These notes refer to the Finance Act 2009 (c.10) which received Royal Assent on 21 July 2009

FINANCE ACT 2009

EXPLANATORY NOTES

INTRODUCTION

Section 35Schedule 15: Tax Treatment of Financing Costs and Income

Details of the Schedule

Part 1 - Overview

5. Schedule 15 is divided into eleven parts. Part 1 provides an overview of the Schedule. Part 2 sets out the circumstances in which the Schedule applies to a worldwide group of companies for any particular period of account. Part 3 provides the basic rules where an amount of financing expense of UK group companies falls to be disallowed. Part 4 provides for certain financing income of UK group companies to be exempted from corporation tax but only to the extent that financing expense has been disallowed under Part 3. Part 5 allows certain intra-group financing income to be exempted from corporation tax where the paying company is resident in the European Economic Area (EEA) unless the paying company is resident in the UK and, the effect of Part 3 aside, is denied a deduction for the payment for tax purposes. Part 6 provides for anti-avoidance measures to counter the effect of schemes designed to avoid provisions of the Schedule. Part 7 and Part 8 define the amounts and types of intra-group financing income and financing expense that are used in Part 3 to calculate any disallowance, and are used in Part 4 to determine the amount of financing income to be disregarded. Part 9 sets out how the external gross finance expense of the worldwide group is to be computed for the purposes of the Schedule. Part 10 contains further definitions and other interpretative provisions. Part 11 deals with commencement and consequential amendments to other legislation.

Part 2 – Application of this Schedule

6. This Part of the Schedule sets out gateway conditions to be applied by reference to a comparison of the consolidated gross debt of the worldwide group with the aggregate figure of net debt of the UK group companies. It also sets out rules for excluding groups engaged in particular financial services business. If these conditions for either test are met for any given period of account of the worldwide group then the UK members of the group are not subject to the remaining Parts of the Schedule.

7. Paragraph 2 sets a condition for application of the Schedule based on the amount of the worldwide group's debt. The term 'worldwide group' is defined in Part 10. The Schedule applies if the 'UK net debt' of the group exceeds 75 per cent of the 'worldwide gross debt' of the group.

8. Sub-paragraph (2) provides that the Schedule will not apply to a period in which the worldwide group is a "qualifying financial services group", which is defined by paragraph 7.

9. Sub-paragraphs (3)-(5) provide for the 75 per cent figure in sub-paragraph (1) to be increased or decreased prospectively by Treasury order, subject to affirmative resolution.

10. Paragraph 3 defines 'UK net debt' for the purpose of paragraph 2 as the average of the opening and closing net debt (the net debt amount) of each relevant group company. The term 'relevant group company' is defined in paragraph 86. Sub-paragraph (3) and (4) provide for a 'net debt' amount of less than £3 million, and for the net debt amount of a dormant company, to be treated as nil for this purpose respectively. Sub-paragraphs (5)-(7) allow the de minimis limit of £3 million to be increased or decreased prospectively by Treasury order.

11. Sub-paragraph (8) takes the opening and closing dates as the beginning and end of the period of account of the 'worldwide group', unless the company is only a 'relevant group company' for part of that period in which case the opening and closing dates are set by reference to when the company became or stopped being a 'relevant group company'.

12. Paragraph 4 explains that the 'net debt' of a 'relevant group company' at any particular time is the company's debt liabilities less its liquid assets such as cash and loans receivables, taken from the company's balance sheet. The class of both relevant liabilities and relevant assets are defined by sub-paragraphs (3) and (4), interpreted by reference to generally accepted accounting practice applicable to UK companies (see sub-paragraph (5)) and can be added to by regulations.

13. Paragraph 5 defines 'worldwide gross debt'. Sub-paragraph (1) explains that the figure is the average of the amounts taken at the end of the current and preceding periods of account of the worldwide group. Sub-paragraph (2) defines the term by reference to particular amounts of information disclosed in the group's balance sheet. The paragraph lists the amounts to be taken into account and sub-paragraph (3) provides that expressions used in the list are to be interpreted in accordance with the accounting standards used to draw up the financial statements. The class of liabilities can be added to by regulations. Sub-paragraph (4) provides that rules which apply to a group's consolidated financial statements within paragraphs 87 to 90 apply to this paragraph.

14. Paragraph 6 explains what is meant by references to amounts disclosed in the balance sheet of a 'relevant group company'. This includes provision (in sub-paragraphs (2)-(4)) to deal with a foreign company that has a UK permanent establishment and to deal with cases where either a UK company has not drawn up financial statements or there are no separate financial statements for a UK permanent establishment of a foreign company. In all cases references are to amounts that would be disclosed if financial statements were drawn up.

15. Paragraph 7 defines 'qualifying financial services groups'.

16. Sub-paragraph (1) provides that a worldwide group is a 'qualifying financial services group' in a period of account where it either meets the 'trading income condition' or would have met it had it not been for losses incurred by the group as a result of trading or investing in financial instruments.

17. Sub-paragraph (2) explains that the 'trading income condition' is met for a period of account where either substantially all of the 'UK trading income' of the worldwide group for that period, or substantially all of the 'worldwide trading income' of the group is derived from 'qualifying activities'. 'Qualifying activities' are defined in paragraph 8.

18. Sub-paragraph (3) defines 'UK trading income' and 'worldwide trading income' for the purposes of Part 2. 'UK trading income' for a period of account of the group is defined as the sum of the trading income of all companies that were "relevant group companies" at any time during that period of account. 'Relevant group company' is defined in paragraph 86. 'Worldwide trading income' for a period is defined as the trading income for that period of the 'worldwide group'. 'Worldwide group' is defined in paragraph 78.

19. Paragraph 8 provides the list of activities that are to be regarded as 'qualifying activities' for the purposes of Part 2. These are lending activities and activities that are ancillary

to lending activities, insurance activities and insurance-related activities and relevant dealing in financial instruments.

20. Paragraph 9 defines 'lending activities and activities ancillary to lending activities'. Sub-paragraph (1) provides the list of activities that are lending activities for the purposes of Part 2. The list includes 'alternative finance arrangements' which has the same meaning as in Chapter 6 of Part 6 of the Corporation Tax Act 2009. This broadly applies to arrangements that have the same effect as lending arrangements without involving the payment of interest and relates primarily to Islamic finance products.

21. Sub-paragraph (2) excludes from the definition of a 'qualifying activity' activities ancillary to lending activities where the income derived from the ancillary activity is significant when compared to the income derived from lending activities by the worldwide group.

22. Sub-paragraph (3) provides that the income to be taken into account for the purposes of the test in sub-paragraph (2) is the same income that is taken into account for the purposes of the trading income condition in paragraph 7.

23. Sub-paragraph (4) provides a regulation making power to allow the Commissioners to make changes to the list of lending activities in sub-paragraph (1).

24. Sub-paragraph (5) provides that activities carried out in connection with lending activities and activities ancillary to lending activities include the buying, holding, managing and selling of assets.

25. Paragraph 10 defines 'insurance activities' and 'insurance related activities' for the purposes of Part 2. Sub-paragraph (1) defines 'insurance activities' as effecting or carrying out 'contracts of insurance' by a 'regulated insurer' and investment business arising directly from that activity. Sub-paragraph (6) defines the terms used elsewhere in the paragraph. 'Contract of insurance' has the same meaning as in Chapter 1 of Part 12 of ICTA 1988. In that Chapter, 'contract of insurance' has the meaning given by Article 3(1) of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001. 'Insurance business' has the same meaning as in the Financial Services Authority Handbook. A 'regulated insurer' is defined as any member of the worldwide group that is authorised to carry on an insurance business under the laws of any state or territory, or is a member of a body or organisation that is so authorised.

26. Sub-paragraph (2) explains what is meant by 'insurance-related activities'. Sub-paragraph (2)(a) covers activities that are ancillary to insurance activities defined in sub-paragraph (1). Sub-paragraph (2)(b) covers activities that are the same kind of activities carried out for the purposes of the insurance activity, but which are not actually carried out those purposes and would not be carried out but for insurance activities being carried out. An example would be the management of assets for a third party by an institution that also manages assets as part of its own insurance business.

27. Sub-paragraph (4) explains that activities within sub-paragraphs (2)(a) and (b) are not to be regarded as related to insurance activity if the income from those activities is significant when compared to the income derived by the worldwide group from insurance activities.

28. Sub-paragraph (5) provides that the income to be taken into account for the purposes of the test in sub-paragraph (4) is the same income that is taken into account for the purposes of the trading income condition in paragraph 7.

29. Paragraph 11 gives the meaning of the phrase 'relevant dealing in financial instruments' in paragraph 8. It provides that dealing in financial instruments is a qualifying activity where the profits or losses from that dealing, excluding those profits made in the capacity of a broker, are included in the trading profits of the business.

30. Paragraph 12 explains how UK trading income of the worldwide group is calculated for the purposes of paragraph 7. The trading income of a relevant group company will normally be the gross income arising from its activities without taking account of any deductions. However, where the income in respect of an activity is normally reported on a net basis in accordance with generally accepted accounting practice, then the trading income from that activity will be the net income.

31. Sub-paragraph (6) provides that where a proportion of an accounting period in which a relevant group company reports its trading income does not fall within a period of account of the worldwide group, then its income will be reduced on a time-apportioned basis.

32. Sub-paragraph (7) provides that gross or net income received from other UK members of the worldwide group is disregarded in calculating the amount of the UK trading income for the purposes of paragraph 7.

33. Paragraph 13 explains how the worldwide trading income of the worldwide group is calculated for the purposes of paragraph 7. As for the trading income of a relevant group company, the trading income of the worldwide group will normally be the gross income arising from its activities without taking account of any deductions. However, where the income in respect of an activity is normally reported on a net basis in accordance with international accounting standards, then the trading income from that activity will be the net income.

34. Paragraph 14 provides that if an amount disclosed in balance sheets at any given date is expressed in a currency other than sterling, then the amount must be translated into sterling by reference to the spot rate at that date. Sub-paragraphs (2) - (3) provide that where the group's and relevant group companies' balance sheets are all expressed in the same foreign currency:

    a. the calculation performed for Part 2 can be made by reference to the functional currency of the group; and

    b. the de minimis figure of £3 million in paragraph 3(3) can be translated into the functional currency of the group.

Part 3 – Disallowance of Deductions

35. Part 3 applies if the 'tested expense amount' exceeds 'the available amount'. In broad terms, the 'tested expense amount' is the aggregate of the net amount of financing expense payable by each of the relevant group companies that have net financing expense, while the available amount is the external gross finance expense of the worldwide group of companies. In calculating the 'tested expense amount', net amounts falling below a de minimis limit are excluded.

36. The excess is the amount of financing expense that must be disallowed in computing the corporation tax profits of the relevant group companies. Part 3 sets out how the group should notify HM Revenue & Customs (HMRC) of the allocation of the disallowance between the relevant group companies by submitting an allocation statement, and provides for an alternative procedure if the group fails to do so.

37. Paragraph 15 applies this Part of the Schedule if for any period of account ('the relevant period of account') of the 'worldwide group', the 'tested expense amount' exceeds the 'available amount'. The 'tested expense amount' is defined in Part 8 and the 'available amount' in Part 9. Under sub-paragraph (2), the excess is called the 'total disallowed amount'.

38. Paragraph 16 provides that Part 3 applies to a company that is a relevant group company at any time during the relevant period of account of the group.

39. Paragraph 17 provides that the companies to which Part 3 applies may appoint one of them to act on their behalf for the relevant period of account in respect of matters governed by Part 3. The appointment must be made by all the relevant group companies together, but once made does not have to be renewed for each subsequent period of account.

40. Sub-paragraph (3) provides a regulation-making power to allow the Commissioners for HM Revenue & Customs to introduce rules governing an appointment within this paragraph, and mentions matters that may be covered in particular in regulations.

41. Paragraph 18 defines the term 'the reporting body' for the purposes of Part 3 as the company appointed under paragraph 17 for the relevant period of account, or the companies to which Part 3 applies (acting jointly) if no such appointment has effect.

42. Paragraph 19 requires the reporting body to send a 'statement of allocated disallowances' for the relevant period of account to HMRC. Sub-paragraph (2) requires the statement to be received by HMRC within 12 months of the end of the period of account, and, by virtue of sub-paragraph (3), it must comply with the requirements of paragraph 21.

43. Paragraph 20 allows the reporting body to submit a revised statement to HMRC, with subsequent revisions also being allowed. Any revised statement must be received by HMRC within 36 months of the end of the period of account. It must also comply with the requirements of paragraph 21 and must indicate where it differs from the previous statement. The revised statement supersedes the previous statement.

44. Paragraph 21 sets out the requirements of a statement of allocated disallowances. Sub-paragraph (3) provides for the statement to show the 'tested expense amount', 'available amount' and 'total disallowed amount'. Under sub-paragraph (4) the statement must list the companies that are allocated a disallowance, and identify the particular financing expense amount(s) that are to be disallowed for each such company, as defined by sub-paragraph (5). Sub-paragraph (6) requires that the total of the amounts specified must equal the total disallowed amount.

45. Paragraph 22 gives the effect of the statement of allocated disallowances. It is that a financing expense amount of a company specified in a statement is not to be brought into account by the company for corporation tax purposes.

46. Paragraph 23 provides that where a company has delivered a company tax return for the relevant period, and as a result of a revised statement either the amount of profits on which corporation tax is chargeable for a relevant accounting period of a company changes, or any other information contained in the return is rendered incorrect, then the company is treated as having amended its return for the accounting period so as to reflect the change or correct the information.

47. Paragraph 24 provides a regulation-making power to allow the Commissioners to introduce rules governing a statement of allocated disallowances, and mentions matters that may be covered in particular.

48. Paragraph 25 sets out the consequences of a failure by a reporting body to submit a statement of allocated disallowances that complies with the requirements of paragraph 21. Sub-paragraph (2) explains that company to which Part 3 applies that has a net financing deduction must reduce the deductions brought into account in respect of financing expense amounts. The term net financing deduction is defined in paragraph 70(2).

49. Sub-paragraph (3) provides, by way of a formula, that a company's share of the total disallowed amount (the reduction) is in the same proportion as its net financing deduction bears to the tested expense amount.

50. Sub-paragraph (4) provides that the particular financing expense amounts that must be reduced, and the amounts of the reductions, must be determined in accordance with regulations. Sub-paragraph (5) lists the areas that the regulations may cover, but is not exhaustive.

51. Paragraph 26 provides a regulation-making power to allow the Commissioners to introduce rules to ensure that a company in relation to which a financing expense amount is reduced under paragraph 25 has sufficient information to determine its amount of disallowance and describes matters that may be covered in particular.

Part 4 – Exemption of financing income

52. Part 4 applies where there has been a disallowance under Part 3. The effect of Part 4 is to allow for an amount of financing income received by one or more UK members of a worldwide group to be exempted from corporation tax. The total amount of financing income that can be disregarded in this way is limited by reference to the 'total disallowed amount' (see paragraph 15), and by the aggregate amount of net financing income of the UK group companies, which is referred to as the 'tested income amount' and is defined in Part 8 as the sum of the net financing incomes of each UK group company.

53. Part 4 sets out how the group should notify HMRC of the allocation of the exemption between the group companies by submitting an allocation statement, and provides for an alternative procedure if the group fails to do so.

54. Paragraph 27 applies this Part of the Schedule to deal with the exemption of financing income for a period of account of the worldwide group where the tested expense amount exceeds the available amount. That is, in the same circumstances in which a disallowance arises under Part 3. Sub-paragraph (2) calls the excess the 'total disallowed amount'.

55. Paragraph 28 provides that Part 4 applies to a company that is a UK group company at any time during the period of account of the worldwide group. A 'UK group company' to which Part 4 applies is defined in paragraph 86 and is a wider class of companies within the worldwide group than 'relevant group companies' to which Part 3 applies.

56. Paragraph 29 provides that the companies to which Part 4 applies may appoint one of them to act on their behalf for the relevant period of account in respect of matters governed by Part 4.

57. Sub-paragraph (2) requires the appointment to be signed on behalf of each company by the 'appropriate person' for that company. The 'appropriate person' is defined by sub-paragraphs (4) and (5) as the proper officer of the company (usually the company secretary) or as such other person as has been authorised to act on its behalf for the purposes of the Schedule.

58. Sub-paragraph (3) provides a regulation-making power to allow the Commissioners to introduce rules governing an appointment within this paragraph, and mentions matters that may be covered in particular.

59. Paragraph 30 defines the term 'the reporting body' for the purposes of Part 4 as the company appointed under paragraph 29 for the relevant period of account, or the companies to which Part 4 applies (acting jointly) if no such appointment has effect.

60. Paragraph 31 requires the reporting body to send a 'statement of allocated exemptions' for the relevant period of account to HMRC. The statement must be received by HMRC within 12 months of the end of the period of account, and must comply with the requirements of paragraph 33.

61. Paragraph 32 allows the reporting body to submit a revised statement to HMRC, with subsequent revisions also being allowed. Any revised statement must be received by

HMRC within 36 months of the end of the period of account, again must comply with the requirements of paragraph 33 and must indicate where it differs from the previous statement. The revised statement supersedes the previous statement.

62. Paragraph 33 sets out the requirements of a statement of allocated exemptions in terms of the information it must contain and sub-paragraph (2) requires it to be signed by the appropriate person or persons.

63. Sub-paragraph (3) provides for the statement to show the ‘tested expense amount’, ‘available amount’ and ‘total disallowed amount’. Under sub-paragraph (4) the statement must list the companies that are allocated an exemption, and identify the particular financing income amount(s) that are to be exempted for each, as defined by sub-paragraph (5). Sub-paragraph (6) requires that the total of the amounts specified must not exceed the lower of

- total disallowed amount, (see paragraph 15), and
- the tested income amount (see Part 8).

64. Paragraph 34 gives the effect of the statement of allocated exemptions. It is that a financing income amount of a company specified in a statement is not to be brought into account by the company for corporation tax purposes.

65. Paragraph 35 provides that where a company has delivered a company tax return for the relevant period, and as a result of a revised statement either the amount of profits on which corporation tax is chargeable for a relevant accounting period of a company changes, or any other information contained in the return is rendered incorrect, then the company is treated as having amended its return for the accounting period so as to reflect the change or correct the information..

66. Paragraph 36 provides a regulation-making power to allow the Commissioners to introduce rules governing a statement of allocated exemption and mentions matters that may be covered in particular.

67. Paragraph 37 sets out the consequences of a failure by a reporting body to submit a statement of allocated exemptions that complies with the requirements of paragraph 33.

68. Sub-paragraph (2) provides that subject to the provisions of the paragraph, each financing income amount for the relevant period of account of each company to which Part 4 applies is to be reduced to nil.

69. Sub-paragraphs (4) and (5) provide, by way of a formula, that if the result of reducing each financing income to nil is that the total reductions for the relevant period exceed the total disallowed amount, then the reduction for each company is reduced by that part of the excess that its reduction bears to the total reduction.

70. Paragraph 38 provides a regulation-making power to allow the Commissioners to introduce rules to ensure that a company to which a financing income amount is reduced under paragraph 30 has sufficient information to determine its amount and mentions matters that may be covered in particular.

71. Sub-paragraph (2) provides for the regulations to require relevant information to be sent from one group company to another.

72. Sub-paragraphs (3) and (4) allow the regulations to make provision for circumstances where insufficient information is held by a company for the purpose of determining its appropriate financing income reduction.

73. Sub-paragraph (5) provides for the regulations to extend the time limits for amending a corporation tax return in certain specified circumstances so as to reflect a reduction under paragraph 37.

74. Paragraph 39 provides that where in certain defined circumstances one company makes a payment to another company as result of an adjustment to taxable income or expenses made under Schedule 15, then those amounts are not to be taken into account in computing the taxable profits of either company.

75. Sub-paragraphs (1)(a) to (d) define the conditions which are necessary for the paragraph to apply. Firstly, the financing income amounts of a company ("company A") and the financing expense amounts of another company ("company B") must both have either not been brought into account or reduced by the provisions of Schedule 15. If, solely or mainly because of those circumstances, company A makes one or more payments "the balancing payments" to company B, then under sub-paragraph (2) those balancing payments are neither taken into account for the purposes of corporation tax nor treated as distributions.

76. Sub-paragraph (3) provides that the amount not taken into account by virtue of sub-paragraph (2) must not exceed the amount of either the financing income amounts or financing expense amounts not brought into account or reduced by the provisions of Schedule 15.

Part 5 – Intra group financing income where payer denied deduction

77. Subject to conditions, Part 5 allows intra-group financing income received from a company resident in the EEA, excluding the UK, to be exempt from corporation tax. To the extent that tax relief is not available for finance costs within the EEA excluding the UK, like consequences follow for the recipient of the income to provide equivalence with an outcome arising from the other Parts of this Schedule.

78. Paragraph 40 gives exemption for an amount of financing income received from a group company that is resident in the EEA excluding the UK. Exemption is subject to meeting all the conditions A to C, which are defined in the following paragraphs.

79. Paragraph 41 defines 'relevant associate' for the purposes of this Part. Condition A of paragraph 40 requires the payer to be a relevant associate of the recipient of the financing income.

80. The payer is a relevant associate if it is a parent company or subsidiary of the recipient or a 75% subsidiary of the parent of the recipient. The term 'parent company' is defined in paragraph 92 by reference to International Accounting Standards (IAS) and the terms '75% subsidiary' is defined in section 838(1)(b) of the Income and Corporation Taxes Acts (ICTA) by reference to the proportion of ordinary share capital held.

81. Paragraph 42 defines 'tax resident' and 'EEA territory' for the purposes of Part 5. Condition B of paragraph 40 requires the payer to be a tax resident of an EEA territory.

82. Paragraphs 43 and 44 define the two elements of condition C of Paragraph 40. Both parts of condition C must be met to fulfil the condition that no relief is available in respect of the financing income.

83. Paragraph 43 defines the requirement set out in the first part of condition C of paragraph 40, which is the requirement that qualifying EEA relief is not available to the payer of the financing income in the current period or any preceding period by reason of the payment. There are two conditions A and B in this paragraph that must both be met in order for this requirement to be satisfied.

84. Sub-paragraph (2) explains that condition A is that no deduction in respect of the payment can be taken into account for the purposes of calculating the taxable profits of the payer in the current period or any preceding period. The current period is the period in which the payment is made (paragraph 40(4)(a)) and taxable profits means the profits taken into account for the taxation purposes of any EEA territory including the UK.

85. Sub-paragraph (3) explains that condition B is that no tax credit or other form of tax relief whatsoever is given to the payer or any other person that is determined by reference to the payment, in the current period or any previous period.

86. Sub-paragraph (4) explains that conditions A and B are not met if there was any step that the payer or any other person could have taken that would have caused the payment to be taken into account as described above.

87. Conditions A and B are also not met if, in certain circumstances, the payment was not taken into account as described above because of this Schedule.

88. Sub-paragraph (5)(b) explains that the Conditions are not met if the payer was denied a deduction or relief in respect of the payment due to provisions in a double taxation treaty. This could be where either the denial of the deduction in the EEA territory is sanctioned by the associated enterprises article of a DTA between that territory and the UK; or where a DTA between the EEA territory and another territory applies to determine which territory has taxing rights in respect of the profits, income or gains whose calculation takes into account the payment in question.

89. Sub-paragraph (6) explains what is meant by double taxation agreements and articles contained in those agreements.

90. Paragraph 44 sets out the second requirement of condition C in paragraph 40. It is very similar to the first requirement described in paragraph 43 above, except that it refers in each case to any future period.

91. Condition A therefore refers to no deduction being given in respect of the payment being taken into account in the computation of any profits that might arise and be chargeable in the EEA territory in any future period. Condition B asks whether any form of relief will become available in any future period, but in answering this question it is sufficient to consider only the position at the end of the current period.

92. As with paragraph 43, this Schedule and the provisions of double taxation agreements are both disregarded when considering conditions A and B.

93. Paragraph 45 defines the term ‘tax’ for the purposes of the Schedule. UK tax refers to corporation tax or income tax and tax of any other territory refers to taxes that are equivalent to either of these two taxes. A tax is not disqualified solely because it is charged by any regional tax authority, such as the German Länder.

94. Paragraph 46 defines the term ‘financing income amount’, which is the term used in paragraph 40 to describe the amount that is exempt from tax in the hands of a company subject to conditions A to C of that paragraph. A financing income amount is an amount that falls within any of conditions A to C in this paragraph.

- condition A refers to any amount taxed under loan relationships legislation except the matters described in sub-paragraph (3)
- condition B refers to a receipt corresponding to the finance element of a finance lease; and
- condition C refers to a receipt corresponding to the finance element of a debt factoring arrangement.

95. For this purpose sub-paragraph (6) provides for the provisions of Part 7 to apply in relation to an amount which is a financing income amount by virtue of meeting condition A, B or C in this paragraph in the same way as they do for a financing income amount that meets condition A, B or C in paragraph 48.

Part 6 – Anti-avoidance

96. Part 6 contains three sets of ant-avoidance rules targeted at schemes designed to circumvent provisions in the Schedule. The first rule is targeted at avoidance schemes that manipulate the rules in Part 2 of Schedule 15 in order to avoid the application of the Schedule to a group of companies that would not otherwise have met the 'gateway' conditions in paragraph 2. The second targets schemes to reduce the amount of a disallowance under the debt cap, whether by decreasing the tested expense amount or by increasing the available amount or the tested income amount, or any combination of these. The third rule counters manipulation of the Part 5 rules which disregard certain intra-group financing income.

97. Paragraph 47 counters schemes that attempt to manipulate the 'gateway' and 'financial services exclusion' rules. For example, a group that would otherwise fail the test in paragraph 2 (so that the debt cap rules applied) might borrow from a bank at the end of its period of account to boost the 'worldwide gross debt' amount defined at paragraph 3, repaying the loan the next day. A period of account of the worldwide group falls within paragraph 47 if three conditions are met.

98. Sub-paragraph (1) provides that, where the conditions are met, the 'gateway' result is ignored and the full rules of Schedule 15 apply to that period of account. This may (or may not) lead to a disallowance of financing costs of UK companies.

99. The first condition, at sub-paragraph (2), is met if a scheme has been entered into at any time before the end of the period, and the period would have been within paragraph 2(1) if the scheme had not been entered into. It is therefore capable of applying to schemes that have been entered into before the start of the period of account, as well as those put in place during the period. 'Scheme' is defined in wide terms at paragraph 53(1) and may involve a single transaction, or more than one.

100. Sub-paragraph (3) gives the second condition. It must be the main purpose, or one of the main purposes, of any party to the scheme to ensure that a group passes the gateway test. The party must have that purpose when it enters into the scheme. So, in the example above of a group company undertaking overnight borrowing at the end of the group's period of account, it would be necessary to examine that company's purpose when it borrowed. If the borrowing was for a genuine commercial purpose, and any consideration of its effect on the 'gateway' condition was no more than incidental, paragraph 47 would not apply.

101. The third condition, in sub-paragraph (4), is that the scheme is not an excluded scheme. 'Excluded scheme' is defined in paragraph 53(2) as one answering to a description specified in regulations made by the HMRC Commissioners (under negative procedure). This power to exclude particular schemes or arrangements applies to all three rules in Part 6, and provides a safeguard against the possibility that some normal tax planning arrangements, which would not be seen as abusive, might nevertheless be caught by the anti-avoidance rule.

102. Paragraph 48 is directed at schemes manipulating the tested expense amount, the tested income amount or the available amount, or any combination of these three. It looks at the aggregate effect of these three amounts – the 'relevant net deduction' - defined in paragraph 49. This is so much of the total disallowed amount (the tested expense amount less the available amount) as cannot be covered by a disregard of financing income of UK group companies. The relevant net deduction may be nil.

103. Sub-paragraph (1) provides that this rule applies where three conditions are met. Both the application of the rule, and the conditions, require a comparison to be made between the effect of the actual scheme, and the effect of an alternative scenario, based on assumptions set out in paragraph 50. Where the conditions are met, the tested expense amount, the tested income amount and the available amount must all be calculated on

the basis of the alternative scenario. It is these amounts that group companies must take account of for the purposes of Part 3 or Part 4 of the Schedule.

104. Paragraph 50 provides that assumptions must be made in calculating amounts or sums in accordance with this paragraph, and sets out those assumptions. The first is that the scheme in question had not been entered into. The second is that, if the effect of the debt cap had not been a factor, anything which is more likely than not to have been done or not done would have been done or not done, as the case may be. For example, if there were three courses which the group might have followed with 60%, 35% and 5% probability respectively, only the one which the group had a 60% chance of following would be 'more likely than not'.

105. Paragraph 48(2) sets out the first condition. It must be the main purpose, or one of the main purposes, of any party to a scheme, on entering into it, to reduce the amount of the relevant net deduction, compared with what it would have been under the alternative scenario based on the assumptions in paragraph 50.

106. A UK member of the group, which had an outstanding loan from its overseas parent, might for example seek to reduce its financing expense amount by paying a lump sum to a bank in return for the bank taking on the obligation to pay interest. Had the debt cap not been a consideration, it would have carried on paying the interest to its parent in the normal way. Since the debits representing the amortisation of the lump sum arise from a related transaction (see paragraph 54(3)(c) of the Schedule), that company's financing expense amount is less than it would have been under the alternative scenario. This in turn means that the tested expense amount, and hence the 'net relevant deduction' are reduced. Provided that it is a main purpose of the UK company (or any other party to the scheme) to achieve this result, the paragraph 48(2) condition will be satisfied.

107. The further condition in paragraph 48(3) means that this anti-avoidance rule will bite only if the scheme also reduces the overall corporation tax profits (or increases the losses) of UK group companies, compared to the alternative scenario. In the example above, the debits from amortisation of the lump sum remain allowable loan relationships debits; the group may incur additional fees and hedging costs; and (absent the anti-avoidance rule) the debt cap restriction on relevant group companies would be reduced. All of this means that the effect of the scheme would almost certainly be a reduction in corporation tax profits.

108. This is not necessarily so, however. For example, the financing expenses of the company would similarly be reduced if the parent company were to replace the loan by equity. Such an arrangement might be a direct response to the introduction of the debt cap, so the group could not argue that reduction or elimination of a debt cap disallowance was not a main purpose. But such action would also increase (or, at any rate, not decrease) the corporation tax profits of the UK group. It would not be caught by the anti-avoidance rule.

109. The words 'profits …chargeable to corporation tax' in paragraph 48(3)(a) take their normal meaning. It is the totality of profits on which corporation tax is paid, after reduction by losses or reliefs brought forward, or group relief surrendered either by another UK company or a subsidiary in the European Economic Area. The alternative test, in paragraph 48(3)(b), is whether the losses of UK group companies, that are capable of being a carried-back or carried-forward amount, are increased. Paragraph 51 gives an exhaustive listing of 'carried-back amounts' or 'carried-forward amounts'. The latter includes capital losses.

110. A loss that has been offset against profits of the period, either in the same company or in another group company, is excluded from being a carried-back or carried-forward amount. For example, suppose that the sole effect of a scheme is to increase the corporation tax profits of UK group company X by £1 million, but also to increase the losses of company Y by £1 million. Y surrenders £1 million to X as group relief. Y's loss is therefore taken into account under paragraph 48(3)(a), and cannot be counted

again under paragraph (b). This means that neither leg of paragraph 48(3) is satisfied: the aggregate corporation tax profits of the group are not decreased, nor is there an increase in the losses capable of being carried forward or back. Even if the remaining paragraph 48 conditions are satisfied, the scheme will not be within the anti-avoidance rule. If, however, Y chooses not to surrender its loss, but instead carries it forward (or back), the condition at paragraph 48(3)(b) will be met, and the anti-avoidance rule is not prevented from applying.

111. Where the accounting period of a UK group company does not coincide with the period of account of the worldwide group, paragraph 48(5) provides for time-apportionment of those profits or losses of accounting periods which fall wholly or partly within the relevant period of account.

112. The rule that losses taken into account in determining corporation tax profits cannot also contribute to carried-back or carried-forward amounts also applies to such time-apportionments. Suppose, for example, the worldwide group has a 12-month period of account ending on 31 December. A UK member of the group prepares accounts to 31 March, so that two of its accounting periods fall partly within the relevant period. This UK company has trading losses arising in the first period, which are carried forward and relieved in the second. In applying paragraph 48(5), losses that are taken into account under paragraph 48(3)(a) because they have reduced the corporation tax profits of the second period are not also treated as ‘carried-forward amounts’ of the first period.

113. Paragraph 48(4) provides that any ‘excluded scheme’ is not caught by this anti-avoidance rule.

114. Paragraph 52 deals with schemes that manipulate the rules in Part 5 of the Schedule. Under paragraph 40, financing income received by a UK company is disregarded for corporation tax purposes where three conditions are met. Sub-paragraph (2) requires that the scheme has the effect of securing that any of these three paragraph 40 conditions are met in relation to a particular financing income amount.

115. As with the previous two anti-avoidance rules, it must be the main purpose or one of the main purposes of any party to the scheme on entering into to it to achieve this effect (sub-paragraph (3)) and the scheme must not be an excluded one (sub-paragraph (4)).

116. Sub-paragraph (5) sets out the consequence of meeting these conditions – the “manipulated” condition of paragraph 40 is treated as if had not been met, and so the financing income amount is not disregarded.

Part 7 – Financing expense amounts and financing income amounts

117. Part 7 provides what is meant by the ‘financing expense amount’ and ‘financing income amount’ of a company. These amounts are used in Part 8 to compute the ‘tested expense amount’ and ‘tested income amount’, which in turn are used, together with the ‘available amount’ (defined in Part 9) to calculate the amounts, if any, of the financing expense incurred by ‘relevant group companies’ to be disallowed and of the financing income receivable by UK group companies to be exempted. In setting the basic rules for the ‘financing expense amount’ and the financing income amount’, Part 7 includes specific rules for finance amounts arising in relation to certain activities or certain types of finance amount.

118. Paragraph 54(1) provides that a ‘financing expense amount’ of a worldwide group company for a period of account is an amount which meets one of three conditions set out in sub-paragraphs (2) to (5).

119. Sub-paragraphs (2) and (3) set condition A. Condition A is that the amount is a debit (broadly an expense) which, in the absence of the Schedule, would be brought into account for corporation tax purposes under the trade loan relationship rules in Corporation Tax Act 2009 (CTA) and which are not one of the specified excluded debits.

120. Sub-paragraph (4) deals with condition B. Condition B is that the debit is an amount which, in the absence of the Schedule, would be brought into account as a financing cost under a finance lease.

121. Sub-paragraph (5) describes condition C. This condition is that the debit is an amount which, in the absence of the Schedule, would be brought into account as a financing cost of debt factoring or a similar transaction.

122. Sub-paragraph (6) ensures that the debit or amount is reduced proportionately where the period in which it would, apart from this Schedule, be taken account of is not the same length as that of the worldwide group. Where the relevant accounting periods of the company straddle the period of account of the worldwide group, then the amounts in question are reduced proportionately.

123. Sub-paragraph (7) makes this paragraph subject to the specific rules provided by the rest of Part 7.

124. Paragraph 55 provides that, other than for the purposes of Part 5, the ‘financing income amount’ of a worldwide group company for a period of account is an amount which meets one of three conditions set out in sub-paragraphs (2) to (5). The three conditions essentially mirror the conditions for ‘financing expense amount in the previous paragraph.

125. Sub-paragraphs (2) and (3) set condition A. Condition A is that the amount is a credit (broadly income or a receipt) which would be brought into account for corporation tax purposes under the loan relationship rules in CTA and which is not one of the specified excluded credits.

126. Sub-paragraph (4) sets condition B. An amount must be an amount which would be brought into account as finance income received under a finance lease.

127. Sub-paragraph (5) sets condition C. The condition is that the amount must be an amount would be brought into account as finance income from debt factoring or a similar transaction.

128. Sub-paragraph (6) ensures that the credit or amount is reduced proportionately where the period in which it would, apart from this schedule, be taken account of is not the same length as that of the worldwide group. Where the relevant accounting periods of the company straddle the period of account of the worldwide group, then the amounts in question are reduced proportionately.

129. Sub-paragraph (7) makes the paragraph subject to the specific rules of the remainder of Part 7.

130. Paragraph 56 sets out that various terms used in paragraph 54 and 55 have the same meaning as they do in the loan relationships rules in CTA.

131. Paragraphs 57 to 69 are intended to remove particular financing expense or income amounts, referred to as the ‘relevant amounts’ within the meaning of paragraphs 54 and 55 from the calculation of a company’s net financing deduction (or in some cases net financing income) where certain conditions are met.

132. Paragraph 57 excludes the financing expense or income amounts where the company is a group treasury company during the worldwide group’s period of account, and the company so elects within three years of the end of that period

133. Sub-paragraph (4) provides where in a period the worldwide group contains more than one group treasury company, an election for the group treasury exclusion will not be valid unless each of those companies makes an election.

134. Sub-paragraphs (5) to (8) establish that a series of conditions must be met before a company can qualify as a group treasury company. Broadly, the company must;

- be a member of the worldwide group
- undertake treasury activities for that group
- where the company is the only UK group company to be a group treasury company during that period 90 per cent of the gross income from its activities (its relevant income) must be group treasury revenue, and
- where the company is not the only UK group company to be a group treasury company during the period the 90 per cent test must be applied to the aggregate gross income of the treasury companies.

135. Sub-paragraph (9) identifies the activities that must be undertaken during a period in order that a company can qualify as a group treasury company.

136. Sub-paragraphs (10) and (11) define 'group treasury revenue', while sub-paragraph (12) defines, amongst other things, 'relevant income'. The amounts are those that are accounted for using general accepted accounting practice (which is defined in section 50 FA 2004). Dividends or other distributions are not treated as group treasury revenue unless they are received from another UK group treasury company.

137. Paragraph 58 excludes financing expense amounts and financing income amounts where they are taken into account in computing profits exempted from tax by virtue of the special rules applying to Real Estate Investment Trusts. The condition for exclusion is that the financing expense amounts and financing income amounts are brought into account in computing the profits of a tax-exempt business by virtue of section 120(3)(a) Finance Act 2006.

138. Paragraph 59 excludes the financing expense or income amounts where the company is engaged in oil extraction activities within the meaning of section 502, ICTA and where the amounts in question are taken into account in calculating the company's trading profits.

139. Paragraph 60 deals with intra-group short-term financing expense. It only applies to an amount which is a finance expense of a company meeting condition A in paragraph 54. In such cases sub-paragraph (2)-(5) provide for an election for the amount not to be included as a finance expense, provided that:

- company A and the other party to the loan relationship (company B) are both members of the worldwide group, and
- the expense relates to a short-term loan relationship as defined in paragraph 62.

140. Sub-paragraph (6) requires the election to be made jointly by companies A and B within 36 months of the end of the accounting period to which the relevant amount relates. Sub-paragraph (7) provides for the election to be irrevocable.

141. Paragraph 61 deals with intra-group short-term financing income. It only applies where a finance expense amount is not treated as such by company A in accordance with paragraph 44. It is a reciprocal provision which ensures that the finance income amount of the other party to the loan ('company B') is not treated as a finance income amount.

142. Paragraph 62 provides what finance arrangements can be treated as short-term loan relationships for the purposes of this Schedule.

143. Sub-paragraph (1) defines a finance arrangement to be a short-term loan relationship if it meets either conditions set out in regulations, or meets one of the conditions provided by sub-paragraphs (2) to (3). The broad effect of these sub-paragraphs is to include loan relationships that are either required from the outset to last for less than twelve months, or where there is no fixed term, are considered to no longer exist within 12 months. A loan relationship with no fixed term can only be treated as a short-term loan relationship once it has been repaid and its character as short-term determined.

144. Sub-paragraphs (4) to (6) provide a Treasury power to make regulations, subject to affirmative resolution, about the circumstances in which finance arrangements will not be considered short-term loan relationships.

145. Sub-paragraph (7) provides a regulating power to allow the Commissioners to introduce rules that will enable minor breaches of the regulations introduced under sub-paragraph (4) to be disregarded.

146. Paragraph 63 deals with stranded deficits in non-trading loan relationships from the perspective of the company incurring the financing expense. It only applies to an amount which is a financing expense of a company meeting condition A in paragraph 54. In such cases sub-paragraph (2) provides for an election for the amount not to be included as a finance expense amount if the following conditions, set by sub-paragraphs (4)-(7) are met;

- the other party to the loan relationship ('company B') is in the same worldwide group as company A;
- company B is either resident in the United Kingdom (UK) or trading in the UK through a branch;
- company B is carrying forward an amount of non-trading deficit and sets it off against the non-trading profits of a period which overlaps with the worldwide group's period of account, and;
- The amount set off is equal to or greater than the amount excluded under this paragraph.

147. Sub-paragraph (8) provides that the election is to be made jointly by companies A and B within 36 months of the end of the accounting period to which the relevant amount relates.

148. Paragraph 64 is a reciprocal provision to paragraph 63 dealing with stranded deficits in non-trading loan relationships from the perspective of the company receiving financing income. It ensures that relevant financing income of Company B which meets Condition A in paragraph 55 is not treated as an amount of finance income where Company A elects to exclude the expense.

149. Paragraph 65 makes provision for stranded management expenses in non-trading loan relationships from the perspective of the company incurring the financing expense. The paragraph applies only to an amount which is a finance expense of a company meeting Condition A in paragraph 54. In such cases sub-paragraph (2) provides for an election for the amount not to be included as a finance expense if the following conditions, set by sub-paragraphs (4)-(8) are met;

- the other party to the finance arrangement ('company B') is in the same worldwide group as company A;
- company B must have an investment business and be either resident in the UK or trading in the UK through a branch;
- company B is allowed a deduction for management expenses under section 1219 CTA in an accounting period which overlaps with the worldwide group's period of account;
- the amount of the deduction is equal to or greater than the relevant amount, and;
- company B would make a loss for corporation tax purposes in that accounting period if the credit corresponding to company A's debit within paragraph 54 is not included in that computation.

150. Sub-paragraph (9) provides that the election must be made jointly by companies A and B within 36 months of the end of the accounting period to which the relevant amount relates.

151. Paragraph 66 is a reciprocal provision to paragraph 65 and deals with stranded management expenses in non-trading loan relationships from the perspective of the company receiving the financing income. It ensures that relevant financing income of company B which meets condition A in paragraph 55 is not treated as an amount of finance income where company A elects to exclude the expense.

152. Paragraphs 67 and 68 exclude relevant amounts paid to charities, designated educational establishments, health service bodies and local authorities from being taken into account in computing any disallowance under the Schedule. This prevents a disallowance being made where a corresponding disregard of amounts receivable is not available because of the tax status of the receiving body.

153. The definition of 'charity' is given as any body of persons or trust established for charitable purposes only. The meanings of 'designated educational establishment' and 'health service body' are given by section 105 of CTA and section 519A of ICTA respectively.

154. The provisions include a regulation-making power to allow the Commissioners to add other public bodies to the list of entities to which payments will be disregarded.

155. Paragraph 69 provides certain defined terms for the purposes of Part 7.

Part 8 – The 'tested expense amount' and 'tested income amount'

156. Part 8 sets out how two key amounts, the 'tested expense amount' and the 'tested income amount are to be calculated.

157. The 'tested expense amount' must be calculated so that, by comparison with the 'available amount' dealt with in Part 8, it may be determined whether the adjustments provided for by Parts 3 and 4 are necessary. The 'tested income amount' is required in calculating the amount of financing income to be exempted from corporation tax by Part 4.

158. Paragraph 70 (1) provides that the 'tested expense amount' for a worldwide group is built up from the sum of each relevant group company's 'net financing deduction'.

159. Sub-paragraphs (2) and (3) explain that the 'net financing deduction' of a company for a period of account is the excess of the company's 'financing expense amounts' over its 'financing income amounts'. Any amounts arising to a company as a result of a transaction which took place when it was not a relevant group company are ignored for this purpose. A transaction in this context means an amount of financing expense or income that is payable or receivable.

160. Sub-paragraph (4) specifies that if the computation of the 'net financing deduction' produces a negative figure, the amount is treated as nil.

161. Sub-paragraph (5) provides that if the 'net financing deduction' is small, as defined by the de minimis limit set by paragraph 72, then the amount is treated as nil.

162. Paragraph 71 contains provision about the tested income amount. Sub-paragraph (1) provides that the 'tested income amount' for a worldwide group is built up from the sum of each UK group company's 'net financing incomes'.

163. Sub-paragraphs (2) and (3) provide that the 'net financing income' of a company for a period of account is the excess of the company's 'financing income amounts' over its 'financing expense amounts'. Any amounts arising to a company as a result of a transaction which took place when it was not a UK group company are ignored for this

purpose. A transaction in this context means an amount of financing expense or income that is payable or receivable.

164. Sub-paragraphs (4) and (5) provide for the 'net financing income' to be treated as nil if the computation produces a negative figure or an amount which is small as defined in Paragraph 72.

165. Paragraph 72 provides that the figure used to determine whether a relevant group company's net financing deduction is small, or whether a UK group company's net financing income is small, is £500,000.

166. Sub-paragraphs (2)-(4) provide for this amount to be increased or decreased by Treasury order, subject to affirmative resolution, with prospective effect.

Part 9 –Calculation of the available amount

167. Part 9 deals with the computation of the 'available amount', which in broad terms is the external gross finance expense of the worldwide group of companies. This Part sets out the basic rules for computing the 'available amount', and provides for the external financing expense arising from certain activities to be disregarded in calculating the available amount.

168. Paragraph 73 provides that the 'available amount' for a period of account of the worldwide group is derived from amounts disclosed in the group's financial statements for that period.

169. Sub-paragraph (1) provides a list of the amounts to be included.

170. Sub paragraphs (1)(a) – (1)(d) cover interest and amortised discounts and premiums, together with the ancillary costs of borrowing. Subparagraph (1)(e) refers to financing costs implicit in payments under finance leases. This is intended to cover the interest or finance element of finance lease payments. . Sub-paragraph (1)(f) covers the financing costs relating to debt factoring. Sub-paragraph (1)(g) enables further types of financing costs to be designated as falling within the 'available amount' by regulation.

171. Sub-paragraph (2) excludes from the available amount dividends arising from preference shares (whether those shares are redeemable or non-redeemable) to the extent that those shares are recognised as a liability of the group.

172. Paragraph 74 excludes from the available amount financing costs arising from oil extraction activities if a member of the group is treated as carrying out a separate trade of oil extraction activities, as defined by section 502 of ICTA and the financing costs under consideration are taken into account when calculating the profits of that oil extraction trade for corporation tax purposes.

173. Paragraph 75 excludes from the available amount financing costs relating to profits which are dealt with under the tonnage tax regime provided two conditions are met.

174. Sub-paragraph (2) provides that the group company must be a tonnage tax company for the purposes of the UK tonnage tax regime.

175. Sub-paragraph (3) provides that the external finance amount has been taken into account in calculating the relevant shipping profits of the tonnage tax company or is treated as a non-trading loan relationship credit of the company or companies outside the ring fence under paragraphs 61 or 62 of Schedule 22 to FA 2000.

176. Paragraph 76 excludes from the available amount financing costs relating to profits exempted from corporation tax by virtue of the special rules applying to Real Estate Investment Trusts. The conditions for exclusion are that a group company is treated as carrying out a separate business under section 113 of FA 2006 and that the external finance amount is brought into account in calculating the profits of that separate tax exempt business.

177. Paragraph 77 confirms that in the absence of any contrary provision, expressions used in Part 9 have the meaning given by IAS.

Part 10 – Other Interpretative provisions

178. Part 10 contains the rules that define which companies make up a group for the purpose of this Schedule and which companies are treated as 'relevant group companies' and 'UK group companies'. This part also explains which accounting standards used to prepare the group consolidated financial statements are acceptable for this Schedule and provides for cases where no such financial statements are prepared.

179. Paragraph 78 defines 'the worldwide group' as any group of entities that is large (see Paragraph 85) and contains at least one company that is tax resident in the UK.

180. Paragraph 79 provides that the term 'group' takes it meaning from IAS. This establishes that the 'worldwide group' defined in paragraph 78 will in the majority of cases be the group of companies whose results are included in the consolidated accounts of the group headed by the ultimate parent.

181. Paragraph 79(3) excludes an entity that is a parent of the ultimate parent of a group from being a member of that group. This means that, unless otherwise provided, the worldwide group whose finance expenses will be compared with the finance expenses of UK members of the group will be limited to the ultimate parent and its subsidiaries.

182. Paragraph 80 defines the 'ultimate parent'. The ultimate parent is a member of a group that is either an entity treated as a 'corporate entity' or a 'relevant non-corporate entity' for the purposes of the Schedule and which is not itself a subsidiary of a corporate entity or a relevant non-corporate entity or a collective investment scheme. A group may contain a number of intermediate parent companies and this rule is intended to identify the top parent company in the group.

183. Paragraph 81 provides that for the purposes of the Schedule a 'corporate entity' is either a body corporate under the law of the UK or any other territory, or any another entity that meets two conditions. The two conditions in sub-paragraphs (2) and (3) are formulated by reference to essential characteristics of a body corporate.

184. Sub-paragraph (4) excludes the UK and foreign governments from the definition of 'corporate entity'.

185. Paragraph 82 defines 'relevant non-corporate entity'. Some publicly listed entities that are not corporate entities can be the ultimate parent of a worldwide group. A "relevant non-corporate entity" must have shares or other interests that are listed on a recognised stock exchange and sufficiently widely held.

186. Paragraph 83 provides that where interests in a corporate or relevant non-corporate entity are stapled to another entity they will be treated as a single corporate or non-corporate entity for the purposes of the Schedule. This provides that the stapled entities and their respective subsidiaries will together be treated as one worldwide group. Subparagraph (3) defines 'stapled' by reference to the nature of the rights attaching to the shares or other interests which one entity has in another.

187. Paragraph 84 treats entities as one corporate entity for the purposes of the Schedule where international accounting standards treat them as a single economic entity by reason of being a business combination achieved by contract. This covers dual headed groups which are not accounted for as an acquisition.

188. Paragraph 85 defines large groups by excluding micro, small and medium enterprises as defined in the Annex to European Commission Recommendation 2003/361/EC of 6 May 2003.

189. Sub-paragraphs (1) and (2) incorporate the Annex for the purposes of deciding whether a business is micro, small or medium sized at any time, with certain qualifications. The

effect of paragraph 85(1) is that provided at least one member of the worldwide group is a large company by reference to the definition in the Annex, then the worldwide group is large and the Schedule applies to all the UK members of that group that satisfy the definition of relevant group company.

190. Sub-paragraph (3) provides that the rights and powers of liquidators and administrators will not by themselves result in the loss of an exemption for small and medium sized enterprises under their charge. The Annex provides qualifying ceilings for staff and financial limits. In order to see if a business meets these ceilings, its own data must be aggregated with the data for associated businesses. This paragraph ensures that aggregation is not required by virtue solely of the appointment of a liquidator or administrator.

191. Sub-paragraph (4) removes the option to make a declaration of status when a business cannot ascertain the extent of control over its associated businesses when aggregating data.

192. Sub-paragraphs (5) and (6) simplify the application of the recommendation when deciding whether a business will qualify as small or medium. Qualification will depend on a business's data for each chargeable period without reference to past history. This simplification also means that it is not necessary to provide additional start-up rules for new businesses.

193. Paragraph 86 defines 'UK group company' and 'relevant group company'.

194. Sub-paragraph (2) provides that a UK group company is one which is

- a UK resident company or a company carrying on a trade in the UK through a branch (see sub-paragraph (4)), and
- a member of the worldwide group. It is a member of the worldwide group if it a subsidiary of the ultimate parent.

195. Sub-paragraph (3) provides that a relevant group company is a UK group company which is:

- a UK resident company or a company carrying on a trade in the UK through a branch (see sub-paragraph (4)), and is either
- the ultimate parent of the group, or a relevant subsidiary of the ultimate parent (see sub-paragraph (5)).

196. Sub-paragraph (6) provides that the relevant subsidiary condition is based on the 75% subsidiary test used for group relief. It is supplemented by rules that ensure that a company is also treated as a relevant subsidiary of an ultimate parent where that entity is beneficially entitled to at least 75% of the profits which are available for distribution to equity holders, or 75% of the assets which are available for distribution to equity holders in the course of a winding up.

197. Paragraph 87 provides for which consolidated financial statements of the worldwide group are used in applying the Schedule and provides that the period of account of the worldwide group is the period for which those accounts are drawn up. Amounts disclosed in the financial statements of the worldwide group for a period form the basis of the amount against which the Schedule compares the net finance deductions of UK members of the group to calculate the amount of any disallowance.

198. Paragraph 88 applies where the consolidated financial statements of the worldwide group for a period are not 'acceptable' and the amounts disclosed in those financial statements are materially different from those that would have been disclosed under IAS. Where the paragraph applies, the Schedule will apply as if the group had prepared consolidated financial statements under IAS for the period.

199. Sub-paragraph (3) provides that financial statements are ‘acceptable’ if:

- they are drawn up in accordance with international accounting standards;
- they meet conditions relating to accounting standards, principles or practice that the Commissioners may specify in regulations; or
- they meet the conditions set out in sub-paragraphs (4) to (6)

200. Sub-paragraphs (4) to (6) set out conditions A to C that financial statements must meet in order to be acceptable. They are that:

- (Condition A) the companies whose results are included in the financial statements must be the same as those that would have been included in financial statements drawn up under IAS; and
- (Condition B) the transactions whose results are relevant to the computation of the available amount under Part 9 included in the financial statements must be the same as those that would have been included in financial statements drawn up under IAS; and
- (Condition C) the amounts which are relevant to the computation of the available amount under Part 9 which are taken from those financial statements are calculated using the effective interest method.

201. Paragraph 89 provides how the Schedule will apply where consolidated financial statements of an ultimate parent and its subsidiaries are not prepared. The paragraph provides that the Schedule will apply as if financial statements had been drawn up under IAS. That is, the Schedule will apply on the basis that particular amounts taken into consideration in Part 9 (calculation of the available amount) will be those that would have been disclosed had the group drawn up consolidated financial statements in accordance with IAS.

202. Sub-paragraphs (2) – (4) provide rules that establish the period of account for the worldwide group where no consolidated financial statements are prepared.

203. Paragraph 90 sets out what is meant by ‘amounts disclosed in group’s financial statements’. Such amounts may include amounts comprised in a larger disclosed amount, and include an amount disclosed in a joint venture that is a member of the group, however presented. Sub-paragraph (2) excludes capitalised amounts that are disclosed in the financial statements of the group for a period where they have already been included in the balance sheet of the group for an earlier period. Sub-paragraph (3) excludes amounts in respect of group pension schemes or any entity that is not a member of the group.

204. Paragraph 91 deals with the currency denomination: all non-sterling denominated amounts are to be converted into sterling at the average rate of exchange for that accounting period.

205. Paragraph 92 provides for specified terms within the Schedule to take their meaning for the purposes of the Schedule from the definition given to them, for the time being, by IAS.

206. Sub-paragraph (2) provides that the paragraph may be amended by regulation.

207. Paragraph 93 defines a ‘relevant accounting period’ of a company as any accounting period that fall wholly or partly within the period of account of the worldwide group.

208. Paragraph 94 defines ‘the Commissioners’, ‘the FSA Handbook’ and ‘HMRC’ for the purposes of the Schedule.

Part 11 – Consequential Amendments and Commencement

209. Paragraph 95 adds regulations made under paragraphs 24 to 26, 36 and 38 of this Schedule, which deal with the allocation of disallowed amounts and exempt amounts, to the list of specified provisions given in section 98 of the Taxes Management Act 1970. Failure to comply with a notice given under a provision specified in section 98 may result in a penalty as set out in that section.

210. Paragraph 96 makes the amendment necessary to ensure that the transfer pricing rules at Sch 28AA ICTA take priority over the Schedule. This ensures that adjustments to financing income made under the Schedule will not be reinstated by transfer pricing rules. It also ensures that financing expenses disallowed under the Schedule cannot also be disallowed by the transfer pricing rules.

211. Paragraph 97 gives the commencement rule for the Schedule, which, subject to paragraph 98, takes effect for periods of account of the worldwide group that begin on or after 1 January 2010. The periods of account of the worldwide group are defined in paragraph 87(3) by reference to the consolidated financial statements of the ultimate parent of the group.

212. Paragraph 98 provides an anti-avoidance rule to prevent the ultimate parent of a worldwide group manipulating its accounting date to take advantage of the commencement provisions at paragraph 97. By moving its accounting date from 31 December 2009 to 30 December 2009, a group would ensure that the Schedule did not apply to it for a further 12 months. Paragraph 98 applies where the main purpose, or one of the main purposes, of a group changing its accounting date is to achieve such a result. Its effect is to apply the provisions of Schedule 15 to the accounting period beginning immediately after the changed accounting date.

213. Paragraph 99 explains how the Schedule will deal with amounts that accrue in the financial statements of a company for a period, but are not brought into account for corporation tax purposes until a later period. If those amounts would have been brought into account for the purposes of corporation tax in a period beginning before 1 January 2010 but for one of the statutory provisions listed in sub-paragraph (2), they cannot be treated as either financing expense amounts or financing income amounts of the company. This ensures that the provisions of the Schedule can only apply to amounts that accrued in periods in respect of which the Schedule has effect.