STATUTORY INSTRUMENTS

2004 No. 3271

INCOME TAX

The Loan Relationships and Derivative Contracts (Change Of Accounting Practice) Regulations 2004

Made - - - -	*9th December 2004*
Laid before the House of Commons - - - -	*10th December 2004*
Coming into force - -	*1st January 2005*

The Treasury, in exercise of the powers conferred upon them by sections 85B(3) and (5) and 90A of, and paragraph 19B of Schedule 9 to, the Finance Act 1996(**1**) and paragraph 17C of Schedule 26 to the Finance Act 2002(**2**), make the following Regulations:

Citation, commencement and effect

1.—(1) These Regulations may be cited as the Loan Relationships and Derivative Contracts (Change of Accounting Practice) Regulations 2004 and shall come into force on 1st January 2005.

(2) These Regulations have effect in relation to periods of account beginning on or after 1st January 2005.

Interpretation

2. In these Regulations—

"amortised cost basis of accounting" has the meaning given by section 103(1) of the Finance Act 1996(**3**);

"fair value accounting" has the meaning given by section 103(1) of the Finance Act 1996;

"impairment" and "impairment loss" have the meanings given by section 103(1) of the Finance Act 1996(**4**).

(**1**) 1996 c. 8. Sections 85B(3) and (5) and 90A were inserted by paragraph 3 of Schedule 10 to the Finance Act 2004 (c. 12) and paragraph 19B was inserted by paragraph 36 of that Schedule.
(**2**) Paragraph 17C was inserted by section 52 of, and paragraph 50 of Schedule 10 to, the Finance Act 2004.
(**3**) This definition was inserted by section 52 of, and paragraph 17 of Schedule 10 to, the Finance Act 2004.
(**4**) These definitions were inserted by paragraph 17 of Schedule 10 to the Finance Act 2004.

Credits and debits not to be brought into account

3. The debits and credits prescribed in regulation 4 shall not be brought into account in the first accounting period of a company beginning on or after 1st January 2005, but shall be brought into account in the first accounting period of the company beginning on or after 1st January 2006.

Prescribed debits and credits

4.—(1) Subject to paragraph (2), the debits and credits prescribed for the purpose of regulation 3 are any debits or credits in the first accounting period of a company beginning on or after 1st January 2005 which must be brought into account in accordance with—

(a) section 85B(1)(b) of the Finance Act 1996 (amounts recognised in determining company's profit or loss)where the debit or credit represents a prior period adjustment;

(b) paragraph 19A(3) of Schedule 9 to the Finance Act 1996 (adjustment on change of accounting policy);

(c) paragraph 17B(1)(b) of Schedule 26 to the Finance Act 2002 (amounts recognised in determining company's profit or loss) where the debit or credit represents a prior period adjustment;

(d) paragraph 50A(2) of Schedule 26 to the Finance Act 2002 (adjustment on change of accounting policy).

(2) The debits and credits falling within any of paragraphs (3), (4), (6) and (7) are not prescribed.

(3) The debits or credits falling within this paragraph are debits or credits in relation to an asset or liability representing a loan relationship of a company (referred to in this regulation respectively as "a relevant asset" and "a relevant liability") where the latest date on which it falls to be fully discharged is within an accounting period of the company which begins on or after 1st January 2005 and ends before 1st January 2006.This paragraph is subject to paragraphs (6) and (7).

(4) The debits or credits falling within this paragraph are those in relation to a derivative contract to which—

(a) regulation 4 of the Disregard Regulations applies, if the matched asset is a relevant asset; or

(b) the Disregard Regulations do not apply, if there is a hedging relationship between the derivative contract and a hedged item which is a relevant asset or liability.

(5) In paragraph (4) "the Disregard Regulations" means the Loan Relationships and Derivative Contracts (Disregard and Bringing into Account of Profits and Losses) Regulations 2004 and expressions which are defined for the purposes of those Regulations have the same meanings in that paragraph (4) as they have in those Regulations.

(6) The debits falling within this paragraph are debits in relation to an asset representing a loan relationship falling within section 94A of the Finance Act 1996 (loan relationships with embedded derivatives) to the extent that the debit falling within section 85B(1)(b) of, or paragraph 19A(3) of Schedule 9 to, the Finance Act 1996 in relation to the host contract does not exceed the amount produced by the formula C – I.

Here—

C is the amount of any credit given in relation to the loan relationship for the accounting periods of the company beginning on or after 1st January 2005 but before 1st January 2006, and

I is the amount of interest receivable under the loan relationship for those periods.

(7) The credits falling within this paragraph are credits in relating to an asset representing a loan relationship falling within section 94A of the Finance Act 1996 (loan relationships with embedded derivatives) to the extent that the debit falling within section 85B(1)(b) of, or paragraph 19A(3) of

Schedule 9 to, the Finance Act 1996 in relation to the host contract does not exceed the amount produced by the formula D – I.

Here—

D is the amount of any debit given in relation to the loan relationship for the accounting periods of the company beginning on or after 1st January 2005 but before 1st January 2006, and

I is the amount of interest receivable under the loan relationship for those periods.

Amounts recognised in determining a company's profit or loss in relation to held-to-maturity assets

5.—(1) Subject to paragraph (6), if the assets representing a loan relationship of a company satisfy the conditions prescribed in paragraph (5) and in accordance with generally accepted accounting practice those assets—

(a) were previously dealt with for accounting purposes on an amortised cost basis of accounting and

(b) are subsequently required to be dealt with for accounting purposes on the basis of fair value accounting,

the debits and credits to be brought into account for the purposes of Chapter 2 of Part 4 of the Finance Act 1996 shall continue to be determined on an amortised cost basis of accounting.

(2) Subject to paragraph (6), the amounts described in paragraphs (3) and (4) are excluded from section 85B(1) of the Finance Act 1996 in the circumstances specified in those paragraphs.

(3) If the assets representing a loan relationship of a company satisfy the conditions prescribed in paragraph (5), the amount is any debit or credit representing the difference between the carrying value of the asset recognised for accounting purposes at the time the company ceased to treat the asset as held-to-maturity and the fair value of the asset immediately after that time.

(4) If the assets representing a loan relationship of a company cease to satisfy the conditions prescribed in paragraph (5), the amount is any debit or credit representing profits or losses—

(a) brought into account in the statement of realised gains or losses or statement of changes in equity for the periods in which the asset was treated as available-for-sale,

(b) which are transferred from the statement of realised gains or losses or statement of changes in equity for the period in which the company ceased to satisfy the conditions in paragraph (5), and

(c) which are brought into account in the company's profit and loss account or income statement for the period in which the company ceased to satisfy the conditions in paragraph (5) and any subsequent accounting period.

(5) The conditions prescribed in relation to an asset are that—

(a) in accordance with generally accepted accounting practice, it is treated at any time as available-for-sale,

(b) in accordance with generally accepted accounting practice, it has at any previous time been treated as held-to-maturity,

(c) it becomes treated as available-for-sale as a result of the disposal by the company of one or more assets previously treated as held-to-maturity, and

(d) the amortised cost of the asset or assets disposed of (referred to in paragraph (c)) in the accounting period in which the disposal was made is greater than 10% of the amortised cost of all the assets then treated by the company as held-to-maturity in that period.

(6) A company may elect that this regulation does not apply.

(7) An election under paragraph (6) applies to all of the company's assets which satisfy the conditions in paragraph (5).

(8) An election under paragraph (6)—

(a) shall be made by notice in writing to the Inland Revenue,

(b) within 90 days of the end of the company's accounting period in which the disposal mentioned in paragraph (5)(c) took place,

has effect for the succeeding accounting period and all subsequent accounting periods until the assets representing a loan relationship of the company cease to satisfy the conditions prescribed in paragraph (5).

Derek Twigg
Jim Murphy
Two of the Lords Commissioners of Her Majesty's Treasury

9th December 2004

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations make provision for certain credits and debits not to be brought into account in the first accounting period of a company beginning on or after 1st January 2005, are for those credits and debits instead to be brought into account in the first accounting period beginning on or after 1st January 2006.

Regulation 1 provides for the citation and commencement of the Regulations, and regulation 2 for interpretation.

Regulation 3 provides that the debits and credits prescribed by regulation 4 shall not be brought into account in the first accounting period of a company beginning on or after 1st January 2005, but shall instead be brought into account in the first accounting period of a company beginning on or after 1st January 2006.

Regulation 4 prescribes the debits and credits referred to in regulation 3.

Regulation 5 allows companies which hold assets which they have treated for accounting purposes as held-to-maturity and which subsequently are required to be treated for those purposes as available-for-sale may continue to be treated for tax purposes as if they were held-to-maturity. The concepts of assets which are held-to maturity or available-for sale are set out in International Accounting Standards 32 and 39 issued by the International Accounting Standards Board.

These Regulations do not impose new costs on business.