

**2002 No. 1970**

**INCOME TAX**

**The Exchange Gains and Losses (Bringing into Account  
Gains or Losses) Regulations 2002**

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| <i>Made</i> - - - - -                   | <i>25th July 2002</i>   |
| <i>Laid before the House of Commons</i> | <i>25th July 2002</i>   |
| <i>Coming into force</i> - - - - -      | <i>1st October 2002</i> |

The Treasury, in exercise of the powers conferred upon them by section 84A(8) to (10) of the Finance Act 1996(a) and paragraph 26(5) of Schedule 23, and paragraph 16(8) to (10) of Schedule 26, to the Finance Act 2002, hereby make the following Regulations:

**Citation, commencement and effect**

1.—(1) These Regulations may be cited as the Exchange Gains and Losses (Bringing into Account Gains or Losses) Regulations 2002 and shall come into force on 1st October 2002 immediately after the Exchange Gains and Losses (Transitional Provisions and Savings) Regulations 2002(b).

(2) These Regulations have effect in relation to accounting periods beginning on or after 1st October 2002.

**Interpretation**

2.—(1) In these Regulations—

“Chapter 2” means Chapter 2 of Part 4 of the Finance Act 1996;

“chargeable gain” and “allowable loss” have the same meaning as they have for the purposes of the 1992 Act;

“foreign business asset”, in relation to a company, means an asset of part of a business in relation to which the company prepares—

(a) accounts using the closing rate/net investment method as mentioned in subsection (2)(a) or (3)(a) of section 93A of the Finance Act 1993(c), or

(b) a return of accounts using that method as mentioned in subsection (2)(b) or (3)(b) of that section;

“a no gain/no loss disposal” means a disposal on which neither a gain nor a loss accrues by virtue of any of the following provisions of the 1992 Act—

(a) section 139(d);

(b) section 140A(e);

(c) section 171(f);

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(a) 1996 c. 8; section 84A was inserted by paragraph 3 of Schedule 23 to the Finance Act 2002 (c. 23).

(b) S.I. 2002/1969.

(c) 1993 c. 34; section 93A was inserted by paragraph 4 of Schedule 24 to the Finance Act 2002.

(d) Section 139 was amended by Part 8(1) of Schedule 26 to the Finance Act 1994 (c. 9), section 134(1) of the Finance Act 1998 (c. 36) and paragraph 5 of Schedule 29 to the Finance Act 2000 (c. 17).

(e) Section 140A was inserted, together with section 140B, by section 44 of the Finance (No. 2) Act 1992 (c. 48).

(f) Section 171 was amended by Part 8(1) of Schedule 26 to the Finance Act 1994, sections 135(1) and 136(2) and (3) of the Finance Act 1998 and paragraph 2 of Schedule 29 to the Finance Act 2000.

(d) section 215; and

(e) section 216(a);

“original shares” and “new holding” have the same meaning as in section 127 of the 1992 Act or (as the case may be) that section as applied by virtue of any enactment relating to chargeable gains;

“paragraph 16” means paragraph 16 of Schedule 26 to the Finance Act 2002;

“section 84A” means section 84A of the Finance Act 1996;

“the 1992 Act” means the Taxation of Chargeable Gains Act 1992(b);

“the 1994 Regulations” means the Exchange Gains and Losses (Alternative Method of Calculation of Gain or Loss) Regulations 1994(c).

(2) In these Regulations—

(a) any reference to a disposal of an asset shall be construed as a reference to any event which is or is treated as a disposal for the purposes of the 1992 Act; and

(b) any reference to the time of the disposal of an asset shall be construed as a reference to the time at which the disposal occurs for the purposes of that Act,

and, for the purposes of this paragraph, any reference to a disposal includes a part disposal.

(3) In these Regulations—

(a) any reference to an asset which is a ship or aircraft includes a reference to a contract—

(i) to which section 67 of the Capital Allowances Act 2001(d) applies; and

(ii) which relates to plant or machinery which is a ship or aircraft; and

(b) any reference to a disposal of an asset which is a ship or aircraft by a person includes a reference to the case where a person ceases to be entitled to the benefit of such a contract and does not then in fact become the owner of the plant or the machinery to which the contract relates.

#### **Prescribed circumstances in which regulation 4 applies**

3.—(1) Regulation 4 applies in either of the circumstances prescribed by paragraphs (2) and (3) below.

(2) The circumstances prescribed by this paragraph are where there is a disposal of an asset by a company and—

(a) any exchange gain or loss arose to the company in relation to the asset in an accounting period beginning on or after 1st October 2002; and

(b) in accordance with generally accepted accounting practice an amount representing the whole or part of an exchange loss or gain which arises to the company in relation to a liability representing a loan relationship of the company or an obligation under a derivative contract—

(i) was carried to or sustained by the reserve mentioned in subsection (5) of section 84A or sub-paragraph (4) of paragraph 16; and

(ii) was set off by or against an amount which represents the whole or part of an exchange gain or loss arising in relation to the asset and falls within subsection (6) of section 84A or sub-paragraph (5) of paragraph 16.

(3) The circumstances prescribed by this paragraph are where there is a disposal of an asset by a company and there is in relation to the asset any of the following—

(a) a deemed disposal under regulation 7(1A) of the 1994 Regulations (as modified by the Exchange Gains and Losses (Transitional Provisions and Savings) Regulations 2002(e));

(b) a deferred gain or loss under regulation 8 of the 1994 Regulations in relation to which paragraph (3) or (4) of that regulation did not apply immediately before the relevant day;

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(a) Section 216 was amended by Part 2(12) of Schedule 40 to the Finance Act 2000.

(b) 1992 c. 12.

(c) S.I. 1994/3227, amended by S.I. 1996/1347 and saved with modifications by S.I. 2002/1969.

(d) 2001 c. 2.

(e) The relevant modification is contained in regulation 14(3) of S.I. 2002/1969.

- (c) a deferred gain or loss under regulation 9 of the 1994 Regulations in relation to which paragraph (3)(a) or (b) or paragraph (4)(a) or (b) of that regulation, as the case may be, did not apply immediately before the relevant day.

(4) In paragraph (3)(b) and (c) above “the relevant day” means the first day of the company’s first accounting period to begin on or after 1st October 2002.

#### **General rule for bringing amounts into account**

4.—(1) For the purposes of the 1992 Act, there shall be brought into account for the accounting period in which the disposal of the asset occurs—

- (a) as a chargeable gain accruing to the company at the time of the disposal, the amount of any net gain; or
- (b) as an allowable loss accruing to the company at the time of the disposal, the amount of any net loss.

(2) Paragraph (1) above does not have effect if the asset disposed of—

- (a) is a foreign business asset immediately before its disposal; or
- (b) consists of shares or an asset related to shares on the disposal of which no chargeable gain is treated as accruing by virtue of Part 1 of Schedule 7AC to the 1992 Act<sup>(a)</sup>.

(3) Paragraph (1) above is subject to regulations 6 and 8.

#### **Calculation of the amount of any net gain or net loss for the purposes of regulation 4**

5.—(1) The amount of any net gain or net loss referred to in regulation 4(1) shall be calculated in accordance with this regulation.

(2) Subject to paragraph (4) below, the amount of any net gain or loss shall be calculated by finding the aggregate of the amounts representing exchange gains or losses which accrued in relation to liabilities matched with the asset disposed of during the period in which the asset was held by the company disposing of it.

(3) The aggregate referred to in paragraph (2) above shall be found in any manner that is just and reasonable having regard to—

- (a) the effect of regulation 6 in the accounting period in which the disposal occurs or in any earlier accounting period; and
- (b) the way in which such an aggregate was found for any earlier accounting period in accordance with this regulation.

(4) Notwithstanding that a loss accruing to a company on the disposal of the asset is not deductible except from a chargeable gain of the kind mentioned in section 18(3) of the 1992 Act, where the aggregate referred to in paragraph (2) would be an amount of net gain for the purposes of regulation 4(1) in relation to that disposal, the amount of such a loss may be deducted from the aggregate.

#### **Assets representing certain loan relationships and ships or aircraft**

6.—(1) This paragraph applies where the asset disposed of—

- (a) represents a loan relationship of the company other than one which falls within section 92 or 93 of the Finance Act 1996 at the time of the disposal, or
- (b) is a ship or aircraft.

(2) Where paragraph (1) applies, the amount to be brought into account under regulation 4(1) shall not be brought into account, for the purposes of the 1992 Act, as a chargeable gain or allowable loss but instead, for the purposes of Chapter 2, as a credit or a debit (according to whether it is an amount of net gain or net loss) in respect of the loan relationships of the company.

(3) Where the asset disposed of represents a loan relationship which falls within section 92 of the Finance Act 1996<sup>(b)</sup> at the time of the disposal—

- (a) the amount of any net gain or loss to be brought into account under regulation 4(1)

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(a) Schedule 7AC was inserted by paragraph 1 of Schedule 8 to the Finance Act 2002.

(b) Section 92 was amended by paragraph 5 of Schedule 23 to the Finance Act 2002.

shall be calculated in accordance with regulation 5 only by reference to exchange gains or losses which accrued in relation to liabilities matched with the asset disposed of during accounting periods beginning before 1st October 2002; and

- (b) for the purposes of Chapter 2—
  - (i) the amount of any relevant exchange losses shall be brought into account as a credit in respect of the loan relationships of the company; and
  - (ii) the amount of any relevant exchange gains shall be brought into account as a debit in respect of those loan relationships.

(4) For the purposes of paragraph (3)(b) above, relevant exchange gains or, as the case may be, losses in the case of the asset are the amounts of any exchange gains or, as the case may be, losses which, if section 84A(3) of the Finance Act 1996 had not had effect in relation to them—

- (a) would have been brought into account under subsection (2)(b) of section 92 of that Act in respect of the asset; and
- (b) for the purposes of subsection (5A) of that section would have been relevant exchange gains or, as the case may be, losses in the case of the asset.

### **Regulations 5 and 6: supplementary**

7.—(1) This regulation has effect for the purposes of regulations 5 and 6.

(2) References to the asset disposed of include references to any predecessor asset which was—

- (a) original shares; or
- (b) “the old asset” construed in accordance with section 116 of the 1992 Act<sup>(a)</sup>.

(3) References to the company disposing of the asset include references to any predecessor company which was “the disposing company” for the purposes of regulation 8 of the 1994 Regulations.

(4) In respect of any time falling within an accounting period beginning before 1st October 2002 a liability is matched with an asset to the extent that it is matched in accordance with an election under regulation 10 of the 1994 Regulations.

(5) In respect of any time falling within an accounting period beginning on or after 1st October 2002—

- (a) a liability is fully matched with an asset where an amount representing the whole of an exchange gain or loss arising in relation to the liability is treated as mentioned in subsection (5) of section 84A or sub-paragraph (4) of paragraph 16; and
- (b) where the amount treated as mentioned in that subsection or that sub-paragraph represents only part of an exchange gain or loss, the liability shall be treated as being matched only to the corresponding extent.

(6) Where in any accounting period beginning on or after 1st October 2002—

- (a) a company holds more than one asset in relation to which there are amounts falling within subsection (6) of section 84A or sub-paragraph (5) of paragraph 16; and
  - (b) the assets are denominated and the liabilities are expressed in the same currency,
- the extent to which an asset is matched shall be determined in accordance with the rules set out in paragraph (7) below.

(7) The following rules shall apply in relation to—

- (a) any disposal of an asset occurring before the relevant disposal;
- (b) any asset held at the time of the relevant disposal.

#### *Rule 1*

Liabilities are to be regarded as having been matched to the greatest possible extent with assets which—

- (a) represent loan relationships of the company (other than ones which fall within section 93 of the Finance Act 1996); or
- (b) are ships or aircraft.

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<sup>(a)</sup> Section 116 was amended by section 46(3) of the Finance (No. 2) Act 1992, paragraph 60 of Schedule 14, paragraph 51 of Schedule 20, and Part 5(10) of Schedule 41, to the Finance Act 1996, section 88(4) of the Finance Act 1997 (c. 16) and paragraph 19 of Schedule 29 to the Finance Act 2000.

*Rule 2*

Subject to Rule 1, liabilities are to be regarded as having been matched to the greatest possible extent with assets (other than foreign business assets) on the disposal of which a chargeable gain accrues or would accrue.

*Rule 3*

Subject to Rules 1 and 2, liabilities are to be regarded as having been matched with assets—

- (a) on the disposal of which no chargeable gain is treated as accruing by virtue of Part 1 of Schedule 7AC to the 1992 Act;
- (b) on a disposal of which no chargeable gain would be treated as accruing by virtue of that Part if the disposal were made on a date falling more than twelve months after the date of the relevant disposal but excluding assets which—
  - (i) are actually disposed of on a date falling less than twelve months after the date of the relevant disposal, and
  - (ii) have been held for less than twelve months at the date of the actual disposal; or
- (c) which are foreign business assets held at the time of the relevant disposal.

(8) For the purposes of paragraph (6) above, the currency in which a liability representing a loan relationship is expressed, or for the acquisition of which an obligation under a currency contract provides, is to be treated as the currency in which an asset is denominated if borrowing in, or the acquisition of, that currency could reasonably be expected to eliminate or substantially reduce the economic risk of holding the asset which is attributable to fluctuations in exchange rates.

(9) In paragraph (7) above, “the relevant disposal” means the disposal referred to in regulation 4.

**No gain/no loss disposals**

8.—(1) This regulation applies where the disposal of the asset is a no gain/no loss disposal.

(2) Where this regulation applies, the amount to be brought into account under regulation 4(1) as a chargeable gain or allowable loss—

- (a) shall not be brought into account for the accounting period in which the disposal of the asset occurs, but instead
- (b) for the purposes of the 1992 Act, shall be brought into account as a chargeable gain or allowable loss, as the case may be, by the company making the first relevant disposal of the asset for the accounting period in which the first relevant disposal occurs.

(3) In paragraph (2)(b) above, in relation to the disposal of an asset which is a no gain/no loss disposal, “the first relevant disposal” means the first subsequent disposal of that asset which is not a no gain/no loss disposal.

**Cases where there is no disposal of the asset by virtue of section 116(10) of the 1992 Act**

9.—(1) This regulation applies in the circumstances prescribed by paragraph (2) below.

(2) The circumstances prescribed by this paragraph are where the circumstances prescribed by regulation 3(2) would exist but for there being no disposal of the asset for the purposes of the 1992 Act by virtue of section 116(10) of that Act (“section 116(10)”).

(3) Where this regulation applies, the amount which, but for section 116(10), would be brought into account under regulation 4(1) as a chargeable gain or allowable loss shall be found and paragraph (4) below shall apply.

(4) Where this paragraph applies—

- (a) if the amount found under paragraph (3) above would be brought into account as a chargeable gain, the market value of the asset shall, for the purposes of paragraph (a) of section 116(10), be increased by an amount equal to that amount;
- (b) if the amount found under paragraph (3) above would be brought into account as an allowable loss—
  - (i) the market value of the asset shall, for the purposes of paragraph (a) of section 116(10), be reduced by an amount equal to that amount; and

- (ii) if that amount exceeds the amount of the market value, an allowable loss equal in amount to the excess shall be treated as accruing on the subsequent disposal of the new asset (within the meaning of section 116(4) of the 1992 Act).

**Cases where, but for section 116, section 127 of the 1992 Act would apply in relation to assets as regards which paragraph (2)(a), but not paragraph (2)(b), of regulation 8 has had effect**

10.—(1) This regulation applies in the circumstances prescribed by paragraph (2) below.

(2) The circumstances prescribed by this paragraph are where, but for section 116 of the 1992 Act, section 127 of that Act would apply in relation to a transaction involving original shares which are or include an asset as regards which paragraph (2)(a), but not paragraph (2)(b), of regulation 8 has had effect.

(3) Where this regulation applies, regulation 9(4) shall apply to the amount which, by virtue of regulation 8(2)(a), is not brought into account as a chargeable gain or an allowable loss for the accounting period in which the disposal of the asset occurs in the same way as it applies to an amount found under regulation 9(3).

**Cases where there is no disposal of the asset by virtue of section 127 of the 1992 Act**

11.—(1) This regulation applies in the circumstances prescribed by paragraph (2) below.

(2) The circumstances prescribed by this paragraph are where the circumstances prescribed by regulation 3(2) would exist but for there being no disposal of the asset for the purposes of the 1992 Act by virtue of section 127 of that Act (“section 127”).

(3) Where this regulation applies, the amount which, but for section 127, would be brought into account under regulation 4(1) as a chargeable gain or allowable loss shall be found and paragraph (4) below shall apply.

(4) Where this paragraph applies—

- (a) if the amount found under paragraph (3) above would be brought into account as a chargeable gain, in computing the amount of any chargeable gain or allowable loss accruing on the subsequent disposal of the new holding, the consideration received on that disposal shall be increased by an amount equal to that amount;
- (b) if the amount found under paragraph (3) above would be brought into account as an allowable loss—
  - (i) in computing the amount of any chargeable gain or allowable loss accruing on the subsequent disposal of the new holding, the consideration received on that disposal shall be reduced by an amount equal to that amount; and
  - (ii) if that amount exceeds the amount of the consideration, an allowable loss equal in amount to the excess shall be treated as accruing on that disposal.

**Cases where section 127 of the 1992 Act applies in relation to assets as regards which paragraph (2)(a), but not paragraph (2)(b), of regulation 8 has had effect**

12.—(1) This regulation applies in the circumstances prescribed by paragraph (2) below.

(2) The circumstances prescribed by this paragraph are where section 127 of the 1992 Act applies in relation to a transaction involving original shares which are or include an asset as regards which paragraph (2)(a), but not paragraph (2)(b), of regulation 8 has had effect.

(3) Where this regulation applies, regulation 11(4) shall apply to the amount which, by virtue of regulation 8(2)(a), has not been brought into account as a chargeable gain or an allowable loss for the accounting period in which the disposal of the asset occurs in the same way as it applies to an amount found under regulation 11(3).

**Cases where exchange gains or losses fall within subsection (4) of section 84A**

13.—(1) This regulation applies in the circumstances prescribed by paragraph (2) below.

(2) The circumstances prescribed by this paragraph are where there is a disposal of an asset by a company and the asset disposed of represents a loan relationship of the company in relation to which exchange gains or losses have fallen within subsection (4) of section 84A.

(3) Where this regulation applies, an amount equal to the amount of any net gain or net loss shall be brought into account, for the purposes of Chapter 2, as a credit or a debit (according to whether it is an amount of net gain or net loss) in respect of the loan relationship for the accounting period in which the disposal occurs.

(4) For the purposes of this regulation, the amount of any net gain or net loss shall be calculated by finding the aggregate of the amounts representing the exchange gains and losses which fell within subsection (4) of section 84A.

*Jim Fitzpatrick*

*Philip Woolas*

25th July 2002

Two of the Lords Commissioners of Her Majesty's Treasury

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## EXPLANATORY NOTE

*(This note is not part of the Regulations)*

Following the repeal of paragraph 4 of Schedule 9 to the Finance Act 1996 (c. 8) (and, in consequence, sections 125 to 169 of the Finance Act 1993 (c. 34)) by section 79(1) of the Finance Act 2002 (c. 23), the tax treatment of exchange gains and losses will be governed by the provisions relating to loan relationships in Chapter 2 of Part 4 of the Finance Act 1996 and derivative contracts in Schedule 26 to the Finance Act 2002.

Subsection (1) of section 84A of the Finance Act 1996 (inserted by paragraph 3 of Schedule 23 to the Finance Act 2002) ("section 84A") provides that any profits, gains and losses arising to a company from its loan relationships and related transactions include exchange gains and losses arising to the company. Subsection (3) of that section provides that subsection (1) does not have effect in relation to certain exchange gains and losses. Subsection (8) of that section, together with paragraph 26(5) of Schedule 23 to the Finance Act 2002, provides that the Treasury may make regulations for the bringing into account of amounts in relation to which subsection (1) does not have effect and amounts reduced to nil under the Exchange Gains and Losses (Alternative Method of Calculation of Gain or Loss) Regulations 1994 (S.I. 1994/3227).

Schedule 26 to the Finance Act 2002 ("Schedule 26") provides for a new regime under which the taxation of profits arising to a company from certain derivative contracts are chargeable to tax as income. Sub-paragraph (1) of paragraph 16 of that Schedule ("paragraph 16") provides that the profits and losses arising from such contracts and related transactions include exchange gains and losses. Sub-paragraph (3) of that paragraph provides that sub-paragraph (1) does not have effect in relation to certain exchange gains and losses. Sub-paragraph (8) of that paragraph provides that the Treasury may make regulations for the bringing into account of amounts in relation to which sub-paragraph (1) does not have effect.

These Regulations provide for the bringing into account of amounts and are made under subsection (8) of section 84A and sub-paragraph (8) of paragraph 16.

Regulation 1 provides for citation, commencement and effect. The Regulations have effect in relation to accounting periods beginning on or after 1st October 2002.

Regulation 2 provides for interpretation.

Regulation 3 prescribes the circumstances in which amounts are to be brought into account.

Regulation 4 provides for a general rule for bringing amounts into account.

Regulation 5 provides for the calculation of the amounts to be brought into account under regulation 4.

Regulation 6 provides for a different rule for bringing amounts into account in the case of assets representing certain loan relationships and ships or aircraft.

Regulation 7 makes supplementary provision in relation to the interpretation of regulations 5 and 6.

Regulation 8 provides for a special rule for bringing into account amounts where the disposal is a no gain/no loss disposal under the Taxation of Chargeable Gains Act 1992 (c. 12) (“the 1992 Act”).

Regulation 9 provides for a special rule for bringing into account amounts where there is no disposal of the asset for the purposes of the 1992 Act by virtue of section 116(10) of that Act.

Regulation 10 provides for a special rule for bringing into account amounts where, but for section 116 of the 1992 Act, section 127 of the 1992 Act would apply in relation to a transaction involving original shares which are or include an asset as regards which paragraph (2)(a), but not paragraph (2)(b), of regulation 8 of these Regulations has had effect.

Regulation 11 provides for a special rule for bringing into account amounts where there is no disposal of the asset for the purposes of the 1992 Act by virtue of section 127 of that Act.

Regulation 12 provides for a special rule for bringing into account amounts where section 127 of the 1992 Act applies in relation to a transaction involving original shares which are or include an asset as regards which paragraph (2)(a), but not paragraph (2)(b), of regulation 8 of these Regulations has had effect.

Regulation 13 provides for a special rule for bringing into account amounts where exchange gains or losses have fallen within subsection (4) of section 84A.

£2.00

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Printed and published in the UK by The Stationery Office Limited  
under the authority and superintendence of Carol Tullo, Controller of  
Her Majesty's Stationery Office and Queen's Printer of Acts of Parliament.  
E1272 8/2002 121272 19585

ISBN 0-11-042657-6



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