

Foreign currency assets and chargeable gains

Who is likely to be affected?

Companies making non-exempt share disposals which have a functional currency other than sterling, or at some time during the period of ownership of the shares had a functional currency other than sterling, or which have made a designated currency election.

General description of the measure

The measure simplifies the calculation of chargeable gains on share disposals for companies which have, or have had, a functional currency other than sterling and for investment companies which have made a designated currency election. Most of these companies will be multinational inward investors.

Such companies will be required to use their functional currency, or in certain circumstances their designated currency, to compute any chargeable gains and losses on disposals of shares not covered by the substantial shareholdings exemption.

Policy objective

The measure contributes to the Government's objective of a fairer tax system by more closely aligning economic outcomes with tax outcomes. Currently, foreign exchange movements against sterling can give rise to gains or losses in chargeable gains computations. This is because profits or losses may arise from the requirement to convert the non sterling acquisition costs and disposal proceeds of shares into sterling if, as is likely, different exchange rates apply at the relevant dates.

Closer alignment with economic outcomes should reduce barriers to commercial decision making by businesses faced with tax gains not matched by a gain of economic substance and reduce administrative burdens for businesses attempting to manage the effects of such gains.

Detailed proposal

Operative date

The measure will have effect for disposals of shares by relevant companies on and after the date that Finance Bill 2013 receives Royal Assent.

Current law

Section 5 of the Corporation Tax Act 2010 (CTA 2010) provides that chargeable gains must be computed in sterling. Unlike for computations of income profits, there are no exceptions to the rule for chargeable gains.

Therefore, even when a company operates entirely in a non-sterling environment, it must translate its costs and proceeds into sterling for the purpose of computing any chargeable gain or loss. This can result in chargeable gains and losses arising (or increasing/decreasing) simply due to changes in foreign exchange rates, between the company's operating currency and sterling, during the period of ownership of the shares.

Proposed revisions

Legislation will be introduced in Finance Bill 2013 to change the chargeable gains computation for share disposals by companies which have a functional currency other than sterling, or at some time during the period of ownership of the shares had a functional

currency other than sterling, or companies which have made a designated currency election (under section 9A CTA 2010).

Companies will be required to compute their chargeable gains and losses using their functional currency at the date of disposal. Any chargeable gain or loss will then be translated into sterling using the exchange rate at the date of disposal.

There is an exception for investment companies which have made a designated currency election. These companies will be required to use their designated currency if the designated currency is the functional currency the company would have had if it was a standalone entity. If the designated currency and standalone functional currency differ, these companies must use their actual functional currency, like all other companies.

There will be special rules for recalculating the base cost of the shares when the functional currency of the company holding the shares changes. This might happen because a change in the facts and circumstances in which the holding company operates causes the functional currency to change, or it could be due to the company changing its accounting standards. It would also happen when shares are transferred intra-group between two companies with different functional currencies.

Summary of impacts

Exchequer impact (£m)	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
	-	negligible	negligible	negligible	negligible	negligible
	This measure is expected to have a negligible impact on the Exchequer. Any impact will be set out at Budget 2013.					
Economic impact	The measure is not expected to have any significant economic impacts.					
Impact on individuals and households	This measure will have no impact on individuals or households.					
Equalities impact	This measure is not expected to have an equality impact on people with any protected characteristic.					
Impact on business including civil society organisations	<p>This measure is expected to have a negligible impact on businesses or civil society organisations. It applies to multinational companies which have a functional currency other than sterling, of which, fewer than 500 are affected.</p> <p>Each company will only be affected in years they dispose of non-exempt shares. The one-off costs will be negligible and limited to reading/understanding the new legislation. Ongoing savings are negligible with some savings due a simpler chargeable gains computation.</p>					
Operational impact (£m) (HMRC or other)	This measure is will have a negligible operational impact.					
Other impacts	Other impacts have been considered and none have been identified.					

Monitoring and evaluation

This measure will be kept under review through communication with affected taxpayer groups.

Further advice

If you have any questions about this change, please contact Ellen Milner on 020 7147 3961 (email: ellen.milner@hmrc.gsi.gov.uk).

1 Currency used in tax calculations: chargeable gains and losses

- (1) Chapter 4 of Part 2 of CTA 2010 (currency) is amended as follows.
- (2) In section 5 (basic rule: sterling to be used), after subsection (2) insert –
 - “(3) See section 9C for provision about the application of subsection (1) so far as it relates to calculating chargeable gains.”
- (3) After section 9B insert –

“9C Chargeable gains and losses of companies

- (1) This section applies if –
 - (a) a company disposes of shares, and
 - (b) at any time beginning with the company’s acquisition of the shares (or, if earlier, the time allowable expenditure was first incurred in respect of the shares) and ending with the disposal, the company’s relevant currency is not sterling.
- (2) A company’s relevant currency at any time is its functional currency at that time, subject to subsection (3).
- (3) If, at any time –
 - (a) a company is a UK resident investment company,
 - (b) the company has a designated currency (see sections 9A and 9B) which is different from its functional currency, and
 - (c) the company’s designated currency and functional currency would be the same if the company were not a member of any group (or, if the company is not a member of any group, its designated currency and functional currency are the same),the company’s relevant currency at that time is that designated currency.
- (4) If the relevant currency of the company at the time of the disposal is not sterling, the chargeable gain or loss accruing to the company on the disposal must be calculated as follows –
 - Step 1*
Calculate the chargeable gain or loss in the relevant currency of the company at the time of the disposal.
 - Step 2*
Take the sterling equivalent of the chargeable gain or loss at that time.
- (5) In any case, subsections (6) to (9) apply for the purposes of calculating the chargeable gain or loss.
- (6) Where any allowable expenditure is incurred in a currency which is not the company’s relevant currency at the time it is incurred, that expenditure is to be translated into that relevant currency by reference to the spot rate of exchange for the day on which it is incurred.
- (7) Where, at any time after any allowable expenditure is incurred but before the shares are disposed of, there is a change in the company’s relevant currency, that expenditure is to be translated (or, if it has previously been translated under this section, further translated) into the relevant currency of the company immediately following the

change, by reference to the spot rate of exchange for the day of the change.

- (8) Any amount of consideration for the disposal which is given in a currency other than the company's relevant currency is to be translated into that relevant currency by reference to the spot rate of exchange on the day of disposal.
- (9) For the purposes of subsections (6) and (7) –
 - (a) any translation of expenditure under subsection (6) is to be done before any translation of the expenditure under subsection (7), and
 - (b) if subsection (7) applies as a result of more than one change in the company's relevant currency, it is to be applied in relation to each change in the order the changes were made (with the earliest first).
- (10) Where, by virtue of any enactment, the company was at any time treated for the purposes of corporation tax on chargeable gains as acquiring the shares –
 - (a) for a consideration of such amount as would secure that neither a gain nor a loss would accrue to the person disposing of the shares, or
 - (b) for a consideration equal to the market value of the asset,for the purposes of this section that allowable expenditure is treated as incurred by the company at that time.
- (11) In this section –
 - “allowable expenditure” means expenditure which, immediately before the disposal, was attributable to the shares under section 38(1)(a) to (c) of TCGA 1992;
 - “group” has the same meaning as it has for the purposes of Part 7 of TIOPA 2010 (see section 338);
 - “interest in shares” has the same meaning as in Schedule 7AC to TCGA 1992 (see paragraph 29 of that Schedule);
 - “shares” includes stock.”
- (4) The amendments made by this section have effect in relation to disposals on or after the day on which this Act is passed.

EXPLANATORY NOTE

CURRENCY USED IN TAX CALCULATIONS: CHARGEABLE GAINS AND LOSSES

SUMMARY

1. This clause provides that companies must compute their chargeable gains and losses on share disposals in the currency which is their functional currency (or if certain conditions are met, their designated currency) at the time of the disposal.

DETAILS OF THE CLAUSE

2. Section (1) amends Chapter 4 of Part 2 of the Corporation Tax Act 2010 (CTA10), which determines the currency to be used in tax calculations
3. Section (2) inserts new subsection (3) after section 5(2) of CTA10 stating that new section 9C will apply to the application of subsection (1) so far as it relates to calculating chargeable gains.
4. Section (3) inserts a new section 9C after section 9B of CTA10.
5. New section 9C(1) sets out when the section will apply:
 - a company must dispose of shares, and,
 - at some point during the ownership of the shares, the company must have had a functional currency which was not sterling, or have made a designated currency election for tax purposes.
6. New section 9C(2) defines the term “relevant currency” to include functional currency or designated currency where the conditions in subsection 9C(3) are satisfied.
7. New section 9C(3) sets out the conditions for when the relevant currency is the designated currency rather than the company’s functional currency:
 - the company must be a UK resident investment company which has made a designated currency election under section 9A Corporation Tax Act 2010;
 - the designated currency must differ from the company’s functional currency; and

- the designated currency must be the same as the functional currency the company would have had if it was not in a group.
8. New section 9C(4) provides the methodology for calculating a chargeable gain or allowable loss when the company has a relevant currency which is not sterling.
 9. New section 9C(5) determines that subsections (6) to (9) apply to all computations of chargeable gains and losses on disposals of shares, regardless of whether or not the relevant currency is sterling at the time of disposal.
 10. New section 9C(6) requires allowable expenditure incurred in a currency other than the relevant currency at the time of the expenditure to be translated into the relevant currency using the spot rate of exchange rate at the date of the expenditure.
 11. New section 9C(7) provides for a recalculation of the base cost of the shares on each occasion when there is a change in relevant currency during the ownership of the shares.
 12. New section 9C(8) provides that on disposal of shares, amounts received as consideration in a currency other than the relevant currency at that time must be translated into the relevant currency using the spot exchange rate at the date of disposal.
 13. New section 9C(9) ensures any translations under new subsection 9C(6) occur before any translations under new subsection 9C(7), and that any translations under new subsection 9C(7) are made in chronological order of the changes of relevant currency.
 14. New section 9C(10) provides that where statute requires that the shares are treated for tax purposes as acquired for a deemed amount, then that amount is treated as being incurred on the date the shares are so acquired.
 15. New section 9C(11) defines the terms: “allowable expenditure”; “group”; “interest in shares” and “shares” for the purposes of the clause.
 16. Subsection (4) provides that the amendments apply to disposals on or after the day on which the Finance Bill receives Royal Assent.

BACKGROUND

17. All companies must currently compute all of their chargeable gains and losses in sterling. This clause provides a limited exception to this rule which will ensure closer alignment between the tax and economic outcomes for companies that do not have a sterling

functional currency. This should reduce barriers to commercial decision making by businesses faced with tax gains not matched by a gain of economic substance and reduce administrative burdens for businesses attempting to manage the effects of such gains.

18. If you have any questions about this change, or comments on the legislation, please contact Ellen Milner on 020 7147 3961 (email: ellen.milner@hmrc.gsi.gov.uk).