



Finance Act 2002

2002 CHAPTER 23

PART 3

INCOME TAX, CORPORATION TAX AND CAPITAL GAINS TAX

CHAPTER 2

OTHER PROVISIONS

Loan relationships

71 Accounting method where rate of interest etc is reset

(1) After section 88 of the Finance Act 1996 (c. 8) insert—

“88A Accounting method where rate of interest is reset

- (1) This section applies where—
- (a) the conditions in subsections (2) and (3) below are satisfied in relation to an asset representing a creditor relationship of a company; and
 - (b) the object, or one of the main objects, of the company entering into or becoming a party to the creditor relationship was the securing, whether for itself or any other person, of a tax advantage (within the meaning of Chapter 1 of Part 17 of the Taxes Act 1988).
- (2) The first condition is that there is or has at any time been a change in—
- (a) the rate of interest payable in the case of the asset;
 - (b) the amount payable to discharge the debt; or
 - (c) the time at which any payments under the asset (whether of interest or otherwise) fall due.
- (3) The second condition is that the difference between—

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Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships. (See end of Document for details)

- (a) the fair value of the asset immediately after the change, and
 - (b) the issue price of the asset,
- is equal to at least 5 per cent of the issue price of the asset.
- (4) On and after the day on which the conditions in subsections (2) and (3) above become satisfied in the case of an asset, the only accounting method authorised for the purposes of this Chapter for use by any company as respects a creditor relationship represented by the asset shall be an authorised mark to market basis of accounting.
 - (5) Where section 90 below applies in consequence of subsection (4) above, no debit shall be brought into account under subsection (2)(c) or (3)(b) of that section.
 - (6) In determining the fair value of an asset for any purpose of this section it shall be assumed that all amounts payable by the debtor will be paid in full as they fall due.”.
- (2) This section has effect on and after the relevant day.
 - (3) Where an authorised mark to market basis of accounting—
 - (a) is required by virtue of this section to be used on and after the relevant day as respects a creditor relationship of a company, but
 - (b) was not being used immediately before that day as respects the relationship, the asset representing the relationship shall be treated for the purposes of Chapter 2 of Part 4 of the Finance Act 1996 as having been acquired by the company for the asset’s fair value (as determined for the purposes of section 88A of that Act) on the relevant day.
 - (4) For the purposes of this section “the relevant day” is—
 - (a) 19th December 2001, in a case where section 88A of that Act applies by reason of a change in the rate of interest payable in the case of the asset in question; or
 - (b) 24th April 2002, in any other case.

72 Convertible securities etc: loan relationships

- (1) Section 92 of the Finance Act 1996 (c. 8) (convertible securities etc) is amended as follows.
- (2) Amend subsection (1) (the assets to which section 92 applies) in accordance with subsections (3) to (9).
- (3) In paragraph (b) (which requires the asset to carry rights to acquire any shares in a company) for “any shares in a company” substitute “ shares in a company ”.
- (4) After paragraph (b) insert—
 - “(bb) the only shares that may be so acquired under any such provision are shares which, at the time when the asset comes or came into existence are or were, and at all times since have been,—
 - (i) qualifying ordinary shares in one or more companies, or
 - (ii) mandatorily convertible preference shares in one or more companies;”.

Status: Point in time view as at 24/07/2002.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships. (See end of Document for details)

- (5) In paragraph (c) (extent to which shares may be acquired under that provision not to be determined using specified cash value) for “that provision”, where first occurring, substitute “ any such provision ”.
- (6) In paragraph (d) (asset not to be a relevant discounted security within the meaning of Schedule 13 to the Finance Act 1996) after “Act” insert “ or an excluded indexed security within the meaning of that Schedule ”.
- (7) After paragraph (d) insert—
- “(dd) the rights attached to the asset do not include provision by virtue of which the company may require a person other than the issuing company to acquire the asset for an amount which would, if payable on redemption, be an amount involving a deep gain for the purposes of paragraph 3 of that Schedule;”.
- (8) In paragraph (e)(more than negligible likelihood of the right to acquire shares being exercised to significant extent)—
- (a) for “the right” substitute “ the rights ”, and
- (b) omit “and”.
- (9) After paragraph (e) insert—
- “(ee) the rights to acquire shares in a company (whether by conversion or exchange or otherwise) are such that exercising them to their full extent would result in the replacement of the asset—
- (i) wholly by shares, or
- (ii) in a case where exercising the rights to acquire shares to their full extent would not confer an entitlement to a whole number of shares, wholly by shares and a cash adjustment in respect of the fraction of a share so arising,
- and the ending of the creditor relationship; and”.
- (10) After subsection (1) insert—
- “(1A) In subsection (1) above—
- “the issuing company” means the company that brought into existence the asset mentioned in subsection (1) above;
- “mandatorily convertible preference shares” means shares (other than qualifying ordinary shares) which are issued upon terms that stipulate that, by a time no more than 24 hours after their acquisition by a person who immediately before that acquisition had the creditor relationship represented by those shares, they must be converted into or exchanged for qualifying ordinary shares;
- “qualifying ordinary shares” means shares in a company which satisfy the conditions in subsections (1B) and (1C) below.
- (1B) The first condition is that the shares are shares representing some or all of the issued share capital (by whatever name called) of the company, other than—
- (a) capital the holders of which have a right to a dividend at a fixed rate but have no other right to share in the profits of the company, or
- (b) capital the holders of which have no right to a dividend of any description nor any other right to share in the profits of the company.
- (1C) The second condition is that the shares are—

Status: Point in time view as at 24/07/2002.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships. (See end of Document for details)

- (a) shares which are listed on a recognised stock exchange, or
- (b) shares in a company which is a trading company or a holding company;

and for this purpose “trading company” and “holding company” have the meaning given by paragraph 22(1) of Schedule A1 to the Taxation of Chargeable Gains Act 1992.”.

(11) After subsection (1C) insert—

“(1D) For the purposes of subsection (1)(ee)(ii) above, the amount which may be paid by way of a cash adjustment may not exceed five per cent of the value of the relevant shares at the relevant time; and for these purposes—

- (a) “the relevant shares” means the shares which would be acquired by exercising the rights attached to the asset to their full extent, and
- (b) “the relevant time” means the time at which the rights to acquire those shares are exercised.”.

(12) In consequence of the amendments made by this section and sections 73 and 74, the sidenote becomes “Convertible securities etc: creditor relationships”.

(13) The amendments made by this section do not have effect for the purpose of determining, in relation to such part of an accounting period as falls before 26th July 2001, whether an asset is, or has ceased to be, an asset to which section 92 of the Finance Act 1996 (c. 8) applies.

(14) Subsection (15) has effect where—

- (a) an asset is, immediately before 26th July 2001, an asset to which section 92 of the Finance Act 1996 applies, but
- (b) on that date, by virtue only of the amendments of that section made by this section, the asset ceases to be an asset to which that section applies.

(15) Where this subsection has effect, the asset shall be taken to have ceased immediately before 26th July 2001 to be an asset to which section 92 of the Finance Act 1996 (c. 8) applies and, accordingly, any deemed disposal and re-acquisition under subsection (7) of that section shall be treated as having taken place immediately before that date.

(16) Subject to subsections (13) to (15), the amendments made by this section have effect for accounting periods ending on or after 26th July 2001 in relation to any asset representing a creditor relationship of a company, unless the creditor relationship in question is one to which the company ceased to be a party before that date.

73 Convertible securities etc: issuing company not to be connected company

(1) In section 92 of the Finance Act 1996 (convertible securities etc) after subsection (1D) (which is inserted by section 72) insert—

“(1E) This section does not apply to an asset representing a creditor relationship of a company if, for the accounting period in which the asset comes into existence, there is a connection between the company and the company which is the issuing company in relation to that asset.

(1F) If, in the case of an asset representing a creditor relationship of a company, the company and the company which is the issuing company in relation to that

Status: Point in time view as at 24/07/2002.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships. (See end of Document for details)

asset become companies between which, for any accounting period, there is a connection—

- (a) the asset shall cease to be an asset to which this section applies, and
- (b) it shall be treated, for the purposes of subsection (7)(a) below, as having ceased to be such an asset at the time when the circumstances giving rise to that connection arose.

(1G) Section 87(3) above (connection between a company and another person for an accounting period) applies for the purposes of subsections (1E) and (1F) above.”.

- (2) The amendments made by this section do not have effect for the purpose of determining, in relation to such part of an accounting period as falls before 19th December 2001, whether an asset is, or has ceased to be, an asset to which section 92 of the Finance Act 1996 applies.
- (3) Subsection (4) has effect where—
 - (a) an asset is, immediately before 19th December 2001, an asset to which section 92 of the Finance Act 1996 applies, but
 - (b) on that date, by virtue only of the amendments of that section made by this section, the asset ceases to be an asset to which that section applies.
- (4) Where this subsection has effect, the asset shall be taken to have ceased immediately before 19th December 2001 to be an asset to which section 92 of the Finance Act 1996 applies and, accordingly, any deemed disposal and re-acquisition under subsection (7) of that section shall be treated as having taken place immediately before that date.
- (5) Subject to subsections (2) to (4), the amendments made by this section have effect for accounting periods ending on or after 19th December 2001 in relation to any asset representing a creditor relationship of a company—
 - (a) unless the creditor relationship in question is one to which the company ceased to be a party before that date, or
 - (b) unless, as regards the company holding the asset representing the creditor relationship immediately before 19th December 2001 (“the creditor company”) and the company which brought that asset into existence (“the issuing company”), the first or the second condition is satisfied.
- (6) The first condition is that, during any period before 19th December 2001 when the creditor company was holding the asset, there was an accounting period in which there was no connection between the creditor company and the issuing company.
- (7) The second condition is that immediately before 19th December 2001—
 - (a) the creditor company was not a 100 per cent subsidiary of the issuing company,
 - (b) the issuing company was not a 100 per cent subsidiary of the creditor company, and
 - (c) the creditor company and the issuing company were not 100 per cent subsidiaries of the same company.
- (8) Section 87(3) of the Finance Act 1996 (c. 8) (connection between a company and another person for an accounting period) applies for the purposes of subsection (6).

Status: Point in time view as at 24/07/2002.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships. (See end of Document for details)

- (9) In its application for the purposes of subsection (7), section 838 of the Taxes Act 1988 (meaning of “subsidiaries” for the purposes of the Tax Acts) has effect as if in subsection (1)(b) of that section—
- (a) “a 100 per cent subsidiary” were substituted for “ a 75 per cent subsidiary ”, and
 - (b) “not less than 100 per cent” were substituted for “ not less than 75 per cent ”.

74 **Convertible securities etc: debtor relationships**

- (1) After section 92 of the Finance Act 1996 insert—

“92A Convertible securities etc: debtor relationships

- (1) This section applies to a liability if—
- (a) the liability represents a debtor relationship of a company (“the debtor company”); and
 - (b) the rights attached to the asset that represents the corresponding creditor relationship include provision by virtue of which a person is or may become entitled to acquire (whether by conversion or exchange or otherwise)—
 - (i) any shares in the debtor company, or
 - (ii) any shares in another company.
- (2) The debits falling for any accounting period to be brought into account for the purposes of this Chapter in respect of a debtor relationship represented by a liability to which this section applies shall not include debits in relation to any of the amounts falling within subsection (3) below.
- (3) The amounts are—
- (a) any amounts payable by the debtor company in respect of, or in connection with, any such acquisition of shares as is described in subsection (1)(b)(ii) above, but not any amounts to which subsection (4) below applies; and
 - (b) any charges or expenses incurred by the debtor company as described in paragraph (b), (c) or (d) of section 84(3) above, where the related transaction in question relates to, or is connected with, the acquisition of shares by another person (whether by conversion or exchange or otherwise) as described in subsection (1)(b) above.
- (4) This subsection applies to amounts payable by the debtor company, as described in subsection (3)(a) above, in respect of the debtor relationship in a case where—
- (a) the debtor company is carrying on a banking business or a business consisting wholly or partly in dealing in securities, and
 - (b) it entered into the debtor relationship in the ordinary course of that business.
- (5) For the purposes of subsection (4) above “securities” has the same meaning as in section 473 of the Taxes Act.

Status: Point in time view as at 24/07/2002.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships. (See end of Document for details)

- (6) Subject to subsection (7) below, only an authorised accruals basis of accounting shall be used for ascertaining the amounts which fall to be taken into account as described in subsection (2) above.
- (7) The requirement in subsection (6) above to use an authorised accruals basis of accounting does not apply in the case of a debtor relationship where—
 - (a) the debtor company is carrying on a banking business or a business consisting wholly or partly in dealing in securities, and
 - (b) it entered into the debtor relationship in the ordinary course of that business.”.
- (2) The amendments made by this section have effect—
 - (a) in relation to any amounts falling within section 92A(3)(a), where those amounts fall to be paid after 25th July 2001, and
 - (b) in relation to any charges or expenses falling within section 92A(3)(b), where those charges or expenses accrue after 25th July 2001.

75 Asset-linked loan relationships

- (1) Section 93 of the Finance Act 1996 (c. 8) (relationships linked to the value of chargeable assets) is amended as follows.
- (2) In subsection (1) (application of section and exclusion of cases where dealing in loan relationships is part of a trade)—
 - (a) for “unless it is one” substitute “unless—
 - (a) in a case where the loan relationship is a creditor relationship, the asset representing the loan relationship is one”; and
 - (b) at the end of that subsection insert—
 - “(b) in a case where the loan relationship is a debtor relationship, the liability representing the loan relationship is a liability entered into by the company in the course of activities forming an integral part of a trade carried on by the company; or
 - (c) the loan relationship is one to which section 93A below applies.”.
- (3) In subsection (10) (meaning of chargeable asset) for the words from “if” to the end substitute—

“the asset is—

 - (a) an estate or interest in land (wherever situated), or
 - (b) qualifying ordinary shares which are listed on a recognised stock exchange.”.
- (4) Subsection (11)(assumptions applying to determine if disposal is chargeable gain for the purposes of subsection (10)) shall cease to have effect.
- (5) After subsection (12) insert—

“(12A) In subsection (10)(b) above “qualifying ordinary shares”, in relation to a company, means shares representing some or all of the issued share capital (by whatever name called) of the company, other than—

Status: Point in time view as at 24/07/2002.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships. (See end of Document for details)

- (a) capital the holders of which have a right to a dividend at a fixed rate but have no other right to share in the profits of the company, or
 - (b) capital the holders of which have no right to a dividend of any description nor any other right to share in the profits of the company.”.
- (6) Subsection (13)(which makes provision in respect of certain indices which, in consequence of the amendment made by subsection (3) above, cannot be indices of chargeable assets) shall cease to have effect.
- (7) At the end of the section add—
- “(14) This section is supplemented by section 93B below.”.
- (8) The amendments made by this section do not have effect for the purpose of determining, in relation to such part of an accounting period as falls before 26th July 2001, whether a loan relationship is, or has ceased to be, a loan relationship to which section 93 of the Finance Act 1996 (c. 8) applies.
- (9) Subject to subsection (8), the amendments made by this section have effect for accounting periods ending on or after 26th July 2001 in relation to any loan relationship of a company, unless the loan relationship in question is one to which the company ceased to be a party before that date.

76 **Asset-linked loan relationships involving guaranteed returns**

- (1) After section 93 of the Finance Act 1996 insert—

“93A Relationships linked to the value of chargeable assets: guaranteed returns

- (1) This section applies to a loan relationship which is a creditor relationship of a company if—
- (a) that loan relationship and one or more other transactions are associated transactions designed to produce a guaranteed return;
 - (b) any such other transaction is a disposal of futures or options; and
 - (c) the guaranteed return comprises the return consisting of the amount that must be paid to discharge the money debt arising in connection with that loan relationship taken together with the return from any one or more of the disposals of futures or options.
- (2) For the purposes of this section a loan relationship of a company and one or more disposals of futures or options are transactions designed to produce a guaranteed return if, taking the transactions together, it would be reasonable to assume, from considering—
- (a) the likely effect of the transactions,
 - (b) the circumstances in which the transactions are entered into, or in which any of them is entered into, or
 - (c) the matters in both of paragraphs (a) and (b),
- that the main purpose of the transactions, or one of their main purposes, is or was the production of a guaranteed return from the loan relationship and any one or more of the disposals.

Status: Point in time view as at 24/07/2002.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships. (See end of Document for details)

- (3) For the purposes of this section a guaranteed return is produced from the loan relationship and any one or more of the disposals of futures or options wherever (taking all the transactions together) risks from fluctuations in the underlying subject matter are so eliminated or reduced as to produce a return from the transactions—
- (a) the amount of which is not, to any significant extent, attributable (otherwise than incidentally) to any such fluctuations; and
 - (b) which equates, in substance, to the return on an investment of money at interest.
- (4) For the purposes of subsection (3) above the cases where risks from fluctuations in the underlying subject matter are eliminated or reduced shall be deemed to include any case where the main reason, or one of the main reasons, for the choice of that subject matter is—
- (a) that there appears to be no risk that that subject matter will fluctuate; or
 - (b) that the risk that it will fluctuate appears to be insignificant.
- (5) In this section—
- (a) the references, in relation to a loan relationship, to the underlying subject matter are references to the value of chargeable assets of a particular description to which that relationship is linked;
 - (b) the references, in relation to a disposal of futures or options, to the underlying subject matter are references to or to the value of the commodities, currencies, shares, stock or securities, interest rates, indices or other matters to which, or to the value of which, those futures or options are referable.
- (6) Subsection (5)(a) above is to be construed in accordance with section 93 above.
- (7) For the purposes of this section—
- (a) references to the disposal of futures or options are to be construed in accordance with paragraphs 4 and 4A of Schedule 5AA to the Taxes Act 1988;
 - (b) references to the return from one or more disposals of futures or options are to be construed in accordance with paragraph 5 of that Schedule; and
 - (c) references to associated transactions are to be construed in accordance with paragraph 6 of that Schedule.”.
- (2) The amendment made by this section has effect for accounting periods ending on or after 26th July 2001 in relation to any loan relationship of a company, unless the loan relationship in question is one to which the company ceased to be a party before that date.

77 Loan relationships ceasing to be within section 93 of the Finance Act 1996

- (1) After section 93A of the Finance Act 1996 (c. 8) (which is inserted by section 76) insert—

Status: Point in time view as at 24/07/2002.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships. (See end of Document for details)

“93B Loan relationships ceasing to be within section 93

- (1) Where a loan relationship of a company—
 - (a) ceases at any time to be a loan relationship to which section 93 above applies, but
 - (b) does not cease at that time to be a loan relationship of that company, subsection (2) below shall have effect in relation to the asset representing that relationship.
- (2) Where this subsection has effect in relation to an asset representing a loan relationship of a company, the company shall be deemed for the purposes of the Taxation of Chargeable Gains Act 1992 and this Chapter—
 - (a) to have disposed of the asset for the relevant consideration immediately before the time when the loan relationship ceases to be one to which section 93 above applies, and
 - (b) to have re-acquired it for the relevant consideration immediately after that time.
- (3) Any deemed disposal and re-acquisition of an asset under subsection (2) above shall be treated for the purposes of the Taxation of Chargeable Gains Act 1992 as a transaction in the case of which—
 - (a) sections 127 to 130 of that Act would apply, apart from the provisions of section 116 of that Act, by virtue of any provision of Chapter 2 of Part 4 of that Act;
 - (b) the asset in question represents both the original shares and the new holding for the purposes of those sections;
 - (c) the market value of the asset at the time of the transaction is an amount equal to the relevant consideration.
- (4) Subject to subsection (5) below, in subsections (2) and (3) above “the relevant consideration”, in relation to an asset, means the amount that would have been taken, in accordance with the relevant accounting method, to be the value of the asset at the time of its deemed disposal if that method had been applied to the asset for tax purposes at all times until then.
- (5) Section 93(5) above shall not apply in the case of a deemed disposal and re-acquisition under subsection (2) above; but the amount of the relevant consideration in such a case shall be treated for the purposes of the Taxation of Chargeable Gains Act 1992 as reduced by so much (if any) of the amount mentioned in subsection (4) above as is referable to interest which—
 - (a) is not paid or payable to the company before the time of the deemed disposal; but
 - (b) is interest falling to be brought into account under section 93(2) and (3) above as having accrued before that time.
- (6) In subsection (4) above “the relevant accounting method”, in relation to an asset representing a loan relationship of a company, means the accounting method which, for the accounting period of that company in which the deemed re-acquisition takes place, is used as respects that asset and the part of that accounting period beginning with the deemed re-acquisition.
- (7) This section shall be construed as one with section 93 above.”.

Status: Point in time view as at 24/07/2002.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships. (See end of Document for details)

- (2) The amendment made by this section does not have effect in relation to a loan relationship which, before 26th July 2001, ceased to be a loan relationship to which section 93 of the Finance Act 1996 (c. 8) (as it has effect by virtue of section 75(8) above) applies.
- (3) Subject to subsection (2), the amendment made by this section has effect for accounting periods ending on or after 26th July 2001 in relation to any loan relationship of a company, unless the loan relationship in question is one to which the company ceased to be a party before that date.

78 Guaranteed returns on transactions involving futures and options

- (1) Schedule 5AA to the Taxes Act 1988 (guaranteed returns on transactions in futures and options) is amended as follows.
- (2) In paragraph 2 (transactions to which Schedule applies) at the end insert—
 - “(3) This Schedule also applies to a transaction if it is one of the disposals of futures or options to which section 93A of the Finance Act 1996 (loan relationships linked to the value of chargeable assets designed to produce guaranteed returns when taken together with disposals of options and futures) refers.”.
- (3) In paragraph 4 (meaning of disposals of futures or options) after sub-paragraph (4) insert—
 - “(4A) Where this paragraph has effect in relation to one of the associated transactions to which section 93A of the Finance Act 1996 refers, sub-paragraph (4) shall have effect as if for paragraph (a) of that sub-paragraph there were substituted—
 - “(“ any one of the associated transactions to which section 93A of the Finance Act 1996 refers is the grant of an option, ”.”.
- (4) In paragraph 4A (futures running to delivery and options exercised) after sub-paragraph (10) insert—
 - “(10A) Where this paragraph has effect in relation to one of the associated transactions to which section 93A of the Finance Act 1996 refers—
 - (a) sub-paragraph (1)(a) shall have effect as if for “two or more related transactions” there were substituted “two or more of the associated transactions to which section 93A of the Finance Act 1996 refers”, and
 - (b) sub-paragraph (1)(c) shall have effect as if for “the other transaction, or one of the other transactions,” there were substituted “one of the other transactions”.”.
- (5) In paragraph 6 (meaning of related transactions) after sub-paragraph (3) insert—
 - “(3A) Where this paragraph has effect in relation to one of the associated transactions to which section 93A of the Finance Act 1996 refers—
 - (a) sub-paragraph (1) shall have effect as if for “two or more transactions are related” there were substituted “two or more transactions are associated transactions to which section 93A of the Finance Act 1996 refers“, and

Status: Point in time view as at 24/07/2002.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships. (See end of Document for details)

- (b) sub-paragraph (2) shall have effect as if for “related transactions” there were substituted “associated transactions to which that section refers”.
- (6) This section has effect for accounting periods ending on or after 26th July 2001 in relation to profits and gains realised, and losses sustained, on or after that date.

Status:

Point in time view as at 24/07/2002.

Changes to legislation:

There are currently no known outstanding effects for the Finance Act 2002, Cross Heading: Loan relationships.