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Amendment 66

Schedule 6, page 185, line 5 [Vol I], leave out sub-paragraph (1) and insert –

‘(1) After section 85B of FA 1996 (amounts recognised in determining company’s profit or loss) insert -

“85C Amounts not fully recognised for accounting purposes

(1) This section applies if -

- (a) a company is, or is treated as being, a party to a creditor relationship in any period,
- (b) an amount is not fully recognised for the period in respect of the creditor relationship,
- (c) the company is, or is treated as being, a party to a debtor relationship in the period or has at any time issued share capital which falls to be treated for accounting purposes as a liability (a “relevant accounting liability”) for the period,
- (d) an amount is not fully recognised for the period in respect of the debtor relationship or relevant accounting liability, and
- (e) the amounts are not fully recognised as mentioned in paragraphs (b) and (d) as a result of the application of generally accepted accounting practice in relation to the creditor relationship and the debtor relationship or relevant accounting liability.

(2) For the purposes of subsection (1) an amount is not fully recognised for the period in respect of any loan relationship or relevant accounting liability of the company if -

- (a) no amount in respect of the relationship or liability is recognised in determining its profit or loss for the period, or

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- (b) an amount in respect of only part of the relationship or liability is recognised in determining its profit or loss for the period.
- (3) In determining the credits and debits to be brought into account by the company in respect of the creditor relationship for the period for the purposes of this Chapter, the applicable assumption (see subsection (6)) must be made.
- (4) In any case where the condition in subsection (1)(c) is met by reference to a debtor relationship of the company, in determining the credits and debits to be brought into account by the company in respect of that relationship for the period for the purposes of this Chapter, the applicable assumption must be made.
- (5) But the amount of any debits to be brought into account by the company for any period for the purposes of this Chapter as a result of subsection (4) must not exceed the amount of any credits to be brought into account by the company for the period as a result of subsection (3).
- (6) For the purposes of this section, in relation to any loan relationship, the applicable assumption is the assumption that an amount in respect of the whole of the relationship is recognised in determining the company's profit or loss for the period.
- (7) In any case where -
- (a) apart from this section any credits or debits are brought into account by the company in respect of any loan relationship for the period for the purposes of this Chapter, and
- (b) the relationship is one to which this section applies, the credits and debits to be so brought into account as a result of this section must be determined on the same basis of accounting on which the credits or debits mentioned in paragraph (a) were determined.
- (8) In any other case, the credits and debits to be so brought into account as a result of this section must be determined on the amortised cost basis of accounting.”’.

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SUMMARY

1. This amendment substitutes a new paragraph 6(1) of Schedule 6 to the Bill, which inserts a new section 85C into Finance Act (“FA”) 1996.
2. Section 85C deals with certain cases where the accounting treatment causes profits on loan relationships not to be recognised, and so fall out of account for tax purposes.

DETAILS

3. Amendment 66 substitutes a new paragraph 6(1) into Schedule 6 to the Finance Bill. Paragraph 6(1) inserts a new section 85C into FA 1996.
4. Section 85C(1) FA 1996 sets out the case, and is where –
 - a company is a party to a creditor loan relationship (i.e. an debt asset) in any period or is treated as being a party (for instance by virtue of section 100 FA 1996 (money debts treated as loan relationships in certain circumstances))
 - an amount in respect of the asset is not fully recognised in the accounts of the company (see note on subsection (2) below defining this term),
 - the company is, or is treated as being, a party to a debtor relationship (i.e. it owes a debt liability) in the period or has at any time issued share capital which falls to be accounted for as a liability. This latter type of liability is called a “relevant accounting liability”.
 - an amount is not fully recognised for the period in respect of the debtor relationship or the relevant accounting liability
 - amounts are not fully recognised as mentioned in paragraphs (b) and (d) because of the application of generally accepted

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accounting practice (e.g. FRS 5) in relation to both asset and liability.

5. Section 85C(2) FA 1996 defines what is meant by an amount not being fully recognised for the period. It is not so recognised if –
 - no amount at all in is recognised in determining profit or loss for the period (i.e. the asset or liability and any profit or loss from it are wholly absent from the accounts) or
 - an amount in respect of part only of the relationship or liability is recognised in determining profit or loss for the period.
6. Section 85C(3) FA 1996 provides that in determining the credits and debits to be brought into account for the purposes of Chapter 2 Part 4 FA 1996 (the loan relationships legislation) in respect of the asset creditor relationship for the period, the applicable assumption must be made (see paragraph 8 below).
7. Section 85C(4) FA 1996 provides that where the relevant liability is a debtor relationship of the company (but not a share treated as a relevant accounting liability) then the applicable assumption must also be made in determining those credits and debits in relation to that debtor relationship.
8. Section 85C(6) FA 1996 says that the applicable assumption is the assumption that an amount in respect of the whole of the relationship is recognised in determining the company's profit and loss for the period for the purposes of Chapter 2 Part 4 FA 1996.
9. Section 85C(5) FA 1996 ensures that where the section requires additional amounts to be brought into account, the amount of any additional debits arising under subsection (4) are not to exceed the amount of any additional credits arising under subsection (3).
10. Section 85C(7) FA 1996 provides that where, apart from this section, any credits or debits are brought into account in respect of a relationship to which the section applies (i.e. in a case where part only of the loan relationship is not recognised in the accounts), then any additional credits and debits brought into account as a result of

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the section must be determined on the same basis of accounting as is used in the accounts for the part actually recognised.

11. Section 85C(8) FA 1996 provides that in any other case (i.e. where no amount is recognised), the additional credits and debits to be brought into account as a result of the section must be determined on an amortised cost basis of accounting. This is without prejudice to any other provisions of Chapter 2 requiring an adjustment, for example making fair value accounting mandatory for tax purposes.

BACKGROUND NOTE

12. The loan relationships regime in Chapter 2 Part 4 FA 1996 taxes all profits and gains arising to a company from its loan relationships.
13. The amounts to be brought into account for a period are those that, in accordance with generally accepted accounting practice, are recognised in determining the company's profit and loss for the period.
14. In certain circumstances, generally accepted accounting practice provides for assets and liabilities to be de-recognised. If the asset is a loan relationship, accounting de-recognition would mean that profits and losses in respect of that relationship would fall out of the charge to tax.