

SCHEDULES

SCHEDULE 23

EXCHANGE GAINS AND LOSSES FROM LOAN RELATIONSHIPS ETC

PART 1

AMENDMENTS OF THE FINANCE ACT 1996

Introductory

- 1 Chapter 2 of Part 4 of the Finance Act 1996 (c. 8) (loan relationships) is amended in accordance with the following provisions of this Part.

Meaning of “related transaction”

- 2 (1) Section 84 (debts and credits brought into account) is amended as follows.
- (2) In subsection (5) (meaning of “related transaction” in the section) for “In this section” substitute “In this Chapter”.
- (3) In subsection (6) (disposals and acquisitions for the purposes of the section) for “for the purposes of this section” substitute “for the purposes of subsection (5) above”.

Exchange gains and losses from loan relationships etc

- 3 After section 84 (debts and credits brought into account) insert—

“84A Exchange gains and losses from loan relationships

- (1) The reference in section 84(1)(a) above to the profits, gains and losses arising to a company from its loan relationships and related transactions includes a reference to exchange gains and losses arising to the company from its loan relationships.
- (2) Subsection (1) above is subject to the following provisions of this section.
- (3) Subsection (1) above does not have effect in relation to—
- (a) so much of an exchange gain or loss arising to a company in relation to an asset representing a loan relationship of the company as falls within subsection (4) below; or
 - (b) so much of an exchange gain or loss arising to a company in relation to a liability representing a loan relationship of the company as falls within subsection (5) below; or
 - (c) so much of any exchange gain or loss arising to a company as results from any translation from one currency to another pursuant

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- to section 93A(4) of the Finance Act 1993 of the profit or loss of part of the company's business and falls within subsection (4) below; or
- (d) so much of an exchange gain or loss arising to a company in relation to an asset or liability representing a loan relationship of the company as falls within a description prescribed for the purpose in regulations made by the Treasury.
- (4) For the purposes of subsection (3)(a) or (c) above, an exchange gain or loss falls within this subsection to the extent that, in accordance with generally accepted accounting practice, an amount representing the whole or part of it is carried to or sustained by a reserve maintained by the company.
- (5) For the purposes of subsection (3)(b) above, an exchange gain or loss falls within this subsection to the extent that, in accordance with generally accepted accounting practice, an amount representing the whole or part of it—
- (a) is carried to or sustained by a reserve maintained by the company; and
- (b) is set off by or against an amount falling within subsection (6) below.
- (6) An amount falls within this subsection if—
- (a) it represents the whole or part of an exchange gain or loss arising to the company in relation to any asset of the company; and
- (b) in accordance with generally accepted accounting practice it is carried to or sustained by the reserve mentioned in subsection (5) (a) above.
- (7) Where by virtue of subsection (3) above subsection (1) above does not have effect in relation to an amount representing the whole or part of an exchange gain or loss, section 84(2)(b) above shall not have effect in relation to that amount (but this subsection is subject to regulations under subsection (8) below).
- (8) The Treasury may by regulations make provision for or in connection with bringing into account in prescribed circumstances amounts in relation to which subsection (1) above does not, by virtue of subsection (3) above, have effect.
- (9) The reference in subsection (8) above to bringing amounts into account is a reference to bringing amounts into account—
- (a) for the purposes of this Chapter, as credits or debits in respect of the loan relationships of the company concerned; or
- (b) for the purposes of the Taxation of Chargeable Gains Act 1992.
- (10) Any power to make regulations under this section includes power to make different provision for different cases.”.

Authorised accounting methods

- 4 (1) Section 85 is amended as follows.
- (2) In subsection (2) (accounting methods authorised only if the conditions in the paragraphs of the subsection are satisfied) after paragraph (b) insert—

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“(bb) it contains proper provision for determining exchange gains and losses from loan relationships for accounting periods; and”.

- (3) In paragraph (c) of that subsection (accruals basis not to give debits by reference to valuation at different times of asset representing loan relationship) after “(other than” insert “provision in respect of exchange losses or”.

Convertible securities etc: exchange gains and losses

- 5 (1) Section 92 (convertible securities etc: creditor relationships) is amended as follows.

- (2) In subsection (2) (which, in the case of securities to which the section applies, confines the amounts to be brought into account under the Chapter to interest) after “confined to” insert “(a)” and at the end of the subsection add “; and

(b) amounts relating to exchange gains or losses”.

- (3) After subsection (5) (consideration for purposes of Taxation of Chargeable Gains Act 1992 (c. 12) to be adjusted by excluding certain amounts relating to interest brought into account under subsections (2) and (3)) insert—

“(5A) For the purposes of that Act the amount or value of the consideration for any disposal of the asset—

- (a) shall be increased by the addition of any relevant exchange losses, determined in accordance with subsection (5C) below; and
(b) shall (after giving effect to any such increase) be reduced (but not below nil) by the deduction of any relevant exchange gains, determined in accordance with that subsection.

(5B) In subsection (5C) below—

“relevant accounting period” means any accounting period beginning on or after 1st October 2002; and

“the relevant condition” is that the asset in question is an asset to which this section applies and is held by the company making the disposal.

(5C) For the purposes of subsection (5A) above, relevant exchange gains or, as the case may be, losses in the case of any asset are—

- (a) the amount of any exchange gains or, as the case may be, losses brought into account under subsections (2) and (3) above in respect of the asset, by the company making the disposal, for a relevant accounting period throughout which the relevant condition is satisfied; and
(b) for any relevant accounting period not falling within paragraph (a) above in which the relevant condition is at some time satisfied, an amount which, on a just and reasonable apportionment, represents so much of the amount of any exchange gains or, as the case may be, losses brought into account under subsections (2) and (3) above in respect of the asset, by the company making the disposal, for that period as is referable to the part of the period for which the relevant condition is satisfied.

(5D) Where—

- (a) the amount of the relevant exchange gains falling to be deducted under subsection (5A)(b) above, exceeds

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- (b) the amount required to reduce the amount or value of the consideration to nil,
the excess shall be treated for the purposes of section 38(1)(c) of the Taxation of Chargeable Gains Act 1992 as incidental costs of making the disposal of the asset.”.
- (4) In subsection (6)—
 - (a) in the opening words (construction of references to disposal in subsection (5)) for “subsection (5)” substitute “subsections (5) and (5A)”; and
 - (b) in paragraph (b) (disposals within the meaning of the Taxation of Chargeable Gains Act 1992 but for section 127 or 116(10)) omit “127 or”.
- (5) In subsection (9) (which, subject to subsection (10), gives the meaning of “the relevant consideration”) for “subsection (10)” substitute “subsections (10) and (10A)”.
- (6) After subsection (10) (which disapplies subsection (5) in the case of a deemed disposal and re-acquisition under subsection (7) but makes corresponding provision) insert—

“(10A) Subsection (5A) above shall not apply in the case of a deemed disposal and re-acquisition under subsection (7) above; but in any such case the amount of the relevant consideration, after any reduction under subsection (10) above, shall be treated for the purposes of the Taxation of Chargeable Gains Act 1992 as further adjusted by making the same additions and deductions (and for the purposes of both the disposal and the re-acquisition) as would fall to be made under subsection (5A) above if it were the consideration for an actual disposal and that subsection also applied in relation to the corresponding acquisition.”.

Extension of section 100 to exchange gains and losses and to items other than money debts

- 6 For section 100 (interest on judgments, imputed interest, etc) substitute—

“100 Interest, and exchange gains and losses, on debts etc not arising from the lending of money

- (1) For the purposes of the Corporation Tax Acts, a company has a relationship to which this section applies in any case where—
 - (a) the company stands, or has stood, in the position of a creditor or debtor as respects a money debt;
 - (b) the money debt is not one which arose from a transaction for the lending of money (so that, in consequence of section 81(1)(b) above, there is no loan relationship); and
 - (c) the money debt is one—
 - (i) on which interest is payable to or by the company; or
 - (ii) in relation to which exchange gains or losses arise to the company;

and references to a relationship to which this section applies, and to a company’s being party to such a relationship, shall be construed accordingly.

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- (2) Where a company has a relationship to which this section applies—
- (a) this Chapter shall have effect in relation to the interest payable under, or the exchange gains or losses arising to the company from, the relationship as it has effect in relation to interest payable under, or (as the case may be) exchange gains or losses arising to the company from, a loan relationship to which the company is a party; but
 - (b) the only credits or debits to be brought into account for the purposes of this Chapter in respect of the relationship are those relating to the interest or (as the case may be) to the exchange gains or losses;
- and, subject to paragraph above, references in the Corporation Tax Acts to a loan relationship accordingly include a reference to a relationship to which this section applies.
- (3) References in this section to interest payable on a money debt include a reference to any amount which, in pursuance of Schedule 28AA to the Taxes Act 1988 (provision not at arm's length), falls to be treated as—
- (a) interest on a money debt; or
 - (b) interest on an amount which is treated as a money debt;
- and references in the other provisions of this section to a money debt accordingly include a reference to the amount on which that amount so falls to be treated as interest.
- (4) Except as provided by subsection (7) below, any question whether debits or credits falling to be brought into account by virtue of this section in relation to a 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 in accordance with subsection (5) below (in the case of interest) or subsection (6) below (in the case of an exchange gain or loss).
- (5) In the case of interest, any such question shall be determined according to the extent (if any) to which the interest—
- (a) is paid for the purposes of a trade carried on by the company;
 - (b) is received in the course of activities forming an integral part of such a trade; or
 - (c) in the case of deemed interest, would be deemed to be so paid or received.
- (6) In the case of an exchange gain or loss, any such question shall be determined according to the extent (if any) to which the money debt—
- (a) is owed by the company for the purposes of a trade carried on by the company; or
 - (b) is held in the course of activities forming an integral part of such a trade.
- (7) Any debits or credits which—
- (a) relate to interest payable under the Tax Acts, and
 - (b) fall to be brought into account by virtue of this section in relation to any company,
- are to be treated as non-trading debits or credits.

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- (8) To the extent that debits or credits fall to be brought into account by a company under section 82(2) above in the case of a relationship to which this section applies, the company shall be regarded for the purposes of the Corporation Tax Acts as being party to the relationship for the purposes of a trade carried on by the company.
- (9) No exchange gains or losses shall be taken to arise for the purposes of this section if the money debt in question—
- (a) is an amount of tax,
 - (b) is an amount of tax payable under the law of a territory outside the United Kingdom, or
 - (c) is an amount which would, but for any statutory provision or rule of law to the contrary other than section 74(1)(f) or (g) of the Taxes Act 1988, be deductible as an expense in computing profits in accordance with Case I of Schedule D or as an expense of management within section 75 of the Taxes Act 1988,
- except to the extent that, in the case of a money debt falling within paragraph (b) above, a reduction in respect of the tax there mentioned falls to be made under section 811 of the Taxes Act 1988 (double taxation relief: deduction for foreign tax where no credit allowable).
- (10) For the purposes of this section so far as relating to exchange gains and losses, each of the following shall be treated as a money debt owed to a company—
- (a) any currency held by the company;
 - (b) in the case of a company carrying on insurance business, any deferred acquisition costs, within the meaning of Assets item G.II in the Balance Sheet Format set out after paragraph 9 of Schedule 9A to the Companies Act 1985 (form and content of accounts of insurance companies and groups) as read with note (17) of the Notes on the Balance Sheet Format (which follow immediately after that format).
- (11) For the purposes of this section so far as relating to exchange gains and losses, each of the following shall be treated as a money debt owed by a company—
- (a) any provision made by the company for the purposes of its statutory accounts in respect of a liability to which the company may become subject;
 - (b) in the case of a company carrying on insurance business—
 - (i) any provision made by the company for unearned premiums, within the meaning of Liabilities item C.1 in the Balance Sheet Format set out after paragraph 9 of Schedule 9A to the Companies Act 1985, as read with note (20) of the Notes on the Balance Sheet Format (which follow immediately after that format);
 - (ii) any provision for unexpired risks, as defined in paragraph 81(1) of that Schedule.
- (12) A provision does not fall within paragraph (a) of subsection (11) above unless—
- (a) the duty to settle the liability in question would (if the company were to become subject to it) be owed for the purposes of a trade,

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- a Schedule A business or an overseas property business (within the meaning of section 70A of the Taxes Act 1988); and
 - (b) the provision falls to be taken into account (apart from this Chapter) in computing the profits or losses of the trade, Schedule A business or overseas property business for corporation tax purposes.
- (13) This section has effect subject to the provisions of Schedules 9 and 11 to this Act.”.

Interpretation

- 7 (1) Section 103 is amended as follows.
- (2) In subsection (1) (definitions) insert each of the following definitions at the appropriate place—
- ““exchange gain” and “exchange loss” shall be construed in accordance with subsections (1A) and (1B) below;”;
 - ““related transaction” shall be construed in accordance with section 84 above (see subsections (5) and (6) of that section);”.
- (3) After subsection (1) insert—
- “(1A) References in this Chapter to exchange gains or exchange losses, in the case of any company, are references respectively to—
 - (a) profits or gains, or
 - (b) losses,which arise as a result of comparing at different times the expression in one currency of the whole or some part of the valuation put by the company in another currency on an asset or liability of the company.
 - If the result of such a comparison is that neither an exchange gain nor an exchange loss arises, then for the purposes of this Chapter an exchange gain of nil shall be taken to arise in the case of that comparison.
 - (1B) Any reference in this Chapter to an exchange gain or loss from a loan relationship of a company is a reference to an exchange gain or loss arising to a company in relation to an asset or liability representing a loan relationship of the company.”.

Bad debt etc: cases where departure allowed from assumption of prompt payment in full

- 8 (1) Paragraph 5 of Schedule 9 is amended as follows.
- (2) After sub-paragraph (1) (departure from assumption of full and prompt payment of debt allowed only to extent debt is bad debt etc) insert—
- “(1A) Such a departure shall be made only where the first and second conditions (set out in sub-paragraphs (2) and (2A) below) are satisfied.”.
- (3) In sub-paragraph (2) (requirement for appropriate adjustments in form of credits where bad debt etc is paid or departure otherwise ceases to be allowed) for “Such a departure shall be made only where” substitute “The first condition is that”.
- (4) After sub-paragraph (2) insert—

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- “(2A) The second condition is that, in determining the credits and debits to be brought into account in respect of exchange gains and losses, the accounting arrangements allowing the departure require a debt—
- (a) to be left out of account, to the extent that such a departure is allowed; and
 - (b) to be taken into account again, to the extent that it is represented by credits brought into account under sub-paragraph (2) above.”.

Bad debts etc where parties have a connection

- 9 (1) Paragraph 6 of Schedule 9 is amended as follows.
- (2) In sub-paragraph (3) (assumption that debts will be paid in full to be applied as if no departure authorised by virtue of paragraph 5 except as provided by sub-paragraph (4)) for “paragraph 5” substitute “paragraph 5(1)”.
- (3) At the end of the paragraph add—
- “(8) Nothing in this paragraph affects the debits or credits to be brought into account for the purposes of this Chapter in respect of exchange gains or losses arising from a debt.”.

Transactions not at arm’s length

- 10 (1) Paragraph 11 of Schedule 9 is amended as follows.
- (2) In sub-paragraph (1), for “Subject to sub-paragraphs (2) and (3) below,” substitute “Subject to sub-paragraphs (2) to (3A) below,”.
- (3) After sub-paragraph (3) insert—
- “(3A) Sub-paragraph (1) above shall not apply to any exchange gains or losses.”.

Exchange gains and losses where loan not on arm’s length terms

- 11 After paragraph 11 of Schedule 9 insert the following paragraph—

“Exchange gains and losses where loan not on arm’s length terms

- 11A (1) Where a company has a debtor relationship in an accounting period and in the case of that accounting period—
- (a) the whole of any interest or other distribution out of the assets of the company in respect of securities of the company that represent the relationship falls by virtue of section 209(2)(da) or (e)(vii) of the Taxes Act 1988 to be regarded as a distribution for the purposes of the Corporation Tax Acts, or
 - (b) the profits and losses of the company fall by virtue of Schedule 28AA to that Act (provision not at arm’s length) to be computed for tax purposes as if the loan had not been made,
- any exchange gains or losses which arise in that accounting period in respect of a liability representing the debtor relationship shall be left out of account in determining the debits or credits to be brought into account for the purposes of this Chapter.

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(2) Where a company has a debtor relationship in an accounting period and in the case of that accounting period—

- (a) part of any interest or other distribution out of the assets of the company in respect of securities of the company that represent the relationship falls by virtue of section 209(2)(da) or (e)(vii) of the Taxes Act 1988 to be regarded as a distribution for the purposes of the Corporation Tax Acts, or
- (b) the profits and losses of the company fall by virtue of Schedule 28AA to that Act to be computed for tax purposes as if the loan had in part not been made,

the proportionate part of any exchange gains or losses which arise in that accounting period in respect of a liability representing the debtor relationship shall be left out of account in determining the debits or credits to be brought into account for the purposes of this Chapter.

(3) In sub-paragraph (2) above, the “proportionate part” of an exchange gain or loss is that part which bears to the whole the proportion which—

- (a) in a case falling within paragraph (a) of that sub-paragraph, the part of the interest or other distribution out of assets that falls to be regarded as a distribution for the purposes of the Corporation Tax Acts bears to the whole of that interest or other distribution out of assets; or
- (b) in a case falling within paragraph (b) of that sub-paragraph, the part of the loan that falls to be treated as if it had not been made bears to the whole of the loan.

(4) Where—

- (a) a company has a creditor relationship in an accounting period,
- (b) the transaction giving rise to the loan is such that it would not have been entered into at all if the parties had been dealing at arm’s length, and
- (c) there is no corresponding debtor relationship such that there would, or would apart from section 84A(2) to (10) of this Act, fall to be brought into account for the purposes of this Chapter, in respect of exchange gains or losses from that debtor relationship, debits or (as the case may be) credits corresponding to, and of the same amount as, the credits or debits that would (apart from this paragraph) fall to be brought into account for the purposes of this Chapter in respect of exchange gains or losses from the creditor relationship,

any exchange gains or losses which arise in that accounting period in respect of an asset representing the creditor relationship shall be left out of account in determining the debits or credits to be brought into account for the purposes of this Chapter.

(5) Where—

- (a) a company has a creditor relationship in an accounting period,
- (b) the circumstances are such that, had the parties to the transaction giving rise to the loan been dealing at arm’s length, the terms would have been the same, except that the amount of the loan would have been an amount (referred to in sub-paragraph (6)

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below as “the adjusted amount”) greater than nil but less than its actual amount, and

- (c) there is no such corresponding debtor relationship as satisfies, in relation to that creditor relationship, the condition set out in sub-paragraph (4)(c) above,

sub-paragraph (4) above shall not apply, but the excess portion of any exchange gain or loss which arises in the accounting period in respect of an asset representing the creditor relationship shall be left out of account in determining the debits or credits to be brought into account for the purposes of this Chapter.

- (6) In sub-paragraph (5) above, the “excess portion” of an exchange gain or loss is so much of the gain or loss as remains after subtracting that part which bears to the whole the proportion which the adjusted amount bears to the amount of the loan.”.

Continuity of treatment: groups etc

- 12 In paragraph 12 of Schedule 9, for sub-paragraph (8) (which applies sub-paragraphs (4) and (5) of paragraph 11 of the Schedule) substitute—

“(8) Sub-paragraph (5) of paragraph 11 above has effect for the purposes of this paragraph as it has effect for the purposes of that paragraph.”.

Loan relationships for unallowable purposes

- 13 In paragraph 13 of Schedule 9, in sub-paragraph (1) (which disallows debits attributable to unallowable purposes)—

- (a) for “the debits”, where first occurring, substitute the following paragraphs—

“(a) the debits, and

(b) the credits in respect of exchange gains,”; and

- (b) after “the debits”, where next occurring, insert “or credits (as the case may be)”.

Life assurance business

- 14 (1) Paragraph 1 of Schedule 11 is amended as follows.

- (2) Before sub-paragraph (2) (effect on debits and credits of applying I minus E basis to profits and gains from loan relationships of insurance companies referable to life assurance business) insert—

“(1B) In applying the I minus E basis for any accounting period in respect of any life assurance business carried on by an insurance company, no exchange gains or losses shall be taken to arise for the purposes of section 100 of this Act except to the extent that the money debt for the purposes of that section—

- (a) arises as a result of an amount of income or expenses which falls to be taken into account in applying the I minus E basis not being paid when it is due and payable; or
- (b) is one that is treated as a money debt for the purposes of that section by virtue of subsection (11)(a) of that section in

accordance with subsection (12) of that section by reference to a Schedule A business or an overseas property business.

This sub-paragraph has effect notwithstanding sub-paragraph (1) above.”.

Special provisions for insurers: apportionments

- 15 In paragraph 3A of Schedule 11 (cases where money debt of insurance company is represented by a liability of the long term business fund) in sub-paragraph (1)—
- (a) in paragraph (a), for “money debt” substitute “loan relationship”; and
 - (b) in paragraph (b), omit “debt or”.

Savings and transitional provisions in the Finance Act 1996

- 16 In Schedule 15 (savings and transitional provisions) omit paragraphs 22 to 24.