

*Status: Point in time view as at 20/07/2005.*

*Changes to legislation: There are currently no known outstanding effects for the Finance (No. 2) Act 2005, SCHEDULE 7. (See end of Document for details)*

## SCHEDULES

### SCHEDULE 7

Section 39

#### AVOIDANCE INVOLVING FINANCIAL ARRANGEMENTS

##### *Rent factoring*

- 1 (1) Part 2 of ICTA (which, at sections 43A to 43G, includes provisions about rent factoring) is amended as follows.
- (2) Section 43C(1) (section 43B not to apply where term over which financial obligation is to be reduced exceeds 15 years) shall cease to have effect.
- (3) In section 43E (interposed lease: exceptions etc) in subsection (1), omit paragraphs (a) and (b) (which relate to certain periods exceeding 15 years).
- (4) The amendments made by this paragraph have effect in relation to finance agreements entered into on or after 16th March 2005.
- (5) But where—
- (a) a finance agreement was entered into on or after 20th March 2000 and before 16th March 2005, and
  - (b) section 43D of ICTA (interposed lease) would apply in relation to the agreement but for section 43E(1)(a) or (b) of that Act,
- sub-paragraph (6) has effect.
- (6) In any such case, any amount of principal in rent paid on or after 16th March 2005 which, apart from this sub-paragraph, would—
- (a) be deductible as an expense in computing profits charged under Case I of Schedule D, or
  - (b) be deductible under section 75 of ICTA (expenses of management), or
  - (c) fall to be brought into account under section 76 of that Act (expenses of insurance companies) at Step 1 in subsection (7) of that section,
- shall not be so deductible or brought into account for any accounting period ending on or after 16th March 2005.
- (7) If payment of an amount of principal in rent is made on or after 16th March 2005 in respect of a rental period that falls—
- (a) partly before that date, and
  - (b) partly on or after it,
- sub-paragraph (6) has effect in relation to only so much of the payment as relates to the part of the period falling on or after 16th March 2005.
- (8) In this paragraph—
- “amount of principal in rent” means so much of any amount of rent payable under a lease as, in the case of the finance agreement in question,

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reduces the amount of the financial obligation mentioned in section 43A(1) of ICTA;

“rental period” means a period in respect of which rent is paid.

*Section 730: restriction to income consisting of distributions in respect of company shares etc*

- 2 (1) Section 730 of ICTA (transfers of income arising from securities) is amended as follows.
- (2) In each place where it occurs—
- (a) for “interest” substitute “ distribution ”;
  - (b) for “securities” substitute “ shares ”.
- (3) In subsection (1) (interest deemed to be income of owner etc)—
- (a) in paragraph (a), for “deemed to be” substitute “ treated as ”,
  - (b) in paragraph (b), for “deemed to be” substitute “ treated as ”, and
  - (c) omit paragraph (c).
- (4) For subsection (2) (sale etc where proceeds chargeable to tax by virtue of section 18(3B) of ICTA) substitute—
- “(2) This section does not have effect in relation to a sale or transfer if the proceeds of the sale or transfer are chargeable to tax.”.
- (5) Omit subsection (2A) (loan relationships).
- (6) For subsection (3) substitute—
- “(3) The proceeds of any subsequent sale or other realisation of the right to receive the distribution shall not, for any of the purposes of the Tax Acts, be regarded as the income of the seller or the person on whose behalf the right is otherwise realised.”.
- (7) In subsection (4), in the words following paragraph (b) after their substitution by paragraph 300(3)(b) of Schedule 1 to ITTOIA 2005, for “interest” substitute “ distribution ”.
- (8) In subsection (4A), for “interest arising” substitute “ distribution ”.
- (9) In subsection (4B), for “interest” substitute “ distribution ”.
- (10) For subsection (7) (definitions) substitute—
- “(7) In this section—
- “distribution”, in relation to shares in a company,—
- (a) has the same meaning as it has in the Corporation Tax Acts (see section 209), but
  - (b) also includes any amount that would be a distribution if the company paying it were resident in the United Kingdom;
- “shares” means shares in a company.”.
- (11) In subsection (8) (information powers) omit from “and for the purpose” to the end of the subsection.
- (12) The heading to the section becomes “ Transfers of rights to receive distributions in respect of shares ”.

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- (13) The amendments made by this paragraph have effect in relation to sales or transfers on or after 2nd December 2004.

*Change in ownership of company with investment business*

- 3 (1) In section 768B(10) of ICTA (Part 4 of Schedule 28A to have effect for restricting the debits to be brought into account in respect of loan relationships) after “debits”, where first occurring, insert “ and non-trading deficits ”.
- (2) In section 768C(9) of ICTA (Part 4 of Schedule 28A to have effect for restricting the debits to be brought into account in respect of loan relationships) after “debits”, where first occurring, insert “ and non-trading deficits ”.
- (3) Schedule 28A to ICTA (change in ownership of investment company: deductions) is amended as follows.
- (4) In paragraph 7(1)(b) (apportionment of excess in paragraph 6(c), or of non-trading deficit, to first part of accounting period) after “the whole amount of the excess” insert “ or, as the case may be, of the deficit ”.
- (5) After paragraph 9 insert—
- “9A (1) This paragraph has effect in any case to which section 768B applies where the non-trading deficit mentioned in paragraph 6(dc) above is apportioned by paragraph 7(b) above to the first part of the accounting period being divided.
- (2) In any such case, none of that non-trading deficit shall be carried forward to—
- (a) the accounting period beginning immediately after the change in the ownership of the company, or
- (b) any subsequent accounting period.”.
- (6) After paragraph 10 insert—
- “10A(1) This paragraph has effect in any case to which section 768C applies where the non-trading deficit mentioned in paragraph 13(1)(ec) below is apportioned by paragraph 16(1)(b) below to the first part of the accounting period being divided.
- (2) In any such case, none of that non-trading deficit shall be carried forward to—
- (a) the accounting period beginning immediately after the change in the ownership of the company, or
- (b) any subsequent accounting period.”.
- (7) In paragraph 16(1)(b) (apportionment of excess in paragraph 13(1)(ec), or of non-trading deficit, to first part of accounting period) after “the whole amount of the excess” insert “ or, as the case may be, of the deficit ”.
- (8) The title of Part 4 of the Schedule becomes “ Disallowed debits and non-trading deficits ”.
- (9) The amendments made by this paragraph have effect in any case where the change in ownership is on or after 10th February 2005.

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*Transfers of rights to receive annual payments*

- 4 (1) After section 775 of ICTA (sale by individual of income derived from his personal activities) insert—

**“775A Transfers of rights to receive annual payments**

- (1) This section applies in any case where—
- (a) a person sells or transfers the right to receive an annual payment to which this section applies (see subsection (4)), and
  - (b) the consideration (if any) for the sale or transfer would not, apart from this section, be chargeable to tax.
- (2) In any such case, tax is charged—
- (a) in the case of income tax, under this section; or
  - (b) in the case of corporation tax, under Case III of Schedule D.
- (3) Where this section applies—
- (a) the tax is charged on an amount equal to the market value of the right to receive the annual payment;
  - (b) the tax is charged for the chargeable period in which the sale or transfer takes place;
  - (c) the person liable for the tax is the person who sells or transfers the right to the annual payment.
- (4) This section applies to any annual payment other than—
- (a) an annual payment under a life annuity;
  - (b) an annual payment under a pension annuity;
  - (c) an annual payment to which section 347A applies (annual payments that are not charges on income);
  - (d) an annual payment in respect of which, by virtue of section 727 of ITTOIA 2005 (payments by individuals arising in UK), no liability to income tax arises under Part 5 of that Act.
- (5) This section applies in relation to part of an annual payment as it applies in relation to the whole of an annual payment.
- (6) For the purposes of this section, a sale or transfer of all rights under an agreement for annual payments, or under an annuity, is a sale or transfer of the rights to each individual payment under the agreement or annuity.
- (7) In this section—
- “life annuity” means—
- (a) a life annuity, as defined in section 657(1); or
  - (b) a life annuity, as defined in section 473(2) of ITTOIA 2005;
- “pension annuity” means an annuity which is pension income within the meaning of Part 9 of ITEPA 2003 (see section 566(2) of that Act).”.
- (2) The amendment made by this paragraph has effect in relation to sales or transfers on or after 16th March 2005.

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*Disposals and acquisitions of company loan relationships with or without interest*

- 5 (1) Section 807A of ICTA is amended as follows.
- (2) After subsection (2A) (exclusion of certain tax) insert—
- “(2B) Where, in the case of any share, section 91A or 91B of the Finance Act 1996 (shares treated as loan relationships) applies in relation to a company for an accounting period, this section has effect—
- (a) in relation to a distribution in respect of the share as it has effect in relation to interest under a loan relationship, and
- (b) in relation to a distribution accruing in respect of the share at a time when the company does not (within the meaning of the section in question) hold the share as it applies in relation to interest accruing under a loan relationship at a time when the company is not a party to the loan relationship.”.
- (3) The amendment made by this paragraph has effect in relation to shares held by a company on or after 16th March 2005.

*Manufactured interest and the accrued income scheme*

- 6 (1) In Schedule 23A to ICTA (manufactured dividends and interest) paragraph 3 (manufactured interest on UK securities) is amended as follows.
- (2) In sub-paragraph (2A) (restriction on relief under sub-paragraph (2)(c))—
- (a) in paragraph (a) (receipt of interest or payment representative of it) after “is chargeable to income tax” insert “ (and see section 714(5) for the amount so chargeable in a case where section 714(4) applies) ”, and
- (b) for paragraph (b) (accrued income scheme) substitute—
- “(b) is, by virtue of section 714(2), chargeable to income tax on annual profits or gains in respect of transfers of securities which are subject to the arrangement giving rise to the payment of manufactured interest; or”.
- (3) In sub-paragraph (2A), in the paragraph (b) so substituted, for “annual profits or gains” substitute “ income ”.
- (4) The amendment made by sub-paragraph (3) has effect in relation to payments of manufactured interest made on or after 6th April 2005.
- (5) The other amendments made by this paragraph have effect in relation to payments of manufactured interest made on or after 16th March 2005.

*Consideration due after time of disposal: creditor relationships etc*

- 7 (1) Section 48 of TCGA 1992 (consideration due after time of disposal) is amended as follows.
- (2) At the beginning insert “ (1) ”.
- (3) At the end add—
- “(2) Subsection (1) above does not apply in relation to so much of any consideration as consists of rights under a creditor relationship to which a company becomes a party as a result of the disposal.

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- (3) In the computation of the gain in a case where subsection (2) above has effect in relation to any consideration, the amount to be brought into account in respect of that consideration is the fair value of the creditor relationship.
- (4) In this section—
- (a) “creditor relationship”, and
  - (b) “fair value”, in relation to a creditor relationship,
- each have the same meaning as in Chapter 2 of Part 4 of the Finance Act 1996 (see section 103(1) of that Act).”.

*Corporate strips: manipulation of price: associated payment giving rise to loss*

- 8 In TCGA 1992, after section 151C (strips: manipulation of price: associated payment giving rise to loss) insert—

**“151D Corporate strips: manipulation of price: associated payment giving rise to loss**

- (1) This section applies if—
- (a) as a result of any scheme or arrangement which has an unallowable purpose, the circumstances are, or might have been, as mentioned in paragraph (a), (b) or (c) of section 452G(2) of ITTOIA 2005,
  - (b) under the scheme or arrangement, a payment falls to be made otherwise than in respect of the acquisition or disposal of a corporate strip, and
  - (c) as a result of that payment or the circumstances in which it is made, a loss accrues to any person.
- (2) The loss shall not be an allowable loss.
- (3) For the purposes of this section a scheme or arrangement has an unallowable purpose if the main benefit, or one of the main benefits, that might have been expected to result from, or from any provision of, the scheme or arrangement (apart from section 452G of ITTOIA 2005 and this section) is—
- (a) the obtaining of a tax advantage by any person, or
  - (b) the accrual to any person of an allowable loss.
- (4) The reference in subsection (1)(b) above to the acquisition or disposal of a corporate strip shall be construed as if it were in Chapter 8 of Part 4 of ITTOIA 2005 (profits from deeply discounted securities) (see, in particular, sections 437 and 452F of that Act for the meaning of “disposal” and section 452E of that Act for the meaning of “corporate strip”).
- (5) In subsection (3)(a) above “tax advantage” has the meaning given by section 709(1) of the Taxes Act.
- (6) This section applies to losses accruing on or after 6th April 2005.”.

*Transactions within a group: shares subject to third party obligations*

- 9 (1) Section 171 of TCGA 1992 (transfers within a group: general provisions) is amended as follows.

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(2) After subsection (3) insert—

“(3A) Subsection (1) above does not apply—

- (a) if section 91A of the Finance Act 1996 (shares subject to third party obligations)—
  - (i) does not apply in the case of the asset in relation to company A immediately before the disposal, but
  - (ii) does apply in the case of the asset in relation to company B immediately after its acquisition, or
- (b) if that section—
  - (i) applies in the case of the asset in relation to company A immediately before the disposal, but
  - (ii) does not apply in the case of the asset in relation to company B immediately after its acquisition.”.

(3) The amendment made by this paragraph has effect in any case where the disposal is on or after 16th March 2005.

*Shares treated as loan relationships*

10 (1) After section 91 of FA 1996 insert the following heading— “ Shares treated as loan relationships ”

(2) After that heading insert the following section—

**“91A Shares subject to outstanding third party obligations**

- (1) This section applies for the purposes of corporation tax in relation to a company if at any time in an accounting period—
  - (a) that company (“the investing company”) holds a share in another company (“the issuing company”),
  - (b) the share is subject to outstanding third party obligations (see subsection (5)), and
  - (c) the share is an interest-like investment (see subsections (7) and (8)).
- (2) This Chapter shall have effect for the accounting period of the investing company in accordance with subsection (3) below as if—
  - (a) the share were rights under a creditor relationship of that company, and
  - (b) any distribution in respect of the share were not a distribution falling within section 209(2)(a) or (b) of the Taxes Act 1988.
- (3) The debits and credits to be brought into account by the investing company for the purposes of this Chapter as respects the share must be determined on the basis of fair value accounting.
- (4) No debits are to be brought into account in respect of any transaction (or series of transactions) which (apart from the assumption in subsection (8)(b) below) would have the effect of causing the condition in paragraph (a) or (b) of subsection (7) below not to be satisfied.
- (5) For the purposes of this section, the cases where a share is subject to outstanding third party obligations are those cases where—

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- (a) the share is subject to obligations of any description in subsection (6) below,
  - (b) the obligations are obligations of a person other than the investing company, and
  - (c) the obligations are yet to be discharged,
- and where a share is subject to any such obligations, they are for the purposes of this section the “third party obligations” in the case of that share.
- (6) The descriptions of obligation are—
- (a) an obligation to meet unpaid calls on the share;
  - (b) an obligation (not falling within paragraph (a) above) to make a contribution to the capital of the issuing company that could affect the value of the share.
- (7) In this section “interest-like investment” means a share whose nature is such that the fair value of the share—
- (a) is likely to increase at a rate which represents a return on an investment of money at a commercial rate of interest (see section 103(3A)), and
  - (b) is unlikely to deviate to a substantial extent from that rate of increase.
- Fluctuations in value resulting from changes in exchange rates are to be left out of account for the purposes of paragraph (b) above.
- (8) For the purposes of subsection (7) above, it shall be assumed—
- (a) that any third party obligations will be met in the amounts, and at the time, at which they are due, and
  - (b) that no transaction (or series of transactions) intended to cause the condition in paragraph (a) or (b) of that subsection not to be satisfied will be entered into.
- (9) For the purposes of this section, the fair value of a share that is subject to outstanding third party obligations must include the fair value of the obligations.
- (10) For the purposes of this section a company shall be treated as continuing to hold a share notwithstanding that the share has been transferred to another person—
- (a) under a repo or stock lending arrangement, or
  - (b) under a transaction which is treated by section 26 of the Taxation of Chargeable Gains Act 1992 as not involving any disposal.”.
- (3) After section 91A insert—

**“91B Non-qualifying shares**

- (1) This section applies for the purposes of corporation tax in relation to a company if at any time in an accounting period—
- (a) the company (“the investing company”) holds a share in another company (“the issuing company”),
  - (b) the share is not one which, by virtue of paragraph 4 of Schedule 10 to this Act (holdings in unit trusts and offshore funds), falls to be



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- treated for that accounting period as if it were rights under a creditor relationship of the investing company, and
- (c) the share is a non-qualifying share (see subsection (6)),
- and at no time in the accounting period does section 91A above apply in relation to the investing company in the case of that share.
- (2) This Chapter shall have effect for that accounting period in accordance with subsection (3) below as if—
- (a) the share were rights under a creditor relationship of the investing company, and
- (b) any distribution in respect of the share were not a distribution falling within section 209(2)(a) or (b) of the Taxes Act 1988.
- (3) The debits and credits to be brought into account by the investing company for the purposes of this Chapter as respects the share must be determined on the basis of fair value accounting.
- (4) In any case where Condition 1 in section 91C below is satisfied, no debits are to be brought into account in respect of any transaction (or series of transactions) which (apart from the assumption in subsection (6) of section 91C below) would have the effect of causing the condition in paragraph (a) or (b) of subsection (1) of that section not to be satisfied.
- (5) In any case where Condition 3 in section 91E below is satisfied—
- (a) debits and credits shall be brought into account for the purposes of Schedule 26 to the Finance Act 2002 (derivative contracts) by the investing company in respect of any associated transaction falling within section 91E below as if it were, or were a transaction in respect of, a derivative contract (if that is not in fact the case), and
- (b) those debits and credits shall be determined on the basis of fair value accounting.
- (6) A share is a non-qualifying share for the purposes of this section if—
- (a) it is not one where section 95 of the Taxes Act 1988 (dealers etc) applies in relation to distributions in respect of the share, and
- (b) one or more of the Conditions in sections 91C to 91E below is satisfied.
- (7) Subsection (10) of section 91A above (company treated as holding a share) also applies for the purposes of this section.”.
- (4) After section 91B insert—

**“91C Condition 1 for section 91B(6)(b)**

- (1) Condition 1 is that the assets of the issuing company are of such a nature that the fair value of the share—
- (a) is likely to increase at a rate which represents a return on an investment of money at a commercial rate of interest, and
- (b) is unlikely to deviate to a substantial extent from that rate of increase.

Fluctuations in value resulting from changes in exchange rates are to be left out of account for the purposes of paragraph (b) above.

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- (2) But Condition 1 is not satisfied if the whole or substantially the whole by fair value of the assets of the issuing company are income producing.
- (3) The assets which, for the purposes of this section, are “income producing” are—
- (a) any share as respects which the conditions in section 91A(1) above are satisfied;
  - (b) any share as respects which Condition 1 above is satisfied or would, apart from subsection (2) above, be satisfied;
  - (c) any share as respects which Condition 2 in section 91D below is satisfied or would, apart from subsection (1)(c) of that section (excepted shares), be satisfied;
  - (d) any share as respects which Condition 3 in section 91E below is satisfied;
  - (e) any asset of a description specified in any paragraph of paragraph 8(2) of Schedule 10 to this Act (qualifying investments in relation to a unit trust scheme or an offshore fund);
  - (f) rights under a repo in relation to which section 730A of the Taxes Act 1988 applies;
  - (g) any share in a company the whole or substantially the whole by fair value of whose assets are assets within paragraphs (a) to (f) above.
- (4) The Treasury may by regulations amend this section for the purpose of adding to the assets which are income producing.
- (5) The provision that may be made by regulations under this section includes provision for the regulations to have effect in relation to accounting periods (whenever beginning) which end on or after the day on which the regulations come into force.
- (6) For the purposes of subsection (1) above, it shall be assumed that no transaction (or series of transactions) intended to cause the condition in paragraph (a) or (b) of that subsection not to be satisfied will be entered into by the investing company.
- (7) This section shall be construed as one with section 91B above.

**91D Condition 2 for section 91B(6)(b)**

- (1) Condition 2 is that the share—
- (a) is redeemable (see subsection (2)),
  - (b) is designed to produce a return which equates, in substance, to the return on an investment of money at a commercial rate of interest, and
  - (c) is not an excepted share (see subsection (3)).
- (2) For the purposes of this section, a share is to be regarded as redeemable only if it is redeemable as a result of its terms of issue (or any collateral agreements, arrangements or understandings)—
- (a) requiring redemption,
  - (b) entitling the holder to require redemption, or
  - (c) entitling the issuer to redeem.

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- (3) A share is an “excepted share” for the purposes of this section if—
- (a) it is a qualifying publicly issued share (see subsections (4) and (5)),
  - (b) it is a share that mirrors a public issue (see subsections (6) to (8)), or
  - (c) the investing company's purpose in acquiring the share is not an unallowable purpose (see subsection (9)).
- (4) A share is a “qualifying publicly issued share” for the purposes of this section if—
- (a) it was issued by a company as part of an issue of shares to independent persons, and
  - (b) less than 10% of the shares in that issue are held by the investing company or persons connected with it.
- (5) But a share is not a qualifying publicly issued share for those purposes if the investing company's purpose in acquiring the share is an unallowable purpose by virtue of subsection (9)(a) below.
- (6) The cases where a share mirrors a public issue are those set out in subsections (7) and (8) below.
- (7) Case 1 is where—
- (a) a company (company A) issues shares (the public issue) to independent persons,
  - (b) within 24 hours of that issue, one or more other companies (companies BB) issue shares (the mirroring shares) to company A on the same, or substantially the same, terms as the public issue,
  - (c) company A and companies BB are associated companies (see subsection (11)), and
  - (d) the total nominal value of the mirroring shares does not exceed the nominal value of the public issue,
- and in any such case the mirroring shares are shares that mirror a public issue.
- (8) Case 2 is where, in the circumstances of Case 1,—
- (a) within 24 hours of the public issue, one or more other companies (companies CC) issue shares (the second-level mirroring shares) to one or more of companies BB on the same, or substantially the same, terms as the public issue,
  - (b) company A, companies BB and companies CC are associated companies, and
  - (c) the total nominal value of the second-level mirroring shares does not exceed the nominal value of the public issue,
- and in any such case the second-level mirroring shares are also shares that mirror a public issue.
- (9) For the purposes of this section, a share is acquired by the investing company for an unallowable purpose if the purpose, or one of the main purposes, for which the company holds the share is—
- (a) the purpose of circumventing section 95 of the Taxes Act 1988 (see subsection (10)), or
  - (b) any other purpose which is a tax avoidance purpose (see subsection (11)).

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- (10) The purpose, or one of the main purposes, for which the investing company holds a share shall, in particular, be taken to be the purpose of circumventing section 95 of the Taxes Act 1988 (taxation of dealers in respect of distributions etc) if the investing company was an associated company of a bank (see subsection (11)) at the time when the investing company acquired the share, unless the investing company shows that—
- (a) immediately before that time, some or all of its business consisted in making and holding investments, and
  - (b) it acquired the share in the ordinary course of that business.
- (11) In this section—
- “associated company”, in relation to any other company, means a company which, within the meaning given by section 413(3)(a) of the Taxes Act 1988, is a member of the same group of companies as that other company;
- “bank” has the meaning given by section 840A of the Taxes Act 1988;
- “independent person”, in relation to a company, means a person who is not connected with the company;
- “tax advantage” has the meaning given by section 709(1) of the Taxes Act 1988;
- “tax avoidance purpose”, in the case of any company, means any purpose that consists in securing a tax advantage (whether for the company or any other person).
- (12) Section 839 of the Taxes Act 1988 (connected persons) applies for the purposes of this section.
- (13) This section is to be construed as one with section 91B above.

**91E Condition 3 for section 91B(6)(b)**

- (1) Condition 3 is that there is a scheme or arrangement under which the share and one or more associated transactions are together designed to produce a return which equates, in substance, to the return on an investment of money at a commercial rate of interest.
- (2) But Condition 3 is not satisfied if—
  - (a) Condition 1 in section 91C above is satisfied as respects the share or would, apart from subsection (2) of that section (income producing assets), be so satisfied, or
  - (b) Condition 2 in section 91D above is satisfied as respects the share or would, apart from subsection (1)(c) of that section (excepted shares), be so satisfied.
- (3) In this section “associated transaction” includes entering into, or acquiring rights or liabilities under, any of the following—
  - (a) a derivative contract;
  - (b) a contract that would be a derivative contract, apart from paragraph 4(2B) of Schedule 26 to the Finance Act 2002 (trades etc: hedging relationships with shares);
  - (c) a contract having a similar effect to—

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- (i) a derivative contract, or
- (ii) a contract falling within paragraph (b) above;
- (d) a contract of insurance or indemnity.

(4) This section is to be construed as one with section 91B above.”.

(5) After section 91E insert—

**“91F Power to add, vary or remove Conditions for section 91B(6)(b)**

(1) The Treasury may by regulations amend this Chapter so as to add, vary or remove Conditions for the purposes of section 91B(6)(b) above.

(2) Where the Treasury so add, vary or remove a Condition, they may also by regulations amend any of the following enactments—

- (a) this Chapter,
- (b) Chapters 1 to 3 of Part 6 of the Taxes Act 1988 (company distributions),
- (c) Part 18 of the Taxes Act 1988 (double taxation relief),
- (d) the Taxation of Chargeable Gains Act 1992,
- (e) Schedule 26 to the Finance Act 2002 (derivative contracts),

so as to make provision for or in connection with taxation in the case of any asset or transaction that is or was mentioned in the Condition.

(3) The power to make regulations under this section includes power—

- (a) to make different provision for different cases, and
- (b) to make such consequential, supplementary, incidental or transitional provisions, or savings, as appear to the Treasury to be necessary or expedient (including provision amending any enactment or any instrument made under an enactment).”.

(6) After section 91F insert—

**“91G Shares beginning or ceasing to be subject to section 91A or 91B**

(1) Where at any time on or after 16th March 2005 the conditions in section 91A(1) or 91B(1) above become satisfied in the case of any share, otherwise than in the circumstances described in subsection (3) below, the investing company shall be deemed for the purposes of the Taxation of Chargeable Gains Act 1992—

- (a) to have disposed of the share immediately before that time for a consideration of an amount equal to its fair value at that time, and
- (b) to have immediately reacquired it for a consideration of the same amount.

(2) Where at any time the conditions in section 91A(1) or 91B(1) above cease to be satisfied in the case of any share, the investing company shall be deemed for the purposes of the Taxation of Chargeable Gains Act 1992 and of this Chapter—

- (a) to have disposed of the share immediately before that time for a consideration of an amount equal to its fair value at that time, and

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- (b) to have immediately reacquired it for a consideration of the same amount.
- (3) In any case where—
- (a) a share is held by a company both—
- (i) at the end of 15th March 2005, and
- (ii) at the beginning of 16th March 2005, and
- (b) the conditions in section 91A(1) or 91B(1) above are satisfied in relation to that share at the beginning of 16th March 2005,
- subsection (4) below applies.
- (4) In any such case, section 116 of the Taxation of Chargeable Gains Act 1992 (reorganisations etc involving qualifying corporate bonds) shall have effect in accordance with—
- (a) the assumptions in subsections (5) and (6) below, and
- (b) the provisions of subsections (7) and (8) below.
- (5) The first of the assumptions is that the share became an asset representing a creditor relationship of the company (and, accordingly, a qualifying corporate bond) in consequence of the occurrence on 16th March 2005 of a transaction such as is mentioned in section 116(1) of the Taxation of Chargeable Gains Act 1992.
- (6) The remaining assumptions are that, in relation to the transaction deemed to have occurred as mentioned in subsection (5) above,—
- (a) the share immediately before 16th March 2005 shall be assumed to be the old asset for the purposes of section 116 of the Taxation of Chargeable Gains Act 1992, and
- (b) the asset representing a creditor relationship immediately after the beginning of 16th March 2005 shall be assumed for those purposes to be the new asset.
- (7) Where—
- (a) subsection (3) above has effect in the case of any share, but
- (b) the conditions in section 91A(1) or 91B(1) above cease to be satisfied in the case of the share at any time on or before 31st December 2005,
- subsection (8) below applies.
- (8) In any such case—
- (a) the deemed disposal of the share at that time by virtue of subsection (2)(a) above shall not be regarded as a disposal for the purposes of subsection (10)(b) or (c) of section 116 of the Taxation of Chargeable Gains Act 1992, but
- (b) the share shall continue to be the new asset for the purposes of that section.”.
- (7) The amendments made by this paragraph have effect in relation to shares held by a company on or after 16th March 2005.

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*Related transactions in relation to right to receive manufactured interest*

- 11 (1) Section 97 of FA 1996 (manufactured interest) is amended as follows.
- (2) In subsection (2) (consequences of company having relationship to which the section applies)—
- (a) paragraph (b) (which restricts the debits and credits to be brought into account to those relating to the manufactured interest) shall cease to have effect, and
- (b) in the closing words, for “paragraphs (a)(ii) and (b)” substitute “paragraph (a)(ii)”.
- (3) After subsection (2) insert—
- “(2A) Where a company—
- (a) has a relationship to which this section applies, but
- (b) enters into a related transaction in respect of the right to receive manufactured interest,
- then, for the purpose of bringing credits into account by virtue of subsection (2) above in respect of that or any other related transaction, the company shall continue to be treated as having a relationship to which this section applies even though the manufactured interest is not payable to the company.”.
- (4) Omit subsections (3) and (3A) (which relate to whether debits or credits are trading or non-trading etc and which are unnecessary, in view of the application of sections 82(2) and 103(2) of FA 1996 by virtue of section 97(2) of that Act).
- (5) The amendments made by this paragraph have effect in relation to related transactions on or after 16th March 2005.

*Money debts etc not arising from lending of money: discounts and profits from transactions*

- 12 (1) Section 100 of FA 1996 (money debts etc not arising from the lending of money) is amended as follows.
- (2) In subsection (1)(c) (money debts to which the section applies) after subparagraph (iii) insert “or
- (iv) as respects which the conditions in subsection (1A) below (discount etc) are satisfied;”.
- (3) After subsection (1) insert—
- “(1A) The conditions mentioned in subsection (1)(c)(iv) above are that—
- (a) the company stands in the position of creditor in relation to the money debt;
- (b) the money debt is one from which a discount (whether of an income or capital nature) arises to the company;
- (c) the discount does not fall to be brought into account under section 50 of the Finance Act 2005 by virtue of section 47 of that Act (alternative finance return);
- (d) if the money debt is some or all of the consideration payable for a disposal of property, the money debt (on the assumption that it

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will be paid in full) does not fall to be brought into account for the purposes of corporation tax as a trading receipt of the company;

- (e) if the money debt is some or all of the consideration payable for a disposal of property, the property in question is not any of the following—
- (i) an asset representing a loan relationship;
  - (ii) a derivative contract.”.

- (4) In subsection (2), as it has effect for periods of account beginning on or after 1st January 2005, in paragraph (a), for “matters mentioned in subsection (1)(c) above” substitute “ matters mentioned in subsection (1)(c)(i) to (iii) above or subsection (2ZA) below ”.

- (5) After subsection (2) insert—

“(2ZA) The matters are—

- (a) in the case of a money debt falling within subsection (1)(c)(i) above, profits (but not losses) arising to the company from any related transaction in respect of the right to receive interest;
- (b) in the case of a money debt falling within subsection (1)(c)(iv) above, each of the following—
  - (i) the discount arising to the company from the money debt;
  - (ii) profits (but not losses) arising to the company from any related transaction;
  - (iii) any impairment arising to the company in respect of the discount;
  - (iv) any reversal of any such impairment.

(2ZB) Where a company—

- (a) has a relationship to which this section applies by virtue of subsection (1)(c)(i) above, but
- (b) enters into a related transaction in respect of the right to receive interest,

then, for the purpose of bringing credits into account by virtue of subsection (2ZA)(a) above in respect of that or any other related transaction, the company shall continue to be treated as having a relationship to which this section so applies even though the interest is not payable to the company.”.

- (6) After subsection (3) (amounts treated as interest under Schedule 28AA to ICTA) insert—

“(3A) For the purposes of this section, a discount shall, in particular, be taken to arise from a money debt in any case where—

- (a) there is a disposal of property for a consideration some or all of which is money that falls to be paid after the sale;
- (b) the amount or value of the whole consideration exceeds what the purchaser would have paid for the property if he had been required to pay in full at the time of the disposal; and
- (c) some or all of the excess can reasonably be regarded as representing a return on an investment of money at interest (and, accordingly, as being a discount arising from the money debt).



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- (3B) The credits to be brought into account for the purposes of this Chapter in respect of a discount arising from a money debt must be determined using an amortised cost basis of accounting (see section 103).”.
- (7) Omit subsections (4) to (6) and (8) (which relate to whether debits or credits are trading or non-trading etc and which are unnecessary, in view of the application of sections 82(2) and 103(2) of FA 1996 by virtue of section 100(2) of that Act).
- (8) Omit subsection (13) (express subsection to Schedules 9 and 11 to FA 1996, which is unnecessary in view of the closing words of subsection (2) of the section).
- (9) In consequence of the amendments made by this paragraph, paragraph (c) of the Case III of Schedule D substituted for the purposes of corporation tax by section 18(3A) of ICTA (tax in respect of discount arising otherwise than in respect of a loan relationship) shall not have effect in relation to any discount arising in an accounting period beginning on or after the commencement date.
- (10) Subject to sub-paragraph (9), the amendments made by this paragraph have effect in relation to any money debt to which a company is party as a creditor on or after the commencement date.
- (11) Where, on or after the commencement date but in a period of account beginning before 1st January 2005, a company is party to a relationship to which section 100 of FA 1996 applies, then, in the application of that section for that period of account, subsection (2) of it shall have effect as follows—
- (a) paragraph (a) shall have effect in relation to—
    - (i) any discount arising to the company from the money debt, and
    - (ii) any profits, impairment of discount, or reversal of impairment of discount, arising to the company as mentioned in subsection (2ZA) of that section,as it has effect (or would have effect) in relation to interest payable to the company under the relationship,
  - (b) paragraph (b) shall have effect as if the reference to interest included a reference to the matters mentioned in paragraph (a)(i) and (ii) above, and
  - (c) the closing words shall have effect accordingly.
- (12) None of the following shall be brought into account for the purposes of Chapter 2 of Part 4 of FA 1996 by virtue of this paragraph—
- (a) credits in respect of discount arising from a money debt, to the extent that the discount accrued before the commencement date;
  - (b) credits in respect of profits arising as mentioned in section 100(2ZA)(a) or (b)(ii) of that Act where the related transaction took place before the commencement date;
  - (c) debits in respect of any impairment arising in respect of discount arising from a money debt, to the extent that the discount accrued before the commencement date;
  - (d) credits in respect of any reversal of any such impairment, to the extent that the discount accrued before the commencement date.
- (13) In this paragraph “the commencement date” means 16th March 2005.

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*Meaning of “commercial rate of interest”*

- 13 (1) In section 103 of FA 1996 (interpretation) after subsection (3) insert—
- “(3A) For the purposes of this Chapter, a commercial rate of interest, in the case of a company and any asset, is—
- (a) a rate (“the simple commercial rate”) that is reasonably comparable to the rate that the company could obtain by placing on deposit the money it invested in the asset, or
  - (b) in any case where—
    - (i) the likely rate of increase in the value of the asset is in question, and
    - (ii) that likely rate is a lower rate than the simple commercial rate, and
    - (iii) the difference is a result of an expectation that the company would also obtain a tax advantage as a result of investing in the asset,
 that lower rate.
- (3B) In subsection (3A) above, “tax advantage” has the meaning given by section 709(1) of the Taxes Act 1988.”
- (2) The amendment made by this paragraph has effect in relation to assets held on or after 16th March 2005 (whenever acquired).

*Capital redemption policies: removal of exclusion from loan relationships computations*

- 14 (1) Schedule 9 to FA 1996 (loan relationships: special computational provisions) is amended as follows.
- (2) In paragraph 1A(1) (credits and debits relating to life policies and capital redemption policies not to be brought into account) paragraph (b) (capital redemption policies) shall cease to have effect.
  - (3) This paragraph has effect in relation to a capital redemption policy on and after 10th February 2005 (whenever the capital redemption policy was effected).
  - (4) Where a capital redemption policy—
    - (a) is held by a company immediately before 10th February 2005, and
    - (b) on or after that date, is, for the purposes of Chapter 2 of Part 4 of FA 1996, a creditor relationship of the company,
 sub-paragraphs (5) and (6) apply.
  - (5) In any such case, Chapter 2 of Part 13 of ICTA (life policies etc: chargeable events) shall have effect as if—
    - (a) immediately before 10th February 2005, the company had assigned the whole of the rights conferred by the policy for money or money's worth, and
    - (b) the value of the consideration for the assignment had been equal to what the carrying value of the creditor relationship would have been had an accounting period of the company ended on that date;
 and Chapter 2 of Part 4 of FA 1996 shall have effect as if, immediately after 9th February 2005, the company had acquired the creditor relationship at a cost equal to that carrying value.

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- (6) But if—
- (a) the accounting period in which the assignment is deemed to have happened (“the assignment period”), and
  - (b) the accounting period in which the company ceases to be party to the creditor relationship (“the cessation period”),
- are not the same accounting period, any gain which, by virtue of the deemed assignment, would have fallen to be brought into account in accordance with section 547(1)(b) of ICTA for the assignment period shall instead be brought into account for the cessation period.
- (7) In this paragraph—
- “assignment”, in relation to Scotland, means an assignation;
  - “carrying value” has the same meaning as it has for the purposes of paragraph 19A of Schedule 9 to FA 1996, as it has effect for periods of account beginning on or after 1st January 2005.

*Deemed disposal of assets and liabilities on company ceasing to be resident in UK etc*

- 15 (1) In Schedule 9 to FA 1996 (loan relationships) paragraph 10A is amended as follows.
- (2) After sub-paragraph (1) (cases where the paragraph applies) insert—
- “(1A) But this paragraph does not apply if—
  - (a) paragraph 12A below (transferee company leaving group) applies in relation to the company, and
  - (b) the cessation in sub-paragraph (1)(a) or (b) above occurs at the same time as the cessation in sub-paragraph (1)(b) of that paragraph.”.
- (3) In sub-paragraph (2) (Schedule to have effect as if there had been an assignment and reacquisition) for “Schedule” substitute “ Chapter ”.
- (4) The amendments made by this paragraph have effect on and after 16th March 2005.

*Transactions not at arm's length: exceptions relating to groups of companies*

- 16 (1) In Schedule 9 to FA 1996 (loan relationships) paragraph 11 (transactions not at arm's length) is amended as follows.
- (2) For sub-paragraph (3) (exceptions relating to groups of companies) substitute—
- “(3) Sub-paragraph (1) above does not apply if the related transaction—
  - (a) is a transaction as a result of which paragraph 12 below (groups)—
  - (i) applies by virtue of sub-paragraph (1)(a) of it, or
  - (ii) would so apply, apart from sub-paragraph (2A) of it (transferor using fair value accounting), or
  - (b) is part of a series of transactions as a result of which that paragraph—
  - (i) applies by virtue of sub-paragraph (1)(b) of it, or
  - (ii) would so apply, apart from sub-paragraph (2A) of it.”.
- (3) In consequence, omit sub-paragraph (5) (construction of references to a member of a group).

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- (4) The amendments made by this paragraph have effect where the related transaction is on or after 16th March 2005.

*Continuity of treatment of groups etc: treatment of transferee company*

- 17 (1) In Schedule 9 to FA 1996 (loan relationships) paragraph 12 (continuity of treatment of groups etc) is amended as follows.

- (2) For sub-paragraph (2) (the credits and debits to be brought into account) substitute—

“(2) For the purpose of determining the credits and debits to be brought into account for the purposes of this Chapter in respect of the loan relationship—

- (a) for the accounting period in which the transaction or, as the case may be, the first of the series of transactions takes place, the transferor company shall be treated as having entered into that transaction for a consideration equal to the notional carrying value of the asset or liability representing the relationship; and
- (b) for any accounting period in which it is a party to the relationship, the transferee company shall be treated as if it had acquired the asset or liability representing the relationship for a consideration equal to the notional carrying value of the asset or liability.

For the purposes of this sub-paragraph, the notional carrying value is the amount that would have been the carrying value of the asset or liability in the accounts of the transferor company if a period of account had ended immediately before the date when the company ceased to be party to the loan relationship.”.

- (3) In sub-paragraph (2A) (paragraph 12 not to apply where transferor uses fair value accounting) for paragraph (aa) (treatment of transferee in respect of the transaction) substitute—

“(aa) paragraph (b) of sub-paragraph (2) above shall have effect in relation to the transferee company.”.

- (4) For sub-paragraph (8) (which applies paragraph 11(5) for construction of references to a member of a group) substitute—

“(8) In this paragraph references to a company which is a member of a group of companies shall be construed in accordance with section 170 of the Taxation of Chargeable Gains Act 1992.”.

- (5) In sub-paragraph (9) (interpretation) insert the following definition at the appropriate place—

““carrying value” has the same meaning as it has for the purposes of paragraph 19A below;”.

- (6) Where the period of account mentioned in the second sentence of the sub-paragraph (2) substituted by sub-paragraph (2) begins before 1st January 2005, “carrying value” shall be construed as if the period had begun on or after that date.

- (7) The amendments made by this paragraph have effect in any case where the relevant transaction is on or after 16th March 2005.

- (8) In this paragraph “the relevant transaction” means—

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- (a) the related transaction mentioned in sub-paragraph (1)(a) of paragraph 12 of Schedule 9 to FA 1996,
- (b) the first of the series of transactions mentioned in sub-paragraph (1)(b) of that paragraph, or
- (c) the transfer mentioned in sub-paragraph (1)(c) or (1)(d) of that paragraph, by virtue of which that paragraph applies or would apply apart from sub-paragraph (2A) of it.

*Transferee leaving group after replacing transferor as party to loan relationship*

- 18 (1) In Schedule 9 to FA 1996 (loan relationships) after paragraph 12 insert—

*“Transferee leaving group after replacing transferor as party to loan relationship*

12A (1) This paragraph applies in any case where—

- (a) paragraph 12 above applies—
  - (i) by virtue of sub-paragraph (1)(a) of that paragraph (“case A”), or
  - (ii) by virtue of sub-paragraph (1)(b) of that paragraph (“case B”), but
- (b) before the end of the relevant 6 year period, the transferee company ceases to be a member of the relevant group.

(2) In any such case, this Chapter shall have effect as if the transferee company had—

- (a) immediately before that cessation, assigned the asset or liability representing the relevant loan relationship for a consideration of an amount equal to its fair value at that time, and
- (b) immediately reacquired it for a consideration of the same amount,

but only if Condition 1 or 2 below is satisfied and sub-paragraph (5) below does not apply.

(3) Condition 1 is that if sub-paragraph (2) above has effect, a credit would in consequence of paragraph (a) of that sub-paragraph fall to be brought into account for the purposes of this Chapter by the transferee company.

(4) Condition 2 is that—

- (a) Condition 1 is not satisfied,
- (b) the loan relationship is a creditor relationship,
- (c) the company has a hedging relationship between a derivative contract and the creditor relationship, and
- (d) in consequence of paragraph 30A(2)(a) of Schedule 26 to the Finance Act 2002, a credit falls to be brought into account by the transferee company for the purposes of that Schedule in respect of the derivative contract.

(5) Where the transferee company ceases to be a member of the relevant group by reason only of an exempt distribution (see sub-paragraph (8))

- (a) sub-paragraph (2) above does not have effect, but

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- (b) if there is chargeable payment within 5 years after the making of the exempt distribution, sub-paragraph (6) below applies.
- (6) Where this sub-paragraph applies, this Chapter shall have effect as if—
- (a) the transferee company had, immediately before the making of the chargeable payment, assigned the asset or liability representing the relevant loan relationship,
  - (b) the assignment had been for a consideration of an amount equal to the fair value of the asset or liability immediately before the transferee company ceased to be a member of the relevant group, and
  - (c) the transferee company had immediately reacquired the asset or liability for a consideration of the same amount,
- but only if Condition 1 or 2 above, as modified by sub-paragraph (7) below, is satisfied.
- (7) The modifications are that—
- (a) in Condition 1, the references to sub-paragraph (2) above, and paragraph (a) of that sub-paragraph, are to be taken respectively as references to sub-paragraph (6) above and paragraphs (a) and (b) of that sub-paragraph, and
  - (b) in Condition 2, the reference to paragraph 30A(2)(a) of Schedule 26 to the Finance Act 2002 is to be taken as a reference to paragraph 30A(6)(a) and (b) of that Schedule.
- (8) In this paragraph—
- “assignment”, in relation to Scotland, means an assignment;
- “chargeable payment” has the meaning given by section 214(2) of the Taxes Act 1988;
- “exempt distribution” means a distribution which is exempt by virtue of section 213(2) of the Taxes Act 1988;
- “the relevant 6 year period” means the period of 6 years following—
- (a) in case A, the transaction mentioned in paragraph 12(1)(a) above, or
  - (b) in case B, the last of the series of transactions mentioned in paragraph 12(1)(b) above;
- “the relevant group” means—
- (a) in case A, the group mentioned in paragraph 12(1)(a) above, or
  - (b) in case B, the group mentioned in paragraph 12(1)(b) above;
- “the relevant loan relationship” means the loan relationship mentioned in paragraph 12(1) above;
- “the transferee company” means the company referred to as such in paragraph 12(1) above.
- (9) Paragraph 12(14) of Schedule 26 to the Finance Act 2002 (hedging relationships) has effect for the purposes of this paragraph.”.

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- (2) The amendment made by this paragraph has effect where a company ceases to be a member of a group on or after 16th March 2005.

*Avoidance involving repos or stock lending*

- 19 (1) In Schedule 9 to FA 1996 (loan relationships) paragraph 15 is amended as follows.
- (2) At the end of sub-paragraph (2) (disposals and acquisitions to which the paragraph applies) add “and as is, in the case of those arrangements, the disposal or acquisition effected by—
- (a) the transfer by A to B mentioned in sub-paragraph (3)(a) below, or
  - (b) any transfer to A that gives effect to the entitlement or requirement described in sub-paragraph (3)(b) below.”.
- (3) In sub-paragraph (3) (meaning of “repo or stock-lending arrangements”)—
- (a) in paragraph (a), after “one person” insert “ (“A”) ” and after “another” insert “ (“B”) ”;
  - (b) in paragraph (b), for “the transferor” substitute “ A ”.
- (4) In sub-paragraph (4A) (which states certain consequences of sub-paragraph (1) for each party), omit paragraph (b) (transferee not to be regarded as a party to the loan relationship) and the word “and” before it, and for the words following that paragraph substitute— “ but nothing in sub-paragraph (1) above prevents the person to whom those rights are transferred from being regarded for the purposes of this Chapter as being party to the loan relationship as a result of the transfer. ”.
- (5) The amendments made by this paragraph have effect in any case where the transfer mentioned in paragraph 15(3)(a) of Schedule 9 to FA 1996 is on or after 2nd December 2004, whenever the repo or stock-lending arrangements in question were entered into.
- (6) In any case involving an arrangement for the sale and repurchase of securities where the arrangement—
- (a) falls within section 737E(1)(b) of ICTA, and
  - (b) involves securities (“substituted securities”) being substituted for other securities,
- the substitution of any securities on or after 2nd December 2004 shall be treated for the purposes of sub-paragraph (5) as if it were a transfer falling within paragraph 15(3)(a) of Schedule 9 to FA 1996.

*Capital redemption policies: computations on the I minus E basis*

- 20 (1) In Schedule 11 to FA 1996 (loan relationships: special provision for insurers) paragraph 1 (I minus E basis) is amended as follows.
- (2) After sub-paragraph (1B) insert—
- “(1C) 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 credits or debits shall be brought into account in respect of any debtor relationship that represents a capital redemption policy, within the meaning of Chapter 2 of Part 13 of the Taxes Act 1988.”.

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- (3) The amendment made by this paragraph has effect in relation to a debtor relationship on and after 10th February 2005 (whenever the capital redemption policy was effected).

*Relevant discounted securities: corporate strips*

- 21 (1) Schedule 13 to FA 1996 (discounted securities: income tax) is amended as follows.
- (2) In paragraph 3 (meaning of “relevant discounted security”) in sub-paragraph (1), for “paragraph 14(1)” substitute “ paragraphs 13B(1) and 14(1) ”.
- (3) In paragraph 4 (meaning of “transfer”)—
- (a) in sub-paragraph (1), after “Subject to sub-paragraph (2)” insert “ and paragraph 13B(4) ”;
- (b) in sub-paragraph (5), after “without prejudice to paragraph” insert “ 13B(2) to (5) or ”.
- (4) In paragraph 5 (redemption to include conversion), in sub-paragraph (3), after “This paragraph does not apply to” insert “—
- (a) the conversion of an interest-bearing corporate security into corporate strips (see paragraph 13A(2) to (7) below), or
- (b) ”.
- (5) After paragraph 13 (excluded indexed securities) insert—

*“Meaning of corporate strip and conversion into corporate strips*

- 13A(1) In this Schedule “corporate strip” means any asset—
- (a) which is, or has at any time been, one of the separate assets mentioned in sub-paragraph (2) below, and
- (b) which is not prevented from being a corporate strip by sub-paragraph (9) below.
- (2) For the purposes of this Schedule a person converts an interest-bearing corporate security into corporate strips of the security if he has an interest-bearing corporate security (“the converted corporate security”) but—
- (a) as a result of any scheme or arrangements, he comes to have two or more separate assets in place of the converted corporate security,
- (b) each of those separate assets satisfies condition A,
- (c) those separate assets, taken together, satisfy condition B, and
- (d) at least one of those separate assets is not prevented from being a corporate strip by sub-paragraph (9) below,
- and related expressions shall be construed accordingly.
- (3) Condition A is that the asset—
- (a) represents the right to, or
- (b) secures,
- one or more stripped payments.
- (4) For the purposes of this paragraph, a “stripped payment” is—
- (a) the payment of, or
- (b) a payment corresponding to,



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the whole or a part of one or more payments (whether of interest or principal) remaining to be made under the converted corporate security.

- (5) Condition B is that the assets, taken together,—
- (a) represent the right to, or
  - (b) secure,
- every payment (whether of interest or principal) remaining to be made under the converted corporate security (or payments corresponding to every such payment).
- (6) Where a person—
- (a) has an interest-bearing corporate security, but
  - (b) sells or transfers the right to one or more payments remaining to be made under it (so that, as a result, there are two or more separate assets which, taken together, satisfy condition B),
- this Schedule has effect as if, as a result of a scheme or arrangements, the person had come to have the separate assets in place of the security immediately before the sale or transfer.
- (7) For the purposes of this Schedule, sub-paragraphs (2) to (6) above also have effect in relation to each of the separate assets mentioned in sub-paragraph (2) above as if it were itself an interest-bearing corporate security (if that is not in fact the case).
- (8) Where sub-paragraphs (2) to (6) above have effect by virtue of sub-paragraph (7) above—
- (a) any reference in this Schedule to converting an interest-bearing corporate security into corporate strips of the security shall be construed accordingly, and
  - (b) sub-paragraph (1) above (meaning of “corporate strip”) has effect accordingly.
- (9) An asset is not a corporate strip if it—
- (a) represents the right to, or
  - (b) secures,
- payments of, or corresponding to, a part of every payment remaining to be made under an interest-bearing corporate security or a corporate strip.
- (10) After a balance has been struck for a dividend on an interest-bearing corporate security, any payment to be made in respect of that dividend shall, at times falling after that balance has been struck, be treated for the purposes of this paragraph as not being a payment remaining to be made under the security.

References to payments the right to which a separate asset represents or secures shall be construed accordingly.

*Corporate strips deemed to be relevant discounted securities*

- 13B (1) Every corporate strip is a relevant discounted security.
- (2) Where a person converts an interest-bearing corporate security into corporate strips of the security, he shall be deemed to have paid, in respect of

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his acquisition of each corporate strip, an amount determined in accordance with sub-paragraph (3) below.

- (3) The amount is that which bears to the acquisition cost of the converted corporate security the proportion that SMV bears to TMV, where—  
SMV is the market value of the corporate strip, and  
TMV is the total of the market values of all the separate assets resulting from the conversion.
- (4) If the converted corporate security is a relevant discounted security—  
(a) its conversion into corporate strips is deemed to be a transfer of the security, and  
(b) the amount payable on the transfer is deemed to be an amount equal to the acquisition cost of the converted corporate security.
- (5) Where corporate strips are consolidated into a single security—  
(a) by being exchanged by any person for that security, or  
(b) by being otherwise converted by any person into that security under any arrangements,  
each of the corporate strips shall be deemed to have been redeemed, at the time of the exchange or other conversion, by the payment to that person of an amount equal to its market value.
- (6) Sub-paragraphs (2) to (5) above have effect for the purposes of this Schedule.
- (7) For the purposes of this paragraph, the acquisition cost of the converted corporate security is the amount paid in respect of his acquisition of the security by the person who has it immediately before the conversion (no account being taken of any costs incurred in connection with that acquisition).
- (8) References in this paragraph to the market value of a security given or received in exchange for, or otherwise converted into, another are references to its market value at the time of the exchange or conversion.

*Corporate strips: manipulation of acquisition, sale or redemption price*

- 13C (1) This paragraph applies in any case where, as a result of any scheme or arrangement,—  
(a) the amount paid by a person in respect of his acquisition of a corporate strip is or was more than the market value of the corporate strip at the time of that acquisition,  
(b) the amount payable to a person on a transfer of a corporate strip by him is less than the market value of the corporate strip at the time of the transfer, or  
(c) on redemption of a corporate strip, the amount payable to a person, as the person holding the corporate strip, is less than the market value of the corporate strip on the day before redemption,  
and the obtaining of a tax advantage by any person is the main benefit, or one of the main benefits, that might have been expected to accrue from, or from any provision of, the scheme or arrangement.

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- (2) In a case falling within sub-paragraph (1)(a) above, the person shall be treated for the purposes of paragraph 1(2)(b) above on a transfer of the corporate strip by him as if he had paid in respect of his acquisition of the corporate strip an amount equal to the market value of the corporate strip at the time of that acquisition.
- (3) In a case falling within sub-paragraph (1)(b) above, the person shall be treated for the purposes of paragraph 1(2)(b) above as if the amount payable to him on the transfer were an amount equal to the market value of the corporate strip at the time of the transfer.
- (4) In a case falling within sub-paragraph (1)(c) above, the person shall be treated for the purposes of paragraph 1(2)(b) above as if the amount payable to him on redemption were an amount equal to the market value of the corporate strip on the day before redemption.
- (5) The market value of a corporate strip at any time shall be determined for the purposes of this paragraph without regard to any increase or diminution in the value of the corporate strip as a result of the scheme or arrangement mentioned in sub-paragraph (1) above.
- (6) For the purposes of this paragraph, no account shall be taken of any costs incurred in connection with any transfer or redemption of a corporate strip or its acquisition.
- (7) In this paragraph “tax advantage” has the meaning given by section 709(1) of the Taxes Act 1988.

*Corporate strips: manipulation of price:  
associated payment giving rise to CGT loss*

13D(1) Where—

- (a) as a result of any scheme or arrangement which has an unallowable purpose, the circumstances are, or might have been, as mentioned in paragraph (a), (b) or (c) of paragraph 13C(1) above,
  - (b) under the scheme or arrangement, a payment falls to be made otherwise than in respect of the acquisition or disposal of a corporate strip, and
  - (c) as a result of that payment or the circumstances in which it is made, a loss accrues to any person for the purposes of capital gains tax,
- the loss shall not be an allowable loss for the purposes of capital gains tax.
- (2) For the purposes of this paragraph, a scheme or arrangement has an unallowable purpose if the main benefit, or one of the main benefits, that might have been expected to result from, or from any provision of, the scheme or arrangement (apart from paragraph 13C above and this paragraph) is—
    - (a) the obtaining of a tax advantage by any person, or
    - (b) the accrual to any person of an allowable loss for the purposes of capital gains tax.
  - (3) In this paragraph “tax advantage” has the meaning given by section 709(1) of the Taxes Act 1988.”

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- (6) In paragraph 15(1) (general interpretation) insert each of the following definitions at the appropriate place—
- ““corporate strip” has the meaning given by paragraph 13A above;”;
- ““interest-bearing corporate security” means any interest-bearing security other than—
- (a) a security issued by the government of a territory;
- (b) a share in a company;”;
- ““interest-bearing security” includes any loan stock or similar security;”.
- (7) In paragraph 15(1)—
- (a) in the definition of “relevant discounted security”, after “paragraphs 3” insert “ , 13B(1) ”;
- (b) in the definition of “strip”, after “ “strip” ” insert “ , except in the expression “corporate strip”, ”.
- (8) The amendments made by this paragraph have effect in any case where a person acquires a corporate strip on or after 2nd December 2004 otherwise than in pursuance of an agreement entered into before that date.

*Transactions within groups: treatment of transferee company*

- 22 (1) In Schedule 26 to FA 2002 (derivative contracts) paragraph 28 (transactions within groups) is amended as follows.
- (2) For sub-paragraph (3) (the credits and debits to be brought into account) substitute—
- “(3) For the purpose of determining the credits and debits to be brought into account for the purposes of this Schedule in respect of the derivative contract—
- (a) for the accounting period in which the transaction or, as the case may be, the first of the series of transactions takes place, the transferor company shall be treated as having entered into that transaction for a consideration equal to the notional carrying value of the contract; and
- (b) for any accounting period in which it is a party to the contract, the transferee company shall be treated as if it had acquired the contract for a consideration equal to its notional carrying value.
- For the purposes of this sub-paragraph the notional carrying value is the amount that would have been the carrying value of the derivative contract in the accounts of the transferor company if a period of account had ended immediately before the date when the company ceased to be party to the contract.”.
- (3) In sub-paragraph (5), after “In this paragraph” insert the following definition—
- ““carrying value” has the same meaning as it has for the purposes of paragraph 50A;”.
- (4) Where the period of account mentioned in the second sentence of the sub-paragraph (3) substituted by sub-paragraph (2) begins before 1st January 2005, “carrying value” shall be construed as if the period had begun on or after that date.

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- (5) The amendments made by this paragraph have effect in any case where the relevant transaction is on or after 16th March 2005.
- (6) In this paragraph “the relevant transaction” means—
- (a) the related transaction mentioned in sub-paragraph (2)(a) of paragraph 28 of Schedule 26 to FA 2002,
  - (b) the first of the series of transactions mentioned in sub-paragraph (2)(b) of that paragraph, or
  - (c) the transfer mentioned in sub-paragraph (2)(c) or (2)(d) of that paragraph, by virtue of which that paragraph applies or would apply apart from paragraph 30 of that Schedule.

*Transactions within groups: fair value accounting*

- 23 (1) In Schedule 26 to FA 2002 (derivative contracts) paragraph 30 (transactions within groups: fair value accounting) is amended as follows.
- (2) In sub-paragraph (1), for paragraph (b) (treatment of transferee in respect of the transaction) substitute—
- “(b) paragraph 28(3)(b) shall have effect in relation to the transferee company.”.
- (3) The amendment made by this paragraph has effect in any case where the relevant transaction is on or after 16th March 2005.
- (4) In this paragraph “the relevant transaction” has the same meaning as in paragraph 22.

*Transferee leaving group after replacing transferor as party to derivative contract*

- 24 (1) In Schedule 26 to FA 2002 (derivative contracts) after paragraph 30 insert—
- “Transferee leaving group after replacing transferor as party to derivative contract*
- 30A (1) This paragraph applies in any case where—
- (a) paragraph 28 applies—
    - (i) by virtue of sub-paragraph (2)(a) of that paragraph (“case A”), or
    - (ii) by virtue of sub-paragraph (2)(b) of that paragraph (“case B”), but
  - (b) before the end of the relevant 6 year period, the transferee company ceases to be a member of the relevant group.
- (2) In any such case, this Schedule shall have effect as if the transferee company had—
- (a) immediately before that cessation, assigned its rights and liabilities under the relevant derivative contract for a consideration of an amount equal to their fair value at that time, and
  - (b) immediately reacquired them for a consideration of the same amount,
- but only if Condition 1 or 2 is satisfied and sub-paragraph (5) does not apply.

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- (3) Condition 1 is that if sub-paragraph (2) has effect, a credit would in consequence of paragraph (a) of that sub-paragraph fall to be brought into account for the purposes of this Schedule by the transferee company.
- (4) Condition 2 is that—
- (a) Condition 1 is not satisfied,
  - (b) the company has a hedging relationship between the relevant derivative contract and a creditor relationship, and
  - (c) in consequence of paragraph 12A(2)(a) of Schedule 9 to the Finance Act 1996, a credit falls to be brought into account by the transferee company for the purposes of Chapter 2 of Part 4 of the Finance Act 1996 in respect of the creditor relationship.
- (5) Where the transferee company ceases to be a member of the relevant group by reason only of an exempt distribution (see sub-paragraph (8))—
- (a) sub-paragraph (2) does not have effect, but
  - (b) if there is chargeable payment within 5 years after the making of the exempt distribution, sub-paragraph (6) applies.
- (6) Where this sub-paragraph applies, this Chapter shall have effect as if—
- (a) the transferee company had, immediately before the making of the chargeable payment, assigned its rights and liabilities under the relevant derivative contract,
  - (b) the assignment had been for a consideration of an amount equal to the fair value of those rights and liabilities immediately before the transferee company ceased to be a member of the relevant group, and
  - (c) the transferee company had immediately reacquired those rights and liabilities for a consideration of the same amount,
- but only if Condition 1 or 2, as modified by sub-paragraph (7), is satisfied.
- (7) The modifications are that—
- (a) in Condition 1, the references to sub-paragraph (2), and paragraph (a) of that sub-paragraph, are to be taken respectively as references to sub-paragraph (6) and paragraphs (a) and (b) of that sub-paragraph, and
  - (b) in Condition 2, the reference to paragraph 12A(2)(a) of Schedule 9 to the Finance Act 1996 is to be taken as a reference to paragraph 12A(6)(a) and (b) of that Schedule.
- (8) In this paragraph—
- “assignment”, in relation to Scotland, means an assignation;
- “chargeable payment” has the meaning given by section 214(2) of the Taxes Act 1988;
- “exempt distribution” means a distribution which is exempt by virtue of section 213(2) of the Taxes Act 1988;
- “creditor relationship” has the same meaning as in Chapter 2 of Part 4 of the Finance Act 1996 (see section 103(1) of that Act);

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“the relevant 6 year period” means the period of 6 years following—

- (a) in case A, the transaction mentioned in paragraph 28(2)(a), or
- (b) in case B, the last of the series of transactions mentioned in paragraph 28(2)(b);

“the relevant derivative contract” means the derivative contract mentioned in paragraph 28(1);

“the relevant group” means—

- (a) in case A, the group mentioned in paragraph 28(2)(a), or
- (b) in case B, the group mentioned in paragraph 28(2)(b);

“the transferee company” means the company referred to as such in paragraph 28(1).”.

- (2) The amendment made by this paragraph has effect where a company ceases to be a member of a group on or after 16th March 2005.

*Deeply discounted securities: corporate strips*

- 25 (1) Chapter 8 of Part 4 of ITTOIA 2005 (profits from deeply discounted securities) is amended as follows.
- (2) In section 430 (meaning of “deeply discounted security”) in subsection (6) (subjections) omit “and” before the entry relating to section 443(1) and at the end of that entry add “, and section 452A(1) (corporate strips).”.
  - (3) In section 437 (transactions which are disposals) after subsection (4) insert—
    - “(5) In the case of interest-bearing corporate securities, further provision about occasions counting as disposals is made by section 452F(2)(a).
    - (6) In the case of corporate strips, further provision about occasions counting as disposals is made by section 452F(2)(a) and (3)(a).”.
  - (4) In section 438 (timing of transfers and acquisitions) for subsection (4) substitute—
    - “(4) This section is subject to—
      - section 445(7) (exchanges for and consolidations of strips);
      - section 452F(4) (conversion into and consolidations of corporate strips).”.
  - (5) In section 440 (market value disposals) for subsection (5) substitute—
    - “(5) Subsection (4) is subject to—
      - section 445(8) (exchanges for and consolidations of strips);
      - section 452F(5) (conversion into and consolidations of corporate strips).”.
  - (6) In section 441 (market value acquisitions) for subsection (3) substitute—
    - “(3) Subsection (2) is subject to—
      - section 445(8) (exchanges for and consolidations of strips);
      - section 452F(5) (conversion into and consolidations of corporate strips).”.

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- (7) In section 444 (meaning of “strip” in Chapter 8) after subsection (5) insert—
- “(6) Nothing in this section affects the meaning of the expression “corporate strip” in this Chapter (see section 452E).”.
- (8) After section 452 insert—

*“Special rules for corporate strips*

#### **452A Application of this Chapter to corporate strips**

- (1) All corporate strips are treated as deeply discounted securities for the purposes of this Chapter, whether or not they would otherwise be so.
- (2) This Chapter applies to corporate strips subject to the rules in—
  - (a) section 452F (corporate strips: acquisitions and disposals), and
  - (b) section 452G (corporate strips: manipulation of acquisition, transfer or redemption payments).

#### **452B Meaning of “interest-bearing corporate security” in Chapter 8**

- (1) In this Chapter “interest-bearing corporate security” means any interest-bearing security other than—
  - (a) a security issued by the government of a territory, or
  - (b) a share in a company.
- (2) In this section “interest-bearing security” includes any loan stock or similar security.
- (3) Section 452D(4)(a) gives an extended meaning to references to converting an interest-bearing corporate security into corporate strips (and related expressions).

#### **452C Conversion of interest-bearing corporate securities into corporate strips**

- (1) For the purposes of this Chapter a person converts an interest-bearing corporate security into corporate strips of the security if he has an interest-bearing corporate security (“the converted corporate security”) but—
  - (a) as a result of any scheme or arrangements, he acquires two or more separate assets in place of the converted corporate security,
  - (b) each of those separate assets satisfies condition A,
  - (c) those separate assets, taken together, satisfy condition B, and
  - (d) at least one of those separate assets is not prevented from being a corporate strip by section 452E(2) or (3),
 and related expressions shall be construed accordingly.
- (2) Condition A is that the asset—
  - (a) represents the right to, or
  - (b) secures,
 one or more stripped payments.
- (3) For the purposes of this section, a “stripped payment” is—



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- (a) the payment of, or
  - (b) a payment corresponding to,the whole or a part of one or more payments (whether of interest or principal) remaining to be made under the converted corporate security.
- (4) Condition B is that the assets, taken together,—
  - (a) represent the right to, or
  - (b) secure,every payment (whether of interest or principal) remaining to be made under the converted corporate security (or payments corresponding to every such payment).
- (5) Where a person—
  - (a) has an interest-bearing corporate security, but
  - (b) sells or transfers the right to one or more payments remaining to be made under it (so that, as a result, there are two or more separate assets which, taken together, satisfy condition B),this Chapter has effect as if, as a result of a scheme or arrangements, the person had acquired the separate assets in place of the security immediately before the sale or transfer.
- (6) After a balance has been struck for a dividend on an interest-bearing corporate security, any payment to be made in respect of that dividend shall, at times falling after that balance has been struck, be treated for the purposes of this paragraph as not being a payment remaining to be made under the security.

#### **452D Conversion into corporate strips: lower level conversions**

- (1) For the purposes of this Chapter, section 452C also has effect in relation to each of the separate assets mentioned in subsection (1) of that section as if that separate asset were itself an interest-bearing corporate security (if that is not in fact the case).
- (2) In subsection (1), the reference to section 452C includes a reference to that section as it has effect by virtue of this section.
- (3) In the application of section 452C by virtue of this section, references to payments the right to which a separate asset represents or secures shall be construed in accordance with subsection (6) of that section.
- (4) Where section 452C has effect by virtue of subsection (1)—
  - (a) any reference in this Chapter to converting an interest-bearing corporate security into corporate strips of the security shall be construed accordingly, and
  - (b) section 452E (meaning of “corporate strip”) has effect accordingly.

#### **452E Meaning of “corporate strip” in Chapter 8**

- (1) In this Chapter “corporate strip” means any asset—
  - (a) which is, or has at any time been, one of the separate assets mentioned in section 452C(1), and

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- (b) which is not prevented from being a corporate strip by subsection (2) or (3).
- (2) An asset is not a corporate strip if it—
  - (a) represents the right to, or
  - (b) secures,
    - payments of, or corresponding to, a part of every payment remaining to be made under an interest-bearing corporate security or a corporate strip.
- (3) An asset is a corporate strip in the case of any person only if he acquired it—
  - (a) on or after 2nd December 2004, and
  - (b) otherwise than in pursuance of an agreement entered into before that date.

#### **452F Corporate strips: acquisitions and disposals**

- (1) A person who converts an interest-bearing corporate security into corporate strips of the security is treated as having acquired each corporate strip by the payment of an amount equal to—

$$A \times \frac{B}{C}$$

where—

A is the acquisition cost of the converted corporate security;

B is the market value of the corporate strip;

C is the total of the market values of all the separate assets resulting from the conversion.

- (2) If the converted corporate security is a deeply discounted security—
  - (a) its conversion into corporate strips is to be treated for the purposes of this Chapter as a transfer of the security, but
  - (b) the amount payable on the transfer is taken to be an amount equal to the acquisition cost of the converted corporate security.
- (3) For the purposes of this Chapter—
  - (a) the consolidation of a corporate strip with other corporate strips into a single security is a disposal of the corporate strip by the person consolidating it (whether or not it would be apart from this subsection), and
  - (b) an amount equal to the market value of the corporate strip at the consolidation is treated as payable on the disposal.
- (4) Section 438 (timing of transfers and acquisitions) does not apply to a conversion within subsection (1) or a consolidation within subsection (3).

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- (5) Subsections (1) to (3) apply instead of sections 440(4) (market value on general conversions of deeply discounted securities) and 441 (market value acquisitions).
- (6) For the purposes of this section, the acquisition cost of the converted corporate security is the amount paid in respect of his acquisition of the security by the person who has it immediately before the conversion (no account being taken of any costs incurred in connection with that acquisition).
- (7) References in this section to the market value of a security given or received in exchange for, or otherwise converted into, another are references to its market value at the time of the exchange or conversion.

#### **452G Corporate strips: manipulation of acquisition, transfer or redemption payments**

- (1) This section applies if—
  - (a) as a result of any scheme or arrangement, an amount referred to in subsection (2)(a), (b) or (c) differs from the market value of the corporate strip in a way specified in that subsection, and
  - (b) the obtaining of a tax advantage by any person is the main benefit, or one of the main benefits, that might have been expected to accrue from, or from any provision of, the scheme or arrangement.
- (2) The ways are that—
  - (a) the amount paid by a person in respect of the acquisition of the corporate strip is or was more than the market value of the corporate strip at the time of that acquisition,
  - (b) the amount payable to a person on transferring the corporate strip is less than the market value at the time of the transfer, or
  - (c) on redemption of the corporate strip the amount payable to a person, as the person holding the corporate strip, is less than the market value on the day before redemption.
- (3) In a case within subsection (2)(a), for the purposes of section 439(1) on transferring the corporate strip the person is treated as if the person had paid to acquire the corporate strip an amount equal to the market value of the corporate strip at the time of the acquisition.
- (4) In a case falling within subsection (2)(b), for those purposes the person is treated as if the amount payable to the person on the transfer were an amount equal to the market value of the corporate strip at the time of the transfer.
- (5) In a case falling within subsection (2)(c), for those purposes the person is treated as if the amount payable to the person on redemption were an amount equal to the market value of the corporate strip on the day before redemption.
- (6) The market value of a corporate strip at any time is to be determined for the purposes of this section without regard to any increase or diminution in the value of the corporate strip as a result of the scheme or arrangement mentioned in subsection (1).

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(7) For the purposes of this section, no account is to be taken of any incidental expenses incurred in connection with any disposal or acquisition of a corporate strip.”.

(9) In Schedule 4 (abbreviations and defined expressions) in Part 2 (expressions defined in the Act or in ICTA) insert each of the following entries at the appropriate place—

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“conversion of an interest-bearing corporate security into corporate strips of the security (for the purposes of Chapter 8 of Part 4)	sections 452C and 452D”;
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“corporate strip (for the purposes of Chapter 8 of Part 4)	section 452E”;
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“interest-bearing corporate security (for the purposes of Chapter 8 of Part 4)	section 452B”.
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(10) ITTOIA 2005 shall have effect as if it had been originally enacted with the amendments made by this paragraph.

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