

2005 No. 3422

INCOME TAX

CORPORATION TAX

The Loan Relationships and Derivative Contracts (Exchange Gains and Losses using Fair Value Accounting) Regulations 2005

<i>Made</i> - - - -	<i>12th December 2005</i>
<i>Laid before the House of Commons</i>	<i>12th December 2005</i>
<i>Coming into force</i> - -	<i>2nd January 2006</i>

The Treasury, in exercise of the powers conferred upon them by section 103(1AA) of the Finance Act 1996(a) and paragraph 54(2A) of Schedule 26 to the Finance Act 2002(b) make the following Regulations:

Citation, commencement and effect

1. These Regulations may be cited as the Loan Relationships and Derivative Contracts (Exchange Gains and Losses using Fair Value Accounting) Regulations 2005 and shall come into force on 2nd January 2006 and shall have effect in relation to periods of account beginning on or after 1st January 2005.

Interpretation

2.—(1) In these Regulations—

“derivative contract” has the same meaning as in Schedule 26 to the Finance Act 2002;

“fair value accounting” has the meaning given in section 103 of the Finance Act 1996;

“generally accepted accounting practice” has the meaning given in section 50 of the Finance Act 2004(c);

“loan relationship” has the same meaning as in Chapter 2 of Part 4 of the Finance Act 1996; and

(a) 1996 c.8. Sub-section (1AA) was inserted by paragraph 29 of Schedule 4 to the Finance Act 2005 with effect for periods of account beginning on or after 1st January 2005 and substituted by paragraph 10 of Schedule 6 to the Finance (No. 2) Act 2005 with effect from 20 July 2005.

(b) 2002 c.23. Sub-paragraph (2A) was inserted by paragraph 36 of Schedule 4 to the Finance Act 2005 with effect for periods of account beginning on or after 1st January 2005 and substituted by paragraph 11 of Schedule 6 to the Finance (No.2) Act 2005 with effect from 20 July 2005.

(c) 2004 c.12.

“designated”, “fair value”, “available-for-sale” and “fair value hedge” have the same meanings as they have for accounting purposes.

Currency

3. For the purposes of these Regulations the currency with which a company computes its profits and losses as determined by sections 92 to 92E(a) of the Finance Act 1993(b) shall be known as the “base currency”.

Exchange gain or loss : general

4. In these Regulations exchange gain or loss shall not include any debits or credits referred to in regulation 4(1), (3) and (4) of the Loan Relationships and Derivative Contracts (Change of Accounting Practice) Regulations 2004(c).

Exchange gain or loss arising from loan relationship assets or liabilities

5.—(1) Paragraphs (2) and (3) set out the rules for calculating the exchange gain or loss arising from loan relationship assets or liabilities in the following circumstances—

- (a) the asset or liability is accounted for at fair value, or
- (b) that asset or liability or part of it is a hedged item in a designated fair value hedge and the risk being hedged is or includes exchange risk.

(2) Where paragraph (1) applies and—

- (a) an amount is recognised in the company’s profit and loss account or income statement which arises from comparing at different times the fair value of the asset or liability (or in the case of regulation 5(1)(b) any part of it), and
- (b) the change in fair value is attributable to any extent to fluctuations in the spot rate of exchange between the currency in which the asset or liability is denominated and the base currency of the company,

the exchange gain or loss is calculated as set out in paragraph (3).

(3) The exchange gain or loss for any accounting period is the change in fair value between the earlier and the later time in that period that is attributable only to fluctuations in the spot rate of exchange between the currency in which the asset or liability is denominated and the base currency of the company.

6. If an asset is accounted for as available-for-sale, the exchange gain or loss is the amount shown in the profit and loss account or income statement which fairly represents that gain or loss in accordance with generally accepted accounting practice.

Exchange gain or loss arising from derivative contracts

7.—(1) Paragraphs (2) and (3) set out the rules for calculating the exchange gain or loss arising from derivative contracts where such a contract is accounted for at fair value.

(2) Where—

- (a) an amount is recognised in the company’s profit and loss account or income statement which arises from comparing at different times the fair value of the derivative contract, and

(a) Sections 92 to 92E were substituted for former sections 92 to 94AB by paragraph 77 of Schedule 10 to the Finance Act 2004 with effect for periods of account beginning on or after 1st January 2005 and, in the case of a company required to prepare accounts under the Companies Act 1985 or the Companies Act (Northern Ireland) Order 1986, any period of account beginning before that date for which the company is required or permitted to prepare such accounts in accordance with international accounting standards.

(b) 1993 c. 34.

(c) S.I. 2004/3271.

- (b) that change in fair value is attributable to any extent to fluctuations in the spot rate of exchange between the base currency of the company and one or more currencies that form part of—
 - (i) the underlying subject matter of the derivative contract, or
 - (ii) in a case in which that currency or those currencies do not form part of the underlying subject matter of the contract, the currency or currencies in which payments under the contract fall to be made,

the exchange gain or loss is calculated as set out in paragraph (3).

(3) The exchange gain or loss for any accounting period is the change in fair value between the earlier and the later time in that period that is attributable only to fluctuations in the spot rate of exchange between the currency or currencies and the base currency.

Calculation of residual profit and loss

8. Regulation 9 applies where there is a fair value profit or loss in relation to a loan relationship or derivative contract which is not wholly an exchange gain or loss (as determined by regulations 5 to 7).

9.—(1) Where there is a fair value profit, the residual profit is calculated by subtracting from the profit any exchange gain, and adding to it the amount of any exchange loss.

(2) Where the exchange gain exceeds the fair value profit, the difference between the two is the residual loss.

(3) Where there is a fair value loss, the residual loss is calculated by adding to the loss any exchange gain or subtracting from it any exchange loss.

(4) Where the exchange loss exceeds the fair value loss the difference between the two is the residual profit.

(5) Residual profits and losses are amounts recognised in determining a company's profit or loss for a period for the purposes of section 85B(1)(a) of the Finance Act 1996 and paragraph 17B(1)(b) of Schedule 26 to the Finance Act 2002.

Vernon Coaker

Dave Watts

Two of the Lords Commissioners of Her Majesty's Treasury

12th December 2005

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- (a) This section together with section 85A substituted for former sections 85 and 86 by paragraph 3 of Schedule 10 to the Finance Act 2004 with effect for periods of account beginning on or after 1st January 2005, and, in the case of a company required to prepare accounts under the Companies Act 1985 or the Companies Act (Northern Ireland) Order 1986, any period of account beginning before that date for which the company is required or permitted to prepare such accounts in accordance with international accounting standards.
 - (b) Paragraphs 17A to 17C were substituted for former paragraphs 17 to 20 by paragraph 50 of Schedule 10 to the Finance Act 2004 with effect for periods of account beginning on or after 1st January 2005, and, in the case of a company required to prepare accounts under the Companies Act 1985 or the Companies Act (Northern Ireland) Order 1986, any period of account beginning before that date for which the company is required or permitted to prepare such accounts in accordance with international accounting standards.

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations set out the calculations for exchange gain and loss in loan relationships and derivative contracts where the assets and liabilities involved are accounted for using fair value accounting.

Regulation 1 provides for citation, commencement and effect.

Regulation 2 provides for interpretation.

Regulation 3 sets out the application of the term “currency” to these Regulations.

Regulation 4 provides that exchange gain or loss does not include debits or credits referred to in parts of regulation 4 of the Loan Relationships and Derivative Contracts (Change of Accounting Practice) Regulations (S.I. 2004/3271).

Regulations 5 and 6 set out how to calculate exchange gain or loss arising from loan relationship assets and liabilities.

Regulation 7 sets out how to calculate exchange gain and loss arising from derivative contracts.

Regulations 8 and 9 set out how to calculate the residual profit or loss in relation to a loan relationship or derivative contract.

Regulation 9(5) clarifies that residual profits and losses are amounts recognised in determining a company’s profit or loss for the purposes of section 85B(1) of the Finance Act 1996 and paragraph 17(B)(1) of Schedule 26 to the Finance Act 2002.

These Regulations do not impose any new costs on business.

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