 8 to this Act (which makes provision about what happens where a claim is made under subsection (2) above) shall have effect.

Computational provisions etc.

84 Debits and credits brought into account

- (1) The credits and debits to be brought into account in the case of any company in respect of its loan relationships shall be the sums which, in accordance with an authorised accounting method and when taken together, fairly represent, for the accounting period in question—
 - (a) all profits, gains and losses of the company, including those of a capital nature, which (disregarding interest and any charges or expenses) arise to the company from its loan relationships and related transactions; and
 - (b) all interest under the company’s loan relationship and all charges and expenses incurred by the company under or for the purposes of its loan relationships and related transactions.
- (2) The reference in subsection (1) above to the profits, gains and losses arising to a company—
 - (a) does not include a reference to any amounts required to be transferred to the company’s share premium account; but
 - (b) does include a reference to any profits, gains or losses which, in accordance with normal accountancy practice, are carried to or sustained by any other reserve maintained by the company.

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- (3) The reference in subsection (1)(b) above to charges and expenses incurred for the purposes of a company's loan relationships and related transactions does not include a reference to any charges or expenses other than those incurred directly—
- (a) in bringing any of those relationships into existence;
 - (b) in entering into or giving effect to any of those transactions;
 - (c) in making payments under any of those relationships or in pursuance of any of those transactions; or
 - (d) in taking steps for ensuring the receipt of payments under any of those relationships or in accordance with any of those transactions.
- (4) Where—
- (a) any charges or expenses are incurred by a company for purposes connected—
 - (i) with entering into a loan relationship or related transaction, or
 - (ii) with giving effect to any obligation that might arise under a loan relationship or related transaction,
 - (b) at the time when the charges or expenses are incurred, the relationship or transaction is one into which the company may enter but has not entered, and
 - (c) if that relationship or transaction had been entered into by that company, the charges or expenses would be charges or expenses incurred as mentioned in subsection (3) above,
- those charges or expenses shall be treated for the purposes of this Chapter as charges or expenses in relation to which debits may be brought into account in accordance with subsection (1)(b) above to the same extent as if the relationship or transaction had been entered into.
- (5) In this section “related transaction”, in relation to a loan relationship, means any disposal or acquisition (in whole or in part) of rights or liabilities under that relationship.
- (6) The cases where there shall be taken for the purposes of this section to be a disposal and acquisition of rights or liabilities under a loan relationship shall include those where such rights or liabilities are transferred or extinguished by any sale, gift, exchange, surrender, redemption or release.
- (7) This section has effect subject to Schedule 9 to this Act (which contains provision disallowing certain debits and credits for the purposes of this Chapter and making assumptions about how an authorised accounting method is to be applied in certain cases).

85 Authorised accounting methods

- (1) Subject to the following provisions of this Chapter, the alternative accounting methods that are authorised for the purposes of this Chapter are—
- (a) an accruals basis of accounting; and
 - (b) a mark to market basis of accounting under which any loan relationship to which that basis is applied is brought into account in each accounting period at a fair value.
- (2) An accounting method applied in any case shall be treated as authorised for the purposes of this Chapter only if—

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- (a) it conforms (subject to paragraphs (b) and (c) below) to normal accountancy practice, as followed in cases where such practice allows the use of that method;
 - (b) it contains proper provision for allocating payments under a loan relationship to accounting periods; and
 - (c) where it is an accruals basis of accounting, it does not contain any provision (other than provision comprised in authorised arrangements for bad debt) that gives debits by reference to the valuation at different times of any asset representing a loan relationship.
- (3) In the case of an accruals basis of accounting, proper provision for allocating payments under a loan relationship to accounting periods is provision which—
- (a) allocates payments to the period to which they relate, without regard to the periods in which they are made or received or in which they become due and payable;
 - (b) includes provision which, where payments relate to two or more periods, apportions them on a just and reasonable basis between the different periods;
 - (c) assumes, subject to authorised arrangements for bad debt, that, so far as any company in the position of a creditor is concerned, every amount payable under the relationship will be paid in full as it becomes due;
 - (d) secures the making of the adjustments required in the case of the relationship by authorised arrangements for bad debt; and
 - (e) provides, subject to authorised arrangements for bad debt and for writing off government investments, that, where there is a release of any liability under the relationship, the appropriate amount in respect of the release is credited to the debtor in the accounting period in which the release takes place.
- (4) In the case of a mark to market basis of accounting, proper provision for allocating payments under a loan relationship to accounting periods is provision which allocates payments to the accounting period in which they become due and payable.
- (5) In this section—
- (a) the references to authorised arrangements for bad debt are references to accounting arrangements under which debits and credits are brought into account in conformity with the provisions of paragraph 5 of Schedule 9 to this Act; and
 - (b) the reference to authorised arrangements for writing off government investments is a reference to accounting arrangements that give effect to paragraph 7 of that Schedule.
- (6) In this section “fair value”, in relation to any loan relationship of a company, means the amount which, at the time as at which the value falls to be determined, is the amount that the company would obtain from or, as the case may be, would have to pay to an independent person for—
- (a) the transfer of all the company’s rights under the relationship in respect of amounts which at that time are not yet due and payable; and
 - (b) the release of all the company’s liabilities under the relationship in respect of amounts which at that time are not yet due and payable.

86 Application of accounting methods

- (1) This section has effect, subject to the following provisions of this Chapter, for the determination of which of the alternative authorised accounting methods that are available by virtue of section 85 above is to be used as respects the loan relationships of a company.
- (2) Different methods may be used as respects different relationships or, as respects the same relationship, for different accounting periods or for different parts of the same accounting period.
- (3) If a basis of accounting which is or equates with an authorised accounting method is used as respects any loan relationship of a company in a company's statutory accounts, then the method which is to be used for the purposes of this Chapter as respects that relationship for the accounting period, or part of a period, for which that basis is used in those accounts shall be—
 - (a) where the basis used in those accounts is an authorised accounting method, that method; and
 - (b) where it is not, the authorised accounting method with which it equates.
- (4) For any period or part of a period for which the authorised accounting method to be used as respects a loan relationship of a company is not determined under subsection (3) above, an authorised accruals basis of accounting shall be used for the purposes of this Chapter as respects that loan relationship.
- (5) For the purposes of this section (but subject to subsection (6) below)—
 - (a) a basis of accounting equates with an authorised accruals basis of accounting if it purports to allocate payments under a loan relationship to accounting periods according to when they are taken to accrue; and
 - (b) a basis of accounting equates with an authorised mark to market basis of accounting if (without equating with an authorised accruals basis of accounting) it purports in respect of a loan relationship—
 - (i) to produce credits or debits computed by reference to the determination, as at different times in an accounting period, of a fair value; and
 - (ii) to produce credits or debits relating to payments under that relationship according to when they become due and payable.
- (6) An accounting method which purports to make any such allocation of payments under a loan relationship as is mentioned in subsection (5)(a) above shall be taken for the purposes of this section to equate with an authorised mark to market basis of accounting (rather than with an authorised accruals basis of accounting) if—
 - (a) it purports to bring that relationship into account in each accounting period at a value which would be a fair value if the valuation were made on the basis that interest under the relationship were to be disregarded to the extent that it has already accrued; and
 - (b) the credits and debits produced in the case of that relationship by that method (when it is properly applied) correspond, for all practical purposes, to the credits and debits produced in the case of that relationship, and for the same accounting period, by an authorised mark to market basis of accounting.
- (7) In this section “fair value” has the same meaning as in section 85 above.
- (8) In this section “statutory accounts”, in relation to a company, means—

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- (a) any accounts relating to that company that are drawn up in accordance with any requirements of the Companies Act 1985 or the Companies (Northern Ireland) Order 1986 that apply in relation to that company;
 - (b) any accounts relating to that company that are drawn up in accordance with any requirements of regulations under section 70 of the Friendly Societies Act 1992 that apply in relation to that company;
 - (c) any accounts relating to that company which are accounts to which Part I of Schedule 21C to the Companies Act 1985 or Part I of Schedule 21D to that Act (companies with UK branches) applies;
 - (d) in the case of a company which—
 - (i) is not subject to any such requirements as are mentioned in paragraphs (a) or (b) above, and
 - (ii) is a company in whose case there are no accounts for the period in question that fall within paragraph (c) above,
 any accounts relating to the company drawn up in accordance with requirements imposed in relation to that company under the law of its home State; and
 - (e) in the case of a company which—
 - (i) is not subject to any such requirements as are mentioned in paragraphs (a), (b) or (d) above, and
 - (ii) is a company in whose case there are no accounts for the period in question that fall within paragraph (c) above,
 the accounts relating to the company that most closely correspond to the accounts which, in the case of a company formed and registered under the Companies Act 1985, are required under that Act.
- (9) For the purposes of subsection (8) above the home State of a company is the country or territory under whose law the company is incorporated.

87 Accounting method where parties have a connection

- (1) This section applies in the case of a loan relationship of a company where for any accounting period there is a connection between the company and—
 - (a) in the case of a debtor relationship of the company, a person standing in the position of a creditor as respects the debt in question; or
 - (b) in the case of a creditor relationship of the company, a person standing in the position of a debtor as respects that debt.
- (2) The only accounting method authorised for the purposes of this Chapter for use by the company as respects the loan relationship shall be an authorised accruals basis of accounting.
- (3) For the purposes of this section there is a connection between a company and another person for an accounting period if (subject to subsection (4) and section 88 below)—
 - (a) the other person is a company and there is a time in that period, or in the two years before the beginning of that period, when one of the companies has had control of the other;
 - (b) the other person is a company and there is a time in that period, or in those two years, when both the companies have been under the control of the same person; or

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- (c) there is a time in that accounting period, or in those two years, when the company was a close company and the other person was a participator in that company or the associate of a person who was such a participator at that time.
- (4) Two companies which have at any time been under the control of the same person shall not, by virtue of that fact, be taken for the purposes of this section to be companies between whom there is a connection if the person was the Crown, a Minister of the Crown, a government department, a Northern Ireland department, a foreign sovereign power or an international organisation.
- (5) The references in subsection (1) above to a person who stands in the position of a creditor or debtor as respects a loan relationship include references to a person who indirectly stands in that position by reference to a series of loan relationships.
- (6) Subsections (2) to (6) of section 416 of the Taxes Act 1988 (meaning of “control”) shall apply for the purposes of this section as they apply for the purposes of Part XI of that Act.
- (7) Subject to subsection (8) below, in this section “participator” and “associate” have the meanings given for the purposes of Part XI of the Taxes Act 1988 by section 417 of that Act.
- (8) A person shall not for the purposes of this section be regarded as a participator in relation to a company by reason only that he is a loan creditor of the company.

88 Exemption from section 87 in certain cases

- (1) Subject to subsection (5) below, where a creditor relationship of a company is one to which that company is a party in any accounting period in exempt circumstances, any connection for that accounting period between the company and a person who stands in the position of a debtor as respects the debt shall be disregarded for the purposes of section 87 above.
- (2) A company having a creditor relationship in any accounting period shall, for that period, be taken for the purposes of this section to be a party to that relationship in exempt circumstances if—
 - (a) the company, in the course of carrying on any activities forming an integral part of a trade carried on by that company in that period, disposes of or acquires assets representing creditor relationships;
 - (b) that period is one for which the company uses an authorised mark to market basis of accounting as respects all the creditor relationships represented by assets acquired in the course of those activities;
 - (c) the asset representing the creditor relationship in question was acquired in the course of those activities;
 - (d) that asset is either—
 - (i) listed on a recognised stock exchange at the end of that period; or
 - (ii) a security the redemption of which must occur within twelve months of its issue;
 - (e) there is a time in that period when assets of the same kind as the asset representing the loan relationship in question are in the beneficial ownership of persons other than the company; and

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- (f) there is not more than three months, in aggregate, in that accounting period during which the equivalent of 30 per cent. or more of the assets of that kind is in the beneficial ownership of connected persons.
- (3) An insurance company carrying on basic life assurance and general annuity business and having a creditor relationship in any accounting period shall, for that period, be taken for the purposes of this section to be a party to that relationship in exempt circumstances if—
- (a) assets of the company representing any of its creditor relationships are linked for that period to its basic life assurance and general annuity business;
 - (b) that period is one for which the company uses an authorised mark to market basis of accounting as respects all the creditor relationships of the company represented by assets that are so linked;
 - (c) the asset representing the creditor relationship in question is so linked;
 - (d) that asset is either—
 - (i) listed on a recognised stock exchange at the end of that period; or
 - (ii) a security the redemption of which must occur within twelve months of its issue;
 - (e) there is a time in that period when assets of the same kind as the asset representing the creditor relationship in question are in the beneficial ownership of persons other than the company; and
 - (f) there is not more than three months, in aggregate, in that accounting period during which the equivalent of 30 per cent. or more of the assets of that kind is in the beneficial ownership of connected persons.
- (4) For the purposes of subsections (2) and (3) above—
- (a) assets shall be taken to be of the same kind where they are treated as being of the same kind by the practice of any recognised stock exchange, or would be so treated if dealt with on such a stock exchange; and
 - (b) a connected person has the beneficial ownership of an asset wherever there is, or (apart from this section) would be, a connection (within the meaning of section 87 above) between—
 - (i) the person who has the beneficial ownership of the asset, and
 - (ii) a person who stands in the position of a debtor as respects the money debt by reference to which any loan relationship represented by that asset subsists.
- (5) Where for any accounting period—
- (a) subsection (1) above has effect in the case of a creditor relationship of a company, and
 - (b) the person who stands in the position of a debtor as respects the debt in question is also a company,
- that subsection shall not apply for determining, for the purposes of so much of section 87 above as relates to the corresponding debtor relationship, whether there is a connection between the two companies.
- (6) Subsection (5) of section 87 above shall apply for the purposes of this section as it applies for the purposes of that section.
- (7) In this section “basic life assurance and general annuity business” and “insurance company” have the same meanings as in Chapter I of Part XII of the Taxes Act 1988,

and section 432ZA of that Act (linked assets) shall apply for the purposes of this section as it applies for the purposes of that Chapter.

89 Inconsistent application of accounting methods

- (1) Where there is any inconsistency or other material difference between the way in which any authorised accounting method is applied as respects the same loan relationship in successive accounting periods, a balancing credit or balancing debit shall be brought into account in the second of those periods (“the second period”).
- (2) The amount of the balancing credit or debit shall be computed as respects the relationship in question by—
 - (a) taking the amount given by subsection (3) below and the amount given by subsection (4) below; and
 - (b) then aggregating those amounts (treating any debit as a negative amount) to produce a net credit or net debit.
- (3) The amount given by this subsection is whichever of the following is applicable—
 - (a) a debit equal to the amount (if any) by which the first of the following amounts exceeds the second, that is to say—
 - (i) the aggregate of the credits actually brought into account for all previous periods in which the accounting method was used; and
 - (ii) the aggregate of the credits that would have been brought into account if that method had been applied in those periods in the same way as it was applied in the second period;
 - (b) a credit equal to the amount (if any) by which the second aggregate mentioned in paragraph (a) above exceeds the first; or
 - (c) if both those aggregates are the same, nil.
- (4) The amount given by this subsection is whichever of the following is applicable—
 - (a) a credit equal to the amount (if any) by which the first of the following amounts exceeds the second, that is to say—
 - (i) the aggregate of the debits actually brought into account for all previous periods in which the accounting method was used; and
 - (ii) the aggregate of the debits that would have been brought into account if that method had been applied in those periods in the same way as it was applied in the second period;
 - (b) a debit equal to the amount (if any) by which the second aggregate mentioned in paragraph (a) above exceeds the first; or
 - (c) if both those aggregates are the same, nil.
- (5) In this section “previous period” means any accounting period before the second period.

90 Changes of accounting method

- (1) This section applies where different authorised accounting methods are used for the purposes of this Chapter as respects the same loan relationship for different parts of the same accounting period or for successive accounting periods.
- (2) Where, in the case of any loan relationship, the use of any authorised accounting method is superseded in the course of any accounting period by the use of another—

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- (a) the assumptions specified in subsection (4) below shall be made;
 - (b) each method shall be applied on those assumptions as respects the part of the period for which it is used; and
 - (c) the credits and debits given by the application of those methods on those assumptions shall be brought into account in the accounting period in which the change of method takes effect.
- (3) Where, in the case of any loan relationship, the use of any authorised accounting method is superseded as from the beginning of an accounting period by the use of another—
- (a) a net credit or debit shall be computed (treating any debit used in the computation as a negative amount) by—
 - (i) aggregating the credits and debits which, on the assumptions specified in subsection (4) below, would have been given in respect of that relationship for the successive accounting periods by the use for each period of the accounting method actually used for that period;
 - (ii) aggregating the credits and debits so given without the making of those assumptions; and
 - (iii) subtracting the second aggregate from the first;
 and
 - (b) the net credit or debit shall be brought into account for the purposes of this Chapter in the accounting period as from the beginning of which the change of method takes effect.
- (4) The assumptions mentioned in subsections (2) and (3) above are—
- (a) that the company ceased to be a party to the relationship immediately before the end of the period, or part of a period, for which the superseded method is used;
 - (b) that the company again became a party to that relationship as from the beginning of the period or, as the case may be, part of a period for which the other authorised accounting method is used;
 - (c) that the relationship to which the company is deemed to have become a party is separate and distinct from the one to which it is deemed to have ceased to be a party;
 - (d) that the amount payable under the transaction comprised in each of the assumptions specified in paragraphs (a) and (b) above was equal to the fair value of the relationship; and
 - (e) so far as relevant, that that amount became due at the time when the company is deemed to have ceased to be a party to the relationship or, as the case may be, to have again become a party to it.
- (5) Where—
- (a) a mark to market basis of accounting is superseded by an accruals basis of accounting in the case of any loan relationship, and
 - (b) the amount which would have accrued in respect of that relationship in the period or part of a period for which the accruals basis of accounting is used falls to be determined for the purposes of this section in accordance with the assumptions mentioned in subsection (4) above,
- that amount shall be taken for those purposes to be equal to the amount resulting from the subtraction of the amount given by subsection (6)(a) below from the amount given by subsection (6)(b) below.

- (6) Those amounts are—
- (a) the amount which by virtue of the assumptions mentioned in subsection (4) above is given as an opening value for the period or part of a period; and
 - (b) the amount equal to whatever, in the computation in accordance with an authorised accruals basis of accounting of the amount accruing in that period or part of a period, would have been taken to be the closing value applicable as at the end of that period or part of a period if such a basis of accounting had always been used as respects the relationship.
- (7) In this section “fair value” has the same meaning as in section 85 above.

91 Payments subject to deduction of tax

- (1) This section applies where—
- (a) any company receives a payment of interest on which it bears income tax by deduction; and
 - (b) in the case of that company, a credit relating to that interest has been brought into account for the purposes of this Chapter for an accounting period ending more than two years before the receipt of the payment.
- (2) On a claim made by the company to an officer of the Board, section 7(2) or, as the case may be, 11(3) of the Taxes Act 1988 (deducted income tax to be set against liability to corporation tax) shall have effect in relation to the income tax on the payment as if the interest had fallen to be taken into account for the purposes of corporation tax in the accounting period in which the payment of that interest is received.
- (3) In determining for the purposes of this section which accounting period is the accounting period for which a credit relating to interest paid subsequently was brought into account, every payment of interest to a company under a loan relationship of that company shall be assumed to be a payment in discharge of the earliest outstanding liability to that company in respect of interest payable under the relationship.
- (4) For the purposes of this section, the earliest outstanding liability to interest payable under a loan relationship of a company shall be identified, in relation to any payment of such interest, according to the authorised accounting method most recently used as respects that relationship, so that—
- (a) if that method is an authorised accruals basis of accounting, it shall be determined by reference to the time when the interest accrued; and
 - (b) if that method is an authorised mark to market basis of accounting, it shall be determined by reference to the time when the interest became due and payable.
- (5) In subsection (4) above the reference, in relation to a payment of interest made to a company in any accounting period, to the authorised accounting method most recently used as respects that relationship is a reference to the authorised accounting method which, in the case of that company, has been used as respects that relationship for the accounting period which, when the payment is made, is the most recent for which amounts in respect of that relationship have been brought into account for the purposes of this Chapter.
- (6) A claim under this section shall not be made in respect of any payment of interest at any time after the later of the following, that is to say—
- (a) the time two years after the end of the accounting period in which the payment is received; and

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- (b) the time six years after the end of the accounting period for which the credit in respect of the interest was brought into account for the purposes of this Chapter.
- (7) Where—
- (a) there is a payment of interest to a company under a loan relationship of that company, and
 - (b) the company is prevented by virtue of subsection (6) above from making any claim under this section in respect of that payment,
- the company shall not be entitled to make any claim under paragraph 5 of Schedule 16 to the Taxes Act 1988 (set off of income tax borne against income tax payable) in respect of that payment.

Special cases

92 Convertible securities etc

- (1) This section applies to an asset if—
- (a) the asset represents a creditor relationship of a company;
 - (b) the rights attached to the asset include provision by virtue of which the company is or may become entitled to acquire (whether by conversion or exchange or otherwise) any shares in a company;
 - (c) the extent to which shares may be acquired under that provision is not determined using a cash value which is specified in that provision or which is or will be ascertainable by reference to the terms of that provision;
 - (d) the asset is not a relevant discounted security within the meaning of Schedule 13 to this Act;
 - (e) at the time when the asset came into existence there was a more than negligible likelihood that the right to acquire shares in a company would in due course be exercised to a significant extent; and
 - (f) the asset is not one the disposal of which by the company would fall to be treated as a disposal in the course of activities forming an integral part of a trade carried on by the company.
- (2) The amounts falling for any accounting period to be brought into account for the purposes of this Chapter in respect of a creditor relationship represented by an asset to which this section applies shall be confined to amounts relating to interest.
- (3) Only an authorised accruals basis of accounting shall be used for ascertaining those amounts.
- (4) Amounts shall be brought into account in computing the profits of the company for the purposes of corporation tax as if the Taxation of Chargeable Gains Act 1992 had effect in relation to any asset to which this section applies as it has effect in relation to an asset that does not represent a loan relationship.
- (5) For the purposes of that Act the amount or value of the consideration for any disposal or acquisition of the asset shall be treated as adjusted so as to exclude so much of it as, on a just and reasonable apportionment, relates to any interest which—
- (a) falls to be brought into account under subsections (2) and (3) above as accruing to any company at any time; and

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- (b) in consequence of, or of the terms of, the disposal or acquisition, is not paid or payable to the company to which it is treated for the purposes of this Chapter as accruing.
- (6) In subsection (5) above the references to a disposal, in relation to an asset, are references to anything which—
- (a) is a disposal of that asset (within the meaning of the Taxation of Chargeable Gains Act 1992); or
 - (b) would be such a disposal but for section 127 or 116(10) of that Act (reorganisations etc.);
- and the references to the acquisition of an asset shall be construed accordingly.

93 Relationships linked to the value of chargeable assets

- (1) This section applies in the case of any loan relationship of a company that is linked to the value of chargeable assets unless it is one the disposal of which by the company would fall to be treated as a disposal in the course of activities forming an integral part of a trade carried on by the company.
- (2) The amounts falling for any accounting period to be brought into account for the purposes of this Chapter in respect of the relationship shall be confined to amounts relating to interest.
- (3) Only an authorised accruals basis of accounting shall be used for ascertaining those amounts.
- (4) Amounts shall be brought into account in computing the profits of the company for the purposes of corporation tax as if the Taxation of Chargeable Gains Act 1992 had effect in relation to the asset representing the relationship as it has effect in relation to an asset that does not represent a loan relationship.
- (5) For the purposes of that Act the amount or value of the consideration for any disposal or acquisition of the asset shall be treated as adjusted so as to exclude so much of it as, on a just and reasonable apportionment, relates to any interest which—
 - (a) falls to be brought into account under subsections (2) and (3) above as accruing to any company at any time; and
 - (b) in consequence of, or of the terms of, the disposal or acquisition, is not paid or payable to the company to which it is treated for the purposes of this Chapter as accruing.
- (6) For the purposes of this section a loan relationship is linked to the value of chargeable assets if, in pursuance of any provision having effect for the purposes of that relationship, the amount that must be paid to discharge the money debt (whether on redemption of a security issued in relation to that debt or otherwise) is equal to the amount determined by applying a relevant percentage change in the value of chargeable assets to the amount falling for the purposes of this Chapter to be regarded as the amount of the original loan from which the money debt arises.
- (7) In subsection (6) above the reference to a relevant percentage change in the value of chargeable assets is a reference to the amount of the percentage change (if any) over the relevant period in the value of chargeable assets of any particular description or in any index of the value of any such assets.
- (8) In subsection (7) above “the relevant period” means—

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- (a) the period between the time of the original loan and the discharge of the money debt; or
 - (b) any other period in which almost all of that period is comprised and which differs from that period exclusively for purposes connected with giving effect to a valuation in relation to rights or liabilities under the loan relationship.
- (9) If—
- (a) there is a provision which, in the case of any loan relationship, falls within subsection (6) above,
 - (b) that provision is made subject to any other provision applying to the determination of the amount payable to discharge the money debt,
 - (c) that other provision is to the effect only that the amount so payable must not be less than a specified percentage of the amount falling for the purposes of this Chapter to be regarded as the amount of the original loan, and
 - (d) the specified percentage is not more than 10 per cent.,
- that other provision shall be disregarded in determining for the purposes of this section whether the relationship is linked to the value of chargeable assets.
- (10) For the purposes of this section an asset is a chargeable asset, in relation to a loan relationship of a company, if any gain accruing on the disposal of the asset by the company on or after 1st April 1996 would, on the assumptions specified in subsection (11) below, be a chargeable gain for the purposes of the Taxation of Chargeable Gains Act 1992.
- (11) Those assumptions are—
- (a) where it is not otherwise the case, that the asset is an asset of the company;
 - (b) that the asset is not one the disposal of which by the company would fall to be treated for the purposes of corporation tax as a disposal in the course of a trade carried on by the company; and
 - (c) that chargeable gains that might accrue under section 116(10) of that Act (postponed charges) are to be disregarded.
- (12) In subsection (5) above references to a disposal, in relation to an asset, are references to anything which—
- (a) is a disposal of that asset (within the meaning of the Taxation of Chargeable Gains Act 1992); or
 - (b) would be such a disposal but for section 127 or 116(10) of that Act (reorganisations etc.);
- and the references to the acquisition of an asset shall be construed accordingly.
- (13) For the purposes of this section neither—
- (a) the retail prices index, nor
 - (b) any similar general index of prices published by the government of any territory or by the agent of any such government,
- shall be taken to be an index of the value of chargeable assets.

94 Indexed gilt-edged securities

- (1) In the case of any loan relationship represented by an index-linked gilt-edged security, the adjustment for which this section provides shall be made in computing the credits and debits which fall, for any accounting period, to be brought into account for the

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purposes of this Chapter in respect of that relationship as non-trading credits or non-trading debits.

- (2) The adjustment shall be made wherever—
 - (a) the authorised accounting method applied as respects the index-linked gilt-edged security gives credits or debits by reference to the value of the security at two different times, and
 - (b) there is any change in the retail prices index between those times.
- (3) Subject to subsection (4) below, the adjustment is such an adjustment of the amount which would otherwise be taken for the purposes of that accounting method to be the value of the security at the earlier time (“the opening value”) as results in the amount in fact so taken being equal to the opening value increased or, as the case may be, reduced by the same percentage as the percentage increase or reduction in the retail prices index between the earlier and the later time.
- (4) The Treasury may, in relation to any description of index-linked gilt-edged securities, by order provide that—
 - (a) there are to be no adjustments under this section; or
 - (b) that an adjustment specified in the order (instead of the adjustment specified in subsection (3) above) is to be the adjustment for which this section provides.
- (5) An order under subsection (4) above—
 - (a) shall not have effect in relation to any gilt-edged security issued before the making of the order; but
 - (b) may make different provision for different descriptions of securities.
- (6) For the purposes of this section the percentage increase or reduction in the retail prices index between any two times shall be determined by reference to the difference between—
 - (a) that index for the month in which the earlier time falls; and
 - (b) that index for the month in which the later time falls.
- (7) In this section “index-linked gilt-edged securities” means any gilt-edged securities the amounts of the payments under which are determined wholly or partly by reference to the retail prices index.

95 Gilt strips

- (1) This section has effect for the purposes of the application of an authorised accruals basis of accounting as respects a loan relationship represented by a gilt-edged security or a strip of a gilt-edged security.
- (2) Where a gilt-edged security is exchanged by any person for strips of that security—
 - (a) the security shall be deemed to have been redeemed at the time of the exchange by the payment to that person of its market value; and
 - (b) that person shall be deemed to have acquired each strip for the amount which bears the same proportion to that market value as is borne by the market value of the strip to the aggregate of the market values of all the strips received in exchange for the security.
- (3) Where strips of a gilt-edged security are consolidated into a single gilt-edged security by being exchanged by any person for that security—

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- (a) each of the strips shall be deemed to have been redeemed at the time of the exchange by the payment to that person of the amount equal to its market value; and
 - (b) that person shall be deemed to have acquired the security received in the exchange for the amount equal to the aggregate of the market values of the strips given in exchange for the security.
- (4) References in this section to the market value of a security given or received in exchange for another are references to its market value at the time of the exchange.
- (5) Without prejudice to the generality of any power conferred by section 202 below, the Treasury may by regulations make provision for the purposes of this section as to the manner of determining the market value at any time of any gilt-edged security (including any strip).
- (6) Regulations under subsection (5) above may—
- (a) make different provision for different cases; and
 - (b) contain such incidental, supplemental, consequential and transitional provision as the Treasury may think fit.
- (7) In this section “strip” means anything which, within the meaning of section 47 of the Finance Act 1942, is a strip of a gilt-edged security.

96 Special rules for certain other gilts

- (1) This section applies as respects any loan relationship of a company if—
- (a) it is represented by a security of any of the following descriptions—
 - (i) 3½% Funding Stock 1999-2004; or
 - (ii) 5½% Treasury Stock 2008-2012;
 and
 - (b) it is one to which the company is a party otherwise than in the course of activities that form an integral part of a trade carried on by the company.
- (2) The amounts falling for any accounting period to be brought into account for the purposes of this Chapter in respect of a loan relationship to which this section applies shall be confined to amounts relating to interest.
- (3) Only an authorised accruals basis of accounting shall be used for ascertaining those amounts.

97 Manufactured interest

- (1) This section applies where—
- (a) any amount (“manufactured interest”) is payable by or on behalf of, or to, any company under any contract or arrangements relating to the transfer of an asset representing a loan relationship; and
 - (b) that amount is, or (when paid) will fall to be treated as, representative of interest under that relationship (“the real interest”).
- (2) In relation to that company the manufactured interest shall be treated for the purposes of this Chapter—
- (a) as if it were interest under a loan relationship to which the company is a party; and

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- (b) where that company is the company to which the manufactured interest is payable, as if that relationship were the one under which the real interest is payable.
- (3) Any question whether debits or credits falling to be brought into account in the case of any company by virtue of this section—
 - (a) are to be brought into account under section 82(2) above, or
 - (b) are to be treated as non-trading debits or non-trading credits,shall be determined according to the extent (if any) to which the manufactured interest is paid for the purposes of a trade carried on by the company or is received in the course of activities forming an integral part of such a trade.
- (4) Where section 737A(5) of the Taxes Act 1988 (deemed manufactured payments) has effect in relation to a transaction relating to an asset representing a loan relationship so as, for the purposes of section 737 of, or Schedule 23A to, that Act, to deem there to have been a payment representative of interest under that relationship, this section shall apply as it would have applied if such a representative payment had in fact been made.
- (5) This section does not apply where the manufactured interest is treated by virtue of paragraph 5(2)(c) or (4)(c) of Schedule 23A to the Taxes Act 1988 (manufactured interest passing through the market) as not being income of the person who receives it.

98 Collective investment schemes

The provisions of this Chapter have effect subject to the provisions of Schedule 10 to this Act (which makes special provision in relation to certain collective investment schemes).

99 Insurance companies

The preceding provisions of this Chapter have effect subject to Schedule 11 to this Act (which makes special provision in relation to certain insurance companies and in relation to corporate members of Lloyd's).

Miscellaneous other provisions

100 Interest on judgments, imputed interest, etc

- (1) This Chapter shall have effect in accordance with subsection (2) below where—
 - (a) interest on a money debt is payable to or by any company;
 - (b) that debt is one as respects which it stands, or has stood, in the position of a creditor or debtor; and
 - (c) that debt did not arise from a loan relationship.
- (2) It shall be assumed for the purposes of this Chapter—
 - (a) that the interest is interest payable under a loan relationship to which the company is a party; but
 - (b) that the only credits or debits to be brought into account for those purposes in respect of that relationship are those relating to the interest.

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- (3) References in this section to interest payable on a money debt include references to any amount which, in pursuance of sections 770 to 772 of the Taxes Act 1988 (transactions at an undervalue or overvalue), as those sections have effect by virtue of section 773(4) of that Act, falls to be treated in pursuance of those sections as—
- (a) interest on a money debt; or
 - (b) interest on an amount which is treated as a money debt.
- (4) Any question whether debits or credits falling to be brought into account in accordance with this section in relation to any company—
- (a) are to be brought into account under section 82(2) above, or
 - (b) are to be treated as non-trading debits or non-trading credits,
- shall be determined according to the extent (if any) to which the interest in question is paid for the purposes of a trade carried on by the company or is received in the course of activities forming an integral part of such a trade, or (in the case of deemed interest) would be deemed to be so paid or received.
- (5) This section has effect subject to the provisions of Schedules 9 and 11 to this Act.

101 Financial instruments

- (1) Chapter II of Part IV of the Finance Act 1994 (provisions relating to certain financial instruments) shall not apply to any profit or loss which, in accordance with that Chapter, accrues to a company for any accounting period on a qualifying contract by virtue of which the company is a party to any loan relationship if—
- (a) an amount representing that profit or loss, or
 - (b) an amount representing the profit or loss accruing to that company on that contract,
- is brought into account for that period for the purposes of this Chapter.
- (2) After section 147 of that Act (qualifying contracts) there shall be inserted the following section—

“147A Debt contracts and options to be qualifying contracts

- (1) For the purposes of this Chapter a debt contract or option is a qualifying contract as regards a qualifying company if the company becomes entitled to rights, or subject to duties, under the contract or option at any time on or after 1st April 1996.
 - (2) For the purposes of this Chapter a qualifying company which is entitled to rights, or subject to duties, under a debt contract or option both immediately before and on 1st April 1996 shall be deemed to have become entitled or subject to those rights or duties on that date.
 - (3) This section has effect subject to paragraph 25 of Schedule 15 to the Finance Act 1996 (transitional provisions).”
- (3) After section 150 of that Act (qualifying contracts) there shall be inserted the section set out in Schedule 12 to this Act (which defines debt contracts and options by reference to contracts and options conferring rights and duties to participate in loan relationships).

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- (4) In section 151 of that Act (provisions that may be included in contracts and options), for the words “or a currency contract or option,”, in each place where they occur, there shall be substituted “a currency contract or option or a debt contract or option”.
- (5) In section 152(1) of that Act (disregard of provisions for relatively small payments in contracts and options), after “150” there shall be inserted “or 150A”.
- (6) In section 153(1) of that Act (qualifying payments), for the word “and” at the end of paragraph (c) there shall be substituted—
 - “(ca) in relation to a qualifying contract which is a debt contract, a payment falling within section 150A(5) or (6) above; and”.

102 Discounted securities: income tax provisions

Schedule 13 to this Act (which, in connection with the provisions of this Chapter relating to corporation tax, makes provision for income tax purposes about discounted securities) shall have effect.

Supplemental

103 Interpretation of Chapter

- (1) In this Chapter—
 - “authorised accounting method”, “authorised accruals basis of accounting” and “authorised mark to market basis of accounting” shall be construed in accordance with section 85 above;
 - “creditor relationship”, in relation to a company, means any loan relationship of that company in the case of which it stands in the position of a creditor as respects the debt in question;
 - “debt” includes a debt the amount of which falls to be ascertained by reference to matters which vary from time to time;
 - “debtor relationship”, in relation to a company, means any loan relationship of that company in the case of which it stands in the position of a debtor as respects the debt in question;
 - “gilt-edged securities” means any securities which—
 - (a) are gilt-edged securities for the purposes of the Taxation of Chargeable Gains Act 1992; or
 - (b) will be such securities on the making of any order under paragraph 1 of Schedule 9 to that Act the making of which is anticipated in the prospectus under which they are issued;
 - “an independent person” means a knowledgeable and willing party dealing at arm’s length;
 - “international organisation” means an organisation of which two or more sovereign powers, or the governments of two or more sovereign powers, are members;
 - “loan” includes any advance of money, and cognate expressions shall be construed accordingly;
 - “money” shall be construed in accordance with section 81(6) above and subsection (5) below;
 - “money debt” shall be construed in accordance with section 81(2) above;

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“non-trading credit” and “non-trading debit” shall be construed in accordance with section 82(3) above;

“retail prices index” has the same meaning as it has, by virtue of section 833(2) of the Taxes Act 1988, in the Income Tax Acts;

“share”, in relation to a company, means any share in the company under which an entitlement to receive distributions may arise.

- (2) For the purposes of this Chapter a company shall be taken to be a party to a creditor relationship for the purposes of a trade carried on by that company only if it is a party to that relationship in the course of activities forming an integral part of that trade.
- (3) For the purposes of this Chapter, and of so much of any other enactment as contains provision by reference to which amounts fall to be brought into account for the purposes of this Chapter, activities carried on by a company in the course of—
 - (a) any mutual trading, or
 - (b) any mutual insurance or other mutual business which is not life assurance business (within the meaning of Chapter I of Part XII of the Taxes Act 1988),
 shall be deemed not to constitute the whole or any part of a trade.
- (4) If, in any proceedings, any question arises whether a person is an international organisation for the purposes of any provision of this Chapter, a certificate issued by or under the authority of the Secretary of State stating any fact relevant to that question shall be conclusive evidence of that fact.
- (5) For the purposes of this Chapter the European currency unit (as for the time being defined in Council Regulation No. 3180/78/EEC or in any Community instrument replacing it) shall be taken to be a currency other than sterling.

104 Minor and consequential amendments

Schedule 14 to this Act (which, for the purposes of both corporation tax and income tax, makes certain minor and consequential amendments in connection with the provisions of this Chapter) shall have effect.

105 Commencement and transitional provisions

- (1) Subject to Schedule 15 to this Act, this Chapter has effect—
 - (a) for the purposes of corporation tax, in relation to accounting periods ending after 31st March 1996; and
 - (b) so far as it makes provision for the purposes of income tax, in relation to the year 1996-97 and subsequent years of assessment.
- (2) Schedule 15 to this Act (which contains transitional provisions and savings in connection with the coming into force of this Chapter) shall have effect.