
STATUTORY INSTRUMENTS

2004 No. 3270

The Finance Act 2002, Schedule 26, Parts
2 and 9 (Amendment No. 2) Order 2004

Amendments of Part 9 of Schedule 26

10. After paragraph 45I insert—

“Issuers of securities with embedded derivatives: deemed options

45J.—(1) This paragraph applies to a derivative contract of a company for an accounting period if the following conditions are satisfied—

- (a) section 94A of the Finance Act 1996⁽¹⁾ (loan relationships with embedded derivatives) has effect in relation to a debtor relationship of the company,
- (b) the derivative contract is the relevant contract, or one of the relevant contracts, to which the company is treated under subsection (2)(b) of that section as party in the case of that debtor relationship,
- (c) that relevant contract is treated by virtue of subsection (3) of that section as an option,
- (d) the additional conditions in sub-paragraph (2) are satisfied,

(2) The additional conditions are—

- (a) at the time when the company became party to the debtor relationship—
 - (i) it was not carrying on a banking business or a business as a securities house, or
 - (ii) if it was carrying on such a business, it did not become party to the debtor relationship in the ordinary course of that business,
- (b) the derivative contract is not one to which any of paragraphs 6 to 8 applies,
- (c) the underlying subject matter of the derivative contract is shares,
- (d) the company is not a body falling within paragraph 45C(3) (authorised unit trusts etc).

(3) Where this paragraph applies to a derivative contract for an accounting period—

- (a) paragraph 14(3) (non-trading credits and debits) shall not apply to the credits and debits given in relation to the contract for the accounting period by paragraph 15, but
- (b) sub-paragraph (5), (7) or (9) (as the case may be) of this paragraph shall, subject to sub-paragraph (4), apply instead.

(4) Sub-paragraphs (5), (7) and (9) do not apply where the company is a party to the debtor relationship mentioned in sub-paragraph (1) immediately before the first accounting period to which this paragraph applies.

⁽¹⁾ 1996 c. 8, section 94A was inserted by paragraph 13 of Part 1 of Schedule 10 to the Finance Act 2004.

(5) This paragraph applies if—

- (a) the option mentioned in sub-paragraph (1)(c) is exercised at any time in an accounting period, and
- (b) shares are issued or transferred in fulfilment of the obligations under the option (the “relevant disposal”)

and where it applies, section 144(2) of Taxation of Chargeable Gains Act 1992 (exercise of options) applies to the relevant disposal as if the amount treated in accordance with section 94A(2) of the Finance Act 1996 as the carrying amount of the option at the time the company became party to the loan relationship (the “initial carrying amount”) was the consideration for the grant of the option.

(6) Sub-paragraph (7) applies if—

- (a) the option mentioned in sub-paragraph (1)(c) is exercised at any time in an accounting period,
- (b) there is no relevant disposal, and
- (c) an amount is paid in fulfilment of the obligations under the option.

(7) Where this sub-paragraph applies—

- (a) if E exceeds F, a chargeable gain equal in amount to the amount of the excess shall be treated as accruing to the company in the accounting period,
- (b) if F exceeds E, an allowable loss equal in amount to the amount of the excess shall be treated as accruing to the company in the accounting period,

(8) In sub-paragraph (7)—

E is the initial carrying amount of the option;

F is the amount paid in fulfilment of the obligations under the option reduced by the aggregate of—

- (a) the initial carrying amount of the option and
- (b) the carrying amount of the host contract (within the meaning of section 94A of the Finance Act 1996) at the time the company became party to the loan relationship.

(9) This paragraph applies if the debtor relationship comes to an end at a time when the option mentioned in sub-paragraph (1)(c) has not been exercised, and where it applies the company is treated for the purposes of corporation tax on chargeable gains as having disposed of the option for a consideration equal to the initial carrying amount.

(10) In this paragraph—

“option” has the same meaning as in paragraph 12, apart from sub-paragraph (10);

“securities house” means a person—

- (a) who is authorised for the purposes of the Financial Services and Markets Act 2000, and
- (b) whose business consists wholly or mainly of dealing as a principal in financial instruments within the meaning of section 349(5) and (6) of the Taxes Act 1988.

Issuers of securities with embedded derivatives: deemed contracts for differences

45K.—(1) This paragraph applies to a derivative contract of a company for an accounting period if the following conditions are satisfied—

- (a) section 94A of the Finance Act 1996 (loan relationships with embedded derivatives) has effect in relation to a debtor relationship of the company,

- (b) the derivative contract is the relevant contract, or one of the relevant contracts, to which the company is treated under subsection (2)(b) of that section as party in the case of that debtor relationship,
 - (c) the relevant contract is treated by virtue of subsection (3) of that section as a contract for differences (other than one which falls within paragraph 45J), and
 - (d) the derivative contract is an exactly tracking contract within the meaning of paragraph 45F, and
 - (e) the additional conditions in sub-paragraph (2) are satisfied.
- (2) The additional conditions are—
- (a) at the time when the company became party to the debtor relationship—
 - (i) it was not carrying on a banking business or a business as a securities house, or
 - (ii) if it was carrying on such a business, it did not become party to the debtor relationship in the ordinary course of that business,
 - (b) the derivative contract is not one to which any of paragraphs 6 to 8 applies,
 - (c) the underlying subject matter of the derivative contract is land (wherever situated) or shares,
 - (d) the company is not a body falling within paragraph 45C(3) (authorised unit trusts etc).

(3) Where this paragraph applies to a derivative contract for an accounting period, paragraph 14(3) (non-trading credits and debits) shall not apply to credits and debits given in relation to the contract for the accounting period by paragraph 15.

(4) In this paragraph “securities house” has the same meaning as in paragraph 45J (see sub-paragraph (10) of that paragraph).

Derivatives not embedded in a loan relationship

45L.—(1) Where—

- (a) a company is treated under paragraph 2(4) as party to a derivative contract, and
- (b) regulation 9 of the Disregard Regulations (interest rate contracts) does not apply to the contract,

paragraph 14(3) (non-trading credits and debits) shall not apply to credits and debits given in relation to the fair value profits and losses arising on the contract.

(2) Where paragraph (1) applies, then notwithstanding paragraph 1(2) of this Schedule, profits and losses are to be brought into account in relation to the host contract for the purposes of the Corporation Tax Acts as if the derivative contract embedded in the host contract were treated for accounting purposes as closely related to the host contract.

(3) In this paragraph “the Disregard Regulations” means the Loan Relationships and Derivative Contracts (Disregard and Bringing into Account of Profits and Losses) Regulations 2004(2).”