
STATUTORY INSTRUMENTS

2006 No. 3269

The Finance Act 2002, Schedule 26,
(Parts 2 and 9) (Amendment) Order 2006

Amendment of Part 9 of Schedule 26

Substitution of paragraphs 44 and 45 of Schedule 26

10. For paragraphs 44 and 45 substitute—

“Contracts which become derivative contracts

43A.—(1) This paragraph applies if—

- (a) a company is a party to a relevant contract which (having not been a derivative contract) becomes a derivative contract, and
- (b) immediately before the time at which the relevant contract becomes a derivative contract, the relevant contract is a chargeable asset.

(2) The company shall, when it ceases to be a party to the relevant contract, bring into account (for the accounting period in which it ceases to be party to the relevant contract) the amount of any chargeable gain or allowable loss treated as accruing to the company on the assumption—

- (a) that it had made a disposal of the relevant contract immediately before the relevant time, and
- (b) that the disposal had been for a consideration equal to the notional carrying value of the relevant contract at that time.

(3) For the purposes of this paragraph an asset is a chargeable asset if any gain accruing on the disposal of the asset by the company would be a chargeable gain for the purposes of TCGA 1992 (and includes any obligations under futures contracts which, by virtue of section 143 of that Act, are regarded as assets to the disposal of which that Act applies).

(4) For the purposes of this paragraph “the relevant time” means the time, on or after 30th December 2006, at which the relevant contract becomes a derivative contract.

(5) For the purposes of this paragraph the “notional carrying value” of a contract at any time is the amount which would have been the carrying value of the contract in the accounts of the company if an accounting period had ended immediately before that time.

Contracts which cease to be derivative contracts

43B.—(1) This paragraph applies if a company is party to a relevant contract which (having been a derivative contract) ceases to be a derivative contract.

(2) The company is to be treated—

- (a) for the purposes of this Schedule, as if at the relevant time it had disposed of the contract in a related transaction for a consideration of an amount equal to the notional carrying value of the contract at that time, and

- (b) for the purposes of TCGA 1992, as if immediately after that time it had reacquired the contract for the same consideration.
- (3) In this paragraph “the relevant time” means the time at which the contract ceases to be a derivative contract.
- (4) Paragraph 43A(5) (meaning of “notional carrying value”) applies for the purposes of this paragraph.”.

Omission of paragraphs 44 and 45 of Schedule 26

- 11. Omit paragraphs 44 and 45.

Amendment of paragraph 45C of Schedule 26

- 12. In paragraph 45C(1) (derivative contracts relating to land or certain tangible movable property) omit sub-paragraphs (1)(d) and (1A).

Amendment of paragraph 45D of Schedule 26

- 13.—(1) Amend paragraph 45D(2) (creditor relationships: embedded derivatives which are options) as follows.
 - (2) In sub-paragraph (1) for paragraphs (a) to (c) substitute—
 - “(a) the derivative contract is a loan-contract embedded derivative to which the company is treated as party by virtue of a creditor relationship of the company (“the original relationship”),
 - (b) the derivative contract is treated as an option by virtue of section 94A(3) of the Finance Act 1996.”.
 - (3) In sub-paragraph (2)(a) for “creditor relationship” substitute “original relationship”.
 - (4) For sub-paragraph (2)(f) substitute—
 - “(f) the original asset is not an existing asset.”.
 - (5) In sub-paragraph (3)(a) for “creditor relationship” substitute “original relationship”.
 - (6) In sub-paragraph (3A) for “paragraph” substitute “Schedule and Chapter 2 of Part 4 of the Finance Act 1996”.
 - (7) In sub-paragraph (8) for “creditor relationship” substitute “original relationship”.

Amendment of paragraph 45E of Schedule 26

- 14. In paragraph 45E(3) (exclusions from paragraph 45D) omit sub-paragraph (2).

Amendment of paragraph 45F of Schedule 26

- 15.—(1) Amend paragraph 45F(4) (creditor relationships: embedded derivatives which are exactly tracking contracts for differences) as follows.
 - (2) In sub-paragraph (1) for paragraphs (a) to (c) substitute—

(1) Paragraph 45C was inserted by article 15 of [S.I. 2004/2201](#) and amended by article 8 of [S.I. 2005/3440](#).
(2) Paragraph 45D was inserted by article 15 of [S.I. 2004/2201](#) and amended by article 13 of [S.I. 2005/2082](#).
(3) Paragraph 45E was inserted by article 15 of [S.I. 2004/2201](#) and amended by article 14 of [S.I. 2005/2082](#).
(4) Paragraph 45F was inserted by article 15 of [S.I. 2004/2201](#) and amended by article 7 of [S.I. 2004/3270](#), by article 15 of [S.I. 2005/646](#) and by article 15 of [S.I. 2005/2082](#).

- “(a) the derivative contract is a loan-contract embedded derivative to which the company is treated as party by virtue of a creditor relationship of the company (“the original relationship”),
- (c) the derivative contract is treated as a contract for differences by virtue of section 94A(3) of the Finance Act 1996.”
- (3) In sub-paragraph (2)(a) for “creditor relationship” substitute “original relationship”.
- (4) In sub-paragraph (2)(c) omit sub-paragraph (i).
- (5) For sub-paragraph (2)(f) substitute—
 - “(f) the original asset is not an existing asset.”
- (6) In sub-paragraph (3)(a) for “creditor relationship” substitute “original relationship”.
- (7) In sub-paragraph (4), in the definition of “C”, for “the asset which represents the creditor relationship” substitute “the original asset”.
- (8) In sub-paragraph (6)—
 - (a) in paragraph (a)(i) for “the asset representing the creditor relationship” substitute “the original asset”
 - (b) in paragraph (a)(ii) for “corresponding debtor relationship” substitute “debtor relationship corresponding to the creditor relationship mentioned in sub-paragraph (1)”, and
 - (c) in paragraph (b) for “the asset representing the creditor relationship” substitute “the original asset”.
- (9) In sub-paragraph (8) for “creditor relationship” substitute “original relationship”.

Amendment of paragraph 45FA of Schedule 26

- 16.** For paragraph 45FA(5) (creditor relationships: existing assets) substitute—

“Creditor relationships: existing assets

45FA.—(1) This paragraph applies if paragraph 45D or 45F would apply to a derivative contract for an accounting period but for sub-paragraph (2)(f) of that paragraph.

(2) Paragraph 14(3) (non-trading debits and credits) shall not apply to the credits and debits given in relation to the contract for the accounting period by paragraph 15.

(3) The original creditor relationship by virtue of which paragraph 45D or 45F would apply to the derivative contract shall not be treated as a qualifying corporate bond by virtue of section 117(A1) of TCGA 1992.

(4) For the purposes of TCGA 1992 the amount or value of the consideration for any disposal of the original asset shall be treated as adjusted so as to exclude so much of it as, on a just and reasonable apportionment, relates to any interest which—

- (a) falls to be brought into account under Chapter 2 of Part 4 of the Finance Act 1996 (loan relationships) as accruing to any company at any time; and
 - (b) in consequence of, or of the terms of, the disposal, is not paid or payable to the company to which it is treated for the purposes of that Chapter as accruing.
- (5) Where—
- (a) there has been a reorganisation for the purposes of sections 126 to 132 of TCGA 1992, and

(b) for the purposes of those sections, the original asset mentioned in sub-paragraph (4) is treated as the original shares,

the reference in sub-paragraph (4) to the disposal of the original asset includes a reference to the disposal of the asset which, as a result of the reorganisation, has become the new holding for the purposes of those sections.

(6) For the purposes of TCGA 1992 the amount or value of the consideration for any disposal by a company of the original asset—

(a) shall be increased by the addition of any relevant exchange losses, and

(b) shall (after giving effect to any such increase) be reduced (but not below nil) by the deduction of any relevant exchange gains,

but this sub-paragraph does not apply in a case where paragraph 45F would apply but for sub-paragraph (2)(f) of that paragraph.

(7) For the purposes of sub-paragraph (6), “relevant exchange gains” and “relevant exchange losses” are—

(a) the amount of any exchange gains or losses in respect of the original asset that are brought into account under Chapter 2 of Part 4 of the Finance Act 1996 by the company for an accounting period throughout which the company holds the original asset; and

(b) for any accounting period not falling within paragraph (a) in which the company holds the original asset, an amount which, on a just and reasonable apportionment, represents so much of the amount of any exchange gains or losses brought into account under that Chapter in respect of the original asset, by the company making the disposal, for that period as is referable to the part of the period for which the company holds the asset.

(8) Where the amount of the relevant exchange gains falling to be deducted under sub-paragraph (6)(b) exceeds the amount required to reduce the amount or value of the consideration to nil, the excess shall be treated for the purposes of section 38(1)(c) of TCGA 1992 as incidental costs of making the disposal of the original asset.”.

Amendment of paragraph 45H of Schedule 26

17.—(1) Amend paragraph 45H(6) as follows.

(2) In sub-paragraph (2) for paragraph (a) substitute—

“(a) sub-paragraph (3) has effect in relation to a disposal of the asset representing the original creditor relationship mentioned in paragraph 45D(1)(a) (“the original relationship”), and”.

(3) In sub-paragraph (3) for “asset representing the associated creditor relationship” substitute “original asset”.

(4) After sub-paragraph (5) insert—

“(5A) Sections 37 and 39 of TCGA 1992 do not apply in relation to a disposal mentioned in sub-paragraph (1)(b), (2)(a) or (b) above.”

(5) In sub-paragraph (6), in the definition of “G”, for paragraph (a) substitute—

“(a) the relevant Chapter 2 amount, and”.

(6) In sub-paragraph (7) for paragraph (a) substitute—

- “(a) the “relevant Chapter 2 amount” means the amount by which the carrying value of the loan-contract host contract at the date on which the option is exercised exceeds the carrying value of that contract at—
- (i) the date on which the company became party to the original relationship, or
 - (ii) (if later) the date on which the derivative contract became one to which paragraph 45D applies;”.

Insertion of paragraph 45HZA of Schedule 26

18. After paragraph 45H insert—

“Treatment of net gains and losses on disposal of certain embedded derivatives

45HZA.—(1) This paragraph applies where—

- (a) a derivative contract is one to which paragraph 45F (creditor relationships: embedded derivatives which are exactly tracking contracts for differences) applies for an accounting period, and
- (b) the asset representing the original relationship mentioned in paragraph 45F(1)(a) is disposed of in the accounting period.

(2) For the purpose of computing any chargeable gain accruing to the company on the disposal, the sums allowable as a deduction under section 38(1)(a) of TCGA 1992 (acquisition costs) shall—

- (a) if G exceeds L, be increased by the amount of that excess,
- (b) if L exceeds G, be reduced by the amount of that excess.

(3) If the amount of the excess in sub-paragraph (2)(b) is greater than the amount of expenditure allowable under section 38(1)(a) of TCGA 1992, the amount of the excess that cannot be deducted from the expenditure so allowable shall, for the purpose mentioned in sub-paragraph (2), be added to the amount of the consideration for the disposal.

(4) Sections 37 and 39 of TCGA 1992 do not apply in relation to the disposal.

(5) In this paragraph—

G is the sum of—

- (a) the relevant Chapter 2 amount, and
- (b) the amount of any chargeable gains treated as accruing to the company under paragraph 45A(4)(a) in respect of the derivative contract in each relevant accounting period, and

L is the sum of the amounts of any allowable losses treated as accruing to the company under paragraph 45A(4)(b) in respect of the derivative contract in each relevant accounting period.

(6) For the purposes of paragraph (5)—

- (a) the relevant Chapter 2 amount means the amount by which the carrying value of the loan-contract host contract at the date of the disposal exceeds the carrying value of that contract at the date on which the company became party to the original relationship;
- (b) a relevant accounting period is—
 - (i) the accounting period in which the disposal is made, or
 - (ii) any previous accounting period.”.

Amendment of paragraph 45HA of Schedule 26

19.—(1) Amend paragraph 45HA (7) as follows.

(2) For sub-paragraph (1) and the heading preceding paragraph 45HA substitute—

“Treatment of credits and debits on terminal exercise of non-embedded option or running to delivery of future

45HA.—(1) This paragraph applies where—

- (a) a company is party to a derivative contract in an accounting period,
- (b) the derivative contract is a plain vanilla contract which is an option,
- (c) rights comprised in the plain vanilla contract are exercised to any extent in that accounting period, and
- (d) those rights are rights to acquire shares.

(1A) This paragraph also applies where—

- (a) a company is party to a derivative contract in an accounting period,
- (b) the derivative contract is a plain vanilla contract which is a future,
- (c) delivery is taken of an asset in accordance with the terms of the future, and
- (d) that asset is shares.”.

(3) In sub-paragraph (2)—

- (a) for “In any such case” substitute “Where this paragraph applies”, and
- (b) for “so acquired” substitute “acquired or delivered”.

(4) In sub-paragraph (4), in the definition of “G”, for “sub-paragraph (1)(b)” substitute “sub-paragraph (1)(c) or the delivery mentioned in sub-paragraph (1A)(c)”.

Amendment of paragraph 45I of Schedule 26

20.—(1) Amend paragraph 45I(8) (index-linked gilt-edged securities with embedded contracts for differences) as follows.

(2) In sub-paragraph (1) for paragraph (a) substitute—

- “(a) the derivative contract is a loan-contract embedded derivative to which the company is treated as party by virtue of a creditor relationship of the company,”.

(3) In sub-paragraph (1)(c) for “equivalent deemed loan relationship” substitute “loan-contract host contract”.

(4) In sub-paragraph (1) omit paragraph (d).

(5) In sub-paragraph (1)(e) for the words from the beginning to “that section” substitute “the derivative contract is treated by virtue of section 94A(3) of the Finance Act 1996”.

(6) In sub-paragraph (3) omit the definition of “the equivalent deemed loan relationship”.

Amendment of paragraph 45J of Schedule 26

21.—(1) Amend paragraph 45J(9) (issuers of securities with embedded derivatives: deemed options) as follows.

(7) Paragraph 45HA was inserted by article 17 of [S.I. 2005/2082](#) and amended by article 10 of [S.I. 2005/3440](#).

(8) Paragraph 45I was inserted by article 15 of [S.I. 2004/2201](#).

(9) Paragraph 45J was inserted by article 10 of [S.I. 2004/3270](#) and amended by article 16 of [S.I. 2005/646](#), article 18 of [S.I. 2005/2082](#) and article 11 of [S.I. 2005/3440](#).

(2) In sub-paragraph (1) for paragraphs (a) and (b) substitute—

“(a) the derivative contract is a loan-contract embedded derivative to which the company is treated as party by virtue of a debtor relationship of the company (“the original relationship”),”.

(3) In sub-paragraph (1)(c) for the words from the beginning to “that section” substitute “the derivative contract is treated by virtue of section 94A(3) of the Finance Act 1996”.

(4) In sub-paragraph (2)(a), in both places, and in sub-paragraph (4) for “debtor” substitute “original”.

(5) In sub-paragraph (3)(b) for “(9)” substitute “(9A)”.

(6) For sub-paragraphs (8) and (9) substitute—

“(8) In sub-paragraph (7)—

E is—

- (a) in a case where the company was a party to the original relationship at the time it was created, the initial carrying value of the option, and
- (b) in a case where the company became a party to the original relationship at a later time, the carrying value of the option at that time;

F is the amount paid by the debtor in fulfilment of the obligations under the original relationship reduced (but not below nil) by the fair value of the loan-contract host contract at the date on which the option is exercised.

(9) Sub-paragraph (9A) applies if the company ceases to be a party to the original relationship at a time when the option mentioned in sub-paragraph (1)(c) has not been exercised.

(9A) The company is treated for the purposes of corporation tax on chargeable gains—

- (a) as having disposed of an asset for a consideration equal to G, and
- (b) as having acquired that asset for a consideration equal to H.

(9B) In sub-paragraph (9A)—

G is—

- (a) in a case where the company was a party to the original relationship at the time it was created, the initial carrying value of the option, and
- (b) in a case where the company became a party to the original relationship at a later time, the carrying value of the option at that time;

H is—

- (a) in a case where the company ceases to be a party to the original relationship as a result of the redemption or repayment of the liability representing the original relationship, the amount paid by the company, and
- (b) in any other case, the consideration given by the company on its ceasing to be party to the original relationship,

in either case reduced (but not below nil) by the fair value of the loan-contract host contract at the date on which it so ceases.”.

Amendment of paragraph 45JA of Schedule 26

22.—(1) Amend paragraph 45JA(10) (issuers of securities with embedded derivatives: equity instruments) as follows.

(10) Paragraph 45JA was inserted by paragraph 19 of [S.I. 2005/2082](#).

- (2) In sub-paragraph (1)—
 - (a) for paragraph (a) substitute—
 - “(a) the company is party to a loan-contract embedded derivative by virtue of a debtor relationship of the company (“the original relationship”),
 - (b) in paragraph (b) for “subsection (1) of that section in the case of that debtor relationship” substitute “section 94A(1) of the Finance Act 1996 in the case of the original relationship”, and
 - (c) in paragraph (b)(ii), at the end, insert “of the company”.
- (3) Omit sub-paragraph (1)(e).
- (4) In sub-paragraph (1)(f) for “loan” substitute “original”.
- (5) In sub-paragraphs (2)(a), in both places, and (2)(b) for “debtor” substitute “original”.
- (6) In sub-paragraph (4) for the definition of “RA” substitute—
 - “RA is the amount paid as mentioned in sub-paragraph (1)(f) reduced (but not below nil) by an amount equal to the fair value of the loan-contract host contract at the time that amount is paid;”.
- (7) In sub-paragraph (4), in the definition of “E”, for “debtor” substitute “original”.

Amendment of paragraph 45K of Schedule 26

23.—(1) Amend paragraph 45K(11) (issuers of securities with embedded derivatives: deemed contracts for differences) as follows.

- (2) In sub-paragraph (1)—
 - (a) For paragraphs (a) and (b) substitute—
 - “(a) the derivative contract is a loan-contract embedded derivative to which the company is treated as party by virtue of a debtor relationship of the company (“the original relationship”),”.
- (3) For sub-paragraph (1)(d) substitute—
 - “(d) the derivative contract is an exactly tracking contract within the meaning of sub-paragraph (2A), and”.
- (4) In sub-paragraphs (2)(a), in both places, and (2)(e) for “debtor” substitute “original”.
- (5) In sub-paragraph (2)(c) omit “land (wherever situated) or”.
- (6) After sub-paragraph (2) insert—
 - “(2A) For the purposes of this paragraph “an exactly tracking contract” is a contract for differences where D is equal to the amount determined by applying R% to C where—
 - D is the amount that must be paid to discharge the rights and liabilities that fall to be treated as comprised in the contract;
 - R% is a relevant percentage change in the value of the underlying subject matter of the contract (see sub-paragraph (2B));
 - C is the amount falling for the purposes of Chapter 2 of Part 4 of the Finance Act 1996 to be regarded in accordance with generally accepted accounting practice as the proceeds of issue of the liability which represents the original relationship.

(11) Paragraph 45K was inserted by article 10 of [S.I. 2004/3270](#) and amended by article 17 of [S.I. 2005/646](#) and article 20 of [S.I. 2005/2082](#).

(2B) In sub-paragraph (2A), the reference to a relevant percentage change in the value of the underlying subject matter of the contract is a reference to the percentage change (if any) over the relevant period in—

- (a) the value of the assets which are the underlying subject matter of the contract, or
- (b) any index of the value of those assets.

(2C) In sub-paragraph (2B) “the relevant period” means—

- (a) the period between—
 - (i) the date when the liability representing the original relationship came into existence, and
 - (ii) the date when the corresponding creditor relationship comes to an end; or
- (b) any other period in which almost all of that period is comprised, and which differs from that period exclusively for purposes connected with giving effect to a valuation in relation to rights or liabilities under the liability representing the original relationship.”.

(7) In sub-paragraphs (3A)(a) and (3B)(b) for “debtor” substitute “original”.

(8) In sub-paragraph (3B) for paragraph (c) substitute—

- “(c) the consideration for the disposal of that asset—
 - (i) in a case where the company was party to the original relationship at the time it was created, is equal to the amount of the proceeds of issue of the security representing that relationship, and
 - (ii) in a case where the company became party to the original relationship after that time, is equal to the amount of the carrying value of the loan-contract host contract at that time, and”.

Insertion of paragraph 45KA of Schedule 26

24. After paragraph 45K insert—

“Securities with embedded options: existing liabilities

45KA.—(1) Where in any accounting period paragraph 45K would apply to a derivative contract but for sub-paragraph (2)(e) of that paragraph, paragraph 14(3) (non-trading credits and debits) shall not apply to the relevant credits and debits.

(2) For the purposes of this paragraph the relevant credits and debits are the credits and debits given in relation to the contract for the accounting period by paragraph 15.”.

Amendment of paragraph 45L of Schedule 26

25.—(1) Amend paragraph 45L(12) (derivatives not embedded in a loan relationship) as follows.

(2) In sub-paragraph (1) for the words from the beginning to the end of paragraph (a) substitute—

- “(1) This paragraph applies where—
 - (a) a company is party to a non-financial embedded derivative or a nested derivative (“the contract”),”.

(3) For sub-paragraph (1A) substitute—

- “(1A) In this paragraph “the original contract” means—

(12) Paragraph 45L was inserted by article 10 of [S.I. 2004/3270](#) and amended by article 21 of [S.I. 2005/2082](#) and article 12 of [S.I. 2005/3440](#).

- (a) the non-financial contract mentioned in paragraph 2A to which the company is party, and as a result of which the company falls to be treated under paragraph 2A(2) as party to the non-financial embedded derivative; or
- (b) the hybrid derivative mentioned in paragraph 2B to which the company is party, and as a result of which the company falls to be treated under paragraph 2B(2) as party to the nested derivative.”.

(4) In sub-paragraph (1B)(b) for the words from “whether” to the end substitute “whether that contract is a hybrid derivative or a non-financial contract”.

(5) In sub-paragraph (1C)—

- (a) for “a derivative contract” substitute “a hybrid derivative”, and
- (b) for paragraph (a) substitute—

“(a) were not one where the rights and liabilities are treated for accounting purposes as divided as mentioned in sub-paragraph (2) of paragraph 2B, and”.

(6) In sub-paragraph (2)—

- (a) for the words from the beginning to “a derivative contract” substitute “If the contract is a non-financial contract”,
- (b) for paragraph (a) substitute—

“(a) were not one where the rights and liabilities are treated for accounting purposes as divided as mentioned in sub-paragraph (2) of paragraph 2A, and”, and

(c) insert the following words after paragraph (b) (but not as part of that paragraph)—

“and, accordingly, this Schedule shall not apply to the contract, but section 42 of the Finance Act 1998 shall apply to the contract as if fair value accounting were not generally accepted accounting practice in relation to the company.”.

Amendment of paragraph 45LA of Schedule 26

26. In paragraph 45LA(13) (elections under paragraph 45L(2A): further provisions) in sub-paragraph (4)(a) for “paragraph 2(4)” substitute “paragraph 2A or 2B”.

Amendment of paragraph 45M of Schedule 26

27.—(1) Amend paragraph 45M(14) (treatment of host contract as a loan relationship) as follows.

(2) For sub-paragraphs (1) and (2) substitute—

“(1) This paragraph applies where for an accounting period—

- (a) a company is party to a hybrid derivative contract falling within paragraph 3(1)(b),
- (b) the nested derivative is a derivative contract falling within paragraph 3(1)(a),
- (c) the underlying subject matter of the derivative contract consists, or is treated as consisting, wholly of—
 - (i) shares in a company, or
 - (ii) rights of a unit holder under a unit trust scheme, and
- (d) the quasi-derivative host contract is treated for accounting purposes as, or as forming part of, a financial asset.

(13) Paragraph 45LA was inserted by article 13 of [S.I. 2005/3440](#).

(14) Paragraph 45M was inserted by article 18 of [S.I. 2005/646](#) and amended by article 22 of [S.I. 2005/2082](#) and article 14 of [S.I. 2005/3440](#).

- (2) Where this paragraph applies—
 - (a) the quasi-derivative host contract shall be treated for the purposes of the Corporation Tax Acts as if it were a creditor relationship of the company, and
 - (b) the nested derivative shall be treated—
 - (i) as satisfying the conditions in paragraph 4(2A), and
 - (ii) as a chargeable asset (within the meaning of paragraph 4A(4)).”
- (3) Omit sub-paragraphs (5) and (6).

Amendment of paragraph 50A of Schedule 26

28. In paragraph 50A(15) (adjustment on company changing to international accounting standards), in sub-paragraph (3B)(b), for “paragraphs 21 and 28” substitute “paragraph 28”.

(15) Paragraph 50A was inserted by paragraph 67 of Schedule 10 to the Finance Act 2004 (c. 12). Sub-paragraphs (3A) and (3B) were inserted by article 12 of S.I. 2004/3270.