HMRC - CFM57071 - Hedging: Default Approach

This guidance applies to periods of account starting on or after 1 January 2015.

Default approach

Following the loan relationship review amendments were made to the Disregard Regulations in 2014 which make following amounts in profit or loss the default position (sometimes referred to the ‘regulation 9A’ approach). The effect is that in most cases the company will simply be able to follow the amounts recognised in profit or loss, with few computational adjustments.

In particular, this approach results in the following specific treatment.

Designated Fair value hedge

If the company has a designated fair value hedge where the hedged item is taxed in line with its accounting treatment, the tax treatment of the derivative is to simply follow the amounts recognised in profit or loss. The result is that both the fair value movement on the hedging instrument and the fair value adjustment on the hedged item will both be taxed. These should largely be offsetting. The company will be taxed on any hedge ineffectiveness recognised in profit or loss.

If the hedged item is not taxed in line with the accounts (e.g. hedges of connected company debt), then regulation 7, 8 or 9 will automatically be invoked by regulation 6. A similar rule applies where the hedged item is accounted for on a fair value basis. This will require computational adjustments, although in many cases the treatment will still broadly be to follow the amounts in profit or loss.

Designated Cash flow hedge

If the company has a designated cash flow hedge, then regulation 9A will have effect. For tax purposes the company will simply follow the amounts recognised in profit or loss. Amounts recognised in OCI will not be brought into account until they are transferred to profit or loss (or in certain cases capitalised in the carrying value of an asset or liability). The company will be taxed on any hedge ineffectiveness recognised in profit or loss. CFM57072 has further details of regulation 9A.

Undesignated hedges

If the cash flow hedge is undesignated, the company will need to follow profit or loss which will include any fair value volatility.

Avoidance arrangements

Where however, the derivative is part of an avoidance arrangement to obtain relief for fair value loss on derivatives that have a hedging function then in certain cases regulations 7, 8 and 9 could be invoked under regulation 6(1)(d). See CFM57371 for further details of this rule.

Previous page

Next page