

Status: Point in time view as at 23/01/2003.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Part 4. (See end of Document for details)

SCHEDULES

SCHEDULE 26 **U.K.**

DERIVATIVE CONTRACTS

Modifications etc. (not altering text)

- C1** Sch. 26 modified by 1996 c. 8, s. 86(3C) (as inserted (24.7.2002 with effect as mentioned in s. 82(2) of the amending Act) by 2002 c. 23, s. 82, Sch. 25 Pt. 1 para. 6(3))
- C1** Sch. 26 extended (retrospective to 30.9.2002) by Finance Act 2003 (c. 14), s. 177(4)(8)(11)

PART 4 **U.K.**

ACCOUNTING METHODS

Authorised accounting methods

- 17 (1) Subject to the following provisions of this Schedule, the alternative accounting methods that are authorised for the purposes of this Schedule are—
- (a) an accruals basis of accounting; and
 - (b) a mark to market basis of accounting under which any derivative contract to which that basis is applied is brought into account in each accounting period at a fair value.
- (2) An accounting method applied in any case shall be treated as authorised for the purposes of this Schedule only if—
- (a) subject to paragraphs (b) to (d), it is in conformity with generally accepted accounting practice to use that method in that case;
 - (b) it contains proper provision for allocating payments under a derivative contract, or arising as a result of a related transaction, to accounting periods;
 - (c) it contains proper provision for determining exchange gains and losses from a derivative contract for accounting periods; and
 - (d) where it is an accruals basis of accounting, it does not contain any provision (other than provision in respect of exchange losses or provision comprised in authorised arrangements for bad debt) that gives debits by reference to the valuation at different times of any derivative contract.
- (3) In the case of an accruals basis of accounting, proper provision for allocating payments under a derivative contract to accounting periods is provision which—
- (a) allocates payments to the period to which they relate, without regard to the periods in which they are made or received or in which they become due and payable;
 - (b) includes provision which, where payments relate to two or more periods, apportions them on a just and reasonable basis between the different periods;

Status: Point in time view as at 23/01/2003.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Part 4. (See end of Document for details)

- (c) assumes, subject to authorised arrangements for bad debt, that every amount payable to the company under the derivative contract will be paid in full as it becomes due;
 - (d) secures the making of the adjustments required in the case of the derivative contract by authorised arrangements for bad debt; and
 - (e) provides, subject to authorised arrangements for bad debt, that, where there is a release of any liability owed by the company under the derivative contract, the appropriate amount in respect of the release is credited to the company in the accounting period in which the release takes place.
- (4) In the case of a mark to market basis of accounting, proper provision for allocating payments under a derivative contract to accounting periods is provision which allocates payments to the periods in which they become due and payable.
- (5) In this paragraph the references to authorised arrangements for bad debt are references to accounting arrangements under which debits and credits are brought into account in conformity with the provisions of paragraph 22.
- (6) In this paragraph “fair value”, in relation to a derivative contract of a company, means the amount which, at the time as at which the value falls to be determined, is the amount that the company would obtain from or, as the case may be, would have to pay to an independent person for—
- (a) the transfer of all the company’s rights under the contract in respect of amounts which at that time are not yet due and payable; and
 - (b) the release of all the company’s liabilities under the contract in respect of amounts which at that time are not yet due and payable.

Application of accounting methods

- 18 (1) This paragraph has effect, subject to the following provisions of this Schedule, for the determination of which of the alternative authorised accounting methods that are available by virtue of paragraph 17 is to be used as respects the derivative contracts of a company.
- (2) Different methods may be used as respects different derivative contracts or, as respects the same derivative contract, for different accounting periods or different parts of the same accounting period.
- (3) If a basis of accounting which is or equates with an authorised accounting method is used as respects any derivative contract of a company in a company’s statutory accounts, then the method which is to be used for the purposes of this Schedule as respects that contract for the accounting period, or part of a period, for which that basis is used in those accounts shall be—
- (a) where the basis used in those accounts is an authorised accounting method, that method; and
 - (b) where it is not, the authorised accounting method to which it equates;
- but this sub-paragraph is subject to paragraphs 19 to 21.
- (4) For any period or part of a period for which the authorised accounting method to be used as respects a derivative contract of a company is not—
- (a) the method determined under sub-paragraph (3),
 - (b) an authorised mark to market basis of accounting in accordance with an election under paragraph 19, or

Status: Point in time view as at 23/01/2003.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Part 4. (See end of Document for details)

- (c) an authorised mark to market basis of accounting in accordance with paragraph 20 or 21,
an authorised accruals basis of accounting shall be used for the purposes of this Schedule as respects that derivative contract.
- (5) For the purposes of this paragraph (but subject to sub-paragraph (6))—
- (a) a basis of accounting equates with an authorised accruals basis of accounting if it purports to allocate payments under a derivative contract to accounting periods according to when they are taken to accrue; and
- (b) a basis of accounting equates with an authorised mark to market basis of accounting if it purports in respect of a derivative contract—
- (i) to produce credits or debits computed by reference to the determination, as at different times in an accounting period, of a fair value; and
- (ii) to produce credits or debits relating to payments under that derivative contract according to when they become due and payable.
- (6) An accounting method which purports to make any such allocation of payments under a derivative contract as is mentioned in sub-paragraph (5)(a) shall be taken for the purposes of this paragraph to equate with an authorised mark to market basis of accounting (rather than with an authorised accruals basis of accounting) if—
- (a) it purports to bring that derivative contract into account in each accounting period at a value which would be fair value if the valuation were made on the basis that any periodic payments falling to be made under the contract were to be disregarded to the extent that they have already accrued; and
- (b) the credits and debits produced in the case of that contract by that method (when it is properly applied) correspond, for all practical purposes, to the credits and debits produced in the case of that contract, and for the same accounting period, by an authorised mark to market basis of accounting.

Application of accounting methods: election to follow generally accepted accounting practice

- 19 (1) Sub-paragraph (2) has effect if, in the case of a company falling within paragraph 52(1)(c) or (d) (companies whose statutory accounts are accounts to which Part 1 of Schedule 21C or 21D to the Companies Act 1985 (c. 6) applies or accounts falling to be drawn up in accordance with the requirements imposed under the law of the home State),—
- (a) an authorised mark to market basis of accounting would be used as respects some or all of the company's derivative contracts, were the company a UK company following generally accepted accounting practice, but
- (b) that is not the basis of accounting used as respects those derivative contracts in the company's statutory accounts.
- (2) Where this sub-paragraph has effect in relation to a company, the company may elect to use an authorised mark to market basis of accounting as its authorised accounting method for the purposes of this Schedule in relation to every derivative contract as respects which that basis would be used were it a UK company following generally accepted accounting practice.
- (3) Any election under sub-paragraph (2)—
- (a) must be made before the expiration of the period of two years following the end of the company's first accounting period beginning on or after 1st

Status: Point in time view as at 23/01/2003.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Part 4. (See end of Document for details)

- October 2002 in which it is party to a derivative contract in relation to which an election under sub-paragraph (2) may be made;
- (b) has effect for that accounting period and all subsequent accounting periods of the company; and
 - (c) is irrevocable.
- (4) A company which makes an election under sub-paragraph (2) as respects its derivative contracts shall be taken for the purposes of Chapter 2 of Part 4 of the Finance Act 1996 (c. 8) to have at the same time made an election under section 86(3A) of that Act having effect—
- (a) for the accounting periods mentioned in sub-paragraph (3)(b), and
 - (b) as respects any loan relationships to which the company is or may become a party in any of those accounting periods,
- and that election shall so have effect notwithstanding anything in paragraph (a) or (b) of subsection (3B) of that section.

Application of accounting methods: requirement to follow generally accepted accounting practice

- 20 (1) Sub-paragraph (2) has effect if, in the case of a company falling within paragraph 52(1)(c) or (d),—
- (a) the company has not made an election under paragraph 19,
 - (b) an authorised mark to market basis of accounting would be used for an accounting period—
 - (i) as respects some or all of the company’s derivative contracts, and
 - (ii) as respects some or all of its loan relationships,
 were the company a UK company following generally accepted accounting practice, and
 - (c) that basis of accounting—
 - (i) is used in the company’s statutory accounts as respects those loan relationships for that accounting period, but
 - (ii) is not the basis of accounting used in the company’s statutory accounts as respects those derivative contracts for that accounting period.
- (2) Where this sub-paragraph has effect in relation to any accounting period, the company must for that accounting period use an authorised mark to market basis of accounting as its authorised accounting method for the purposes of this Schedule in relation to every derivative contract as respects which that basis would be used were it a UK company following generally accepted accounting practice.
- (3) Sub-paragraph (4) has effect where, in the case of a derivative contract of a company,
-
- (a) the company uses, as respects the contract, a basis of accounting other than an authorised mark to market basis of accounting for an accounting period (the “preceding period”), but
 - (b) by virtue of sub-paragraph (2), the company must for the succeeding accounting period (the “first mark to market period”) use, as respects the contract, an authorised mark to market basis of accounting as its authorised accounting method for the purposes of this Schedule.

Status: Point in time view as at 23/01/2003.

Changes to legislation: There are currently no known outstanding effects for the Finance Act 2002, Part 4. (See end of Document for details)

- (4) Where this sub-paragraph has effect in relation to a derivative contract of a company, the company shall be deemed—
- (a) to have disposed of the contract immediately before the end of the preceding period for a consideration of an amount equal to the fair value of the contract at that time, and
 - (b) to have reacquired it for the same consideration immediately after the beginning of the first mark to market period.

Basis of accounting for contracts falling within paragraph 6, 7 or 8

- 21 (1) This paragraph applies in relation to a contract which is a derivative contract for the purposes of this Schedule by virtue of—
- (a) paragraph (contracts producing a guaranteed return),
 - (b) paragraph (contracts where guaranteed amount payable on maturity), or
 - (c) paragraph (contracts to provide insurance benefits).
- (2) Where this paragraph applies in relation to a derivative contract, the accounting method to be used as respects the derivative contract for an accounting period shall be an authorised mark to market basis of accounting.

Status:

Point in time view as at 23/01/2003.

Changes to legislation:

There are currently no known outstanding effects for the Finance Act 2002, Part 4.