**EXPLANATORY MEMORANDUM TO**

**THE LOAN RELATIONSHIPS AND DERIVATIVE CONTRACTS (CHANGE OF ACCOUNTING PRACTICE) (AMENDMENT) REGULATIONS 2005**

**2005 No. 3383**

**1.** This explanatory memorandum has been prepared by the Her Majesty's Commissioners of Revenue and Customs and is laid before the House of Commons by Command of Her Majesty.

## 2. Description

2.1 The regulations provide for spreading over 10 years, for tax purposes, profits and losses arising as a result of a company's transition from following existing UK Generally Accepted Accounting Practice (GAAP) to following International Accounting Standards (IAS) or revised UK GAAP.

2.2 They also make further amendments to SI 2004/3271 to cater for certain interest rate contracts

## 3. Matters of special interest to the Select Committee on Statutory Instruments

3.1 None

## 4. Legislative Background

4.1 The power to make the regulations is in section 85B(3) and (5) of, and paragraph 19B of Schedule 9 to, the Finance Act 1996 and paragraph 17C of Schedule 26 to the Finance Act 2002. These provisions allow certain profits and losses from loan relationships and derivative contracts to be left out of account, to be brought into account in a different way or to be brought into account at a later date. In addition paragraph 52 of Schedule 4 to the Finance Act 2005 (also cited) permits the regulations to have effect for the accounting periods in which they are made.

## 5. Extent

5.1 The instrument applies to all of the United Kingdom.

## 6. European Convention on Human Rights

6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

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## 7. Policy background

7.1 Profits and losses on debts and derivative contracts are generally brought into account as they are recognised in accounts drawn up using UK Generally Accepted Accounting Practice (GAAP). From 2005 all companies will be permitted to use International Accounting Standards (IAS) to draw up their

accounts, and such accounts will be an acceptable basis for tax purposes – section 50 of the Finance Act 2004.

7.2 Where a company changes its accounting basis, any difference between the carrying value of the asset or liability between the period of change and the previous period are brought into account for tax purposes in the period of change. In this particular case, the change to IAS in 2005, the amounts involved are both potentially very large and difficult to quantify. By the Loan Relationships and Derivative Contracts (Change of Accounting Practice) Regulations 2004 (SI 2004/3271) the tax effect of the adjustments was deferred to 2006 until reliable figures were available. In the light of the figures the Government has decided to spread the adjustments over 10 years starting in 2006 for most companies, and in 2007 for banks and Building Societies in relation to dormant account balances.

## 8. Impact

8.1 A Regulatory Impact Assessment has not been prepared for this instrument as it has no impact on small business, charities or voluntary bodies.

8.2 The impact on the public sector is nil.

## 9. Contact

Josephine Crimmin at Her Majesty's Revenue & Customs, telephone 020 7147 2543 or e-mail josephine.crimmin@hmrc.gsi.gov.uk can answer any queries regarding the instrument.