

DETERMINATION > FINANCIAL ARRANGEMENTS > GENERAL

Foreign Currency Rates

Issued: 24 October 1991

G6D

This Determination may be cited as "Determination G6D: Foreign Currency Rates".

1 Explanation (which does not form part of the determination)

This determination rescinds and replaces Determination G6C: Foreign Currency Rates, made on 24 October 1990.

This determination differs from Determination G6C by approving the Australian foreign currency market in the currencies listed in paragraph 6(1) of the method as a source of exchange rate information.

This determination applies where, for the purpose of calculating the income or expenditure of a person in respect of a financial arrangement denominated in a foreign currency, it is necessary to establish the rate of that currency in New Zealand currency. This will be required in the circumstances outlined in paragraph 3 of this determination.

This determination sets out the approved markets, sources of information and method to be used for determining the rate for foreign currency conversion.

2 Reference

This determination is made pursuant to section 64E(1) and section 64E(6) of the Act.

This determination rescinds and replaces Determination G6C: Foreign Currency Rates, made on 24 October 1990.

3 Scope of Determination

This determination applies where it is necessary for the purposes of sections 64B to 64M of the Act to ascertain the value in New Zealand currency of:

- a) A cashflow paid or received in a foreign currency under a financial arrangement; or
- b) A financial arrangement denominated in a foreign currency using a method that has regard to market valuation; or
- c) In any other circumstances, an amount expressed in foreign currency.

4 Principle

1. Markets in foreign currencies are approved having regard to the following criteria:
 - a) The number of participants in the market or having access to the market;

- b) Frequency of trading in the market;
 - c) The nature of trading in the market, how the rate for the foreign currency is determined and how the foreign currency is traded on the market;
 - d) The potential or demonstrated capacity of a person or group of persons to significantly influence the market;
 - e) Significant barriers to entry;
 - f) Discrimination on the basis of the quantity bought and sold unless based on the risks involved or the transaction costs or economies of scale.
2. Sources of information for foreign currency rates are approved having regard to the following criteria:
- a) Reliance on the sources of information by participants in the market; and
 - b) The accessibility of the sources of information for participants in the market.
3. Methods of obtaining a rate for foreign currency at the end of the income year for the purposes of valuing a financial arrangement are approved if:
- a) The rate is obtained at the cut-off time; and
 - b) The method for determining the cut-off time adopted by a person will be consistently applied in respect of each income year.

5 Interpretation

1. In this determination, unless the context otherwise requires—

Expressions used, except the expression "income year", have the same meanings as in sections 2 and 64B to 64M of the Income Tax Act 1976:

"the Act" means the Income Tax Act 1976:

"Approved foreign exchange dealer" means,—

(i) In New Zealand, a foreign exchange dealer that is a registered bank for the purposes of the Reserve Bank of New Zealand Act 1989 and is active in the market; and

(ii) In Australia a registered bank which is an authorised dealer as defined in the Australian Commonwealth Banking (Foreign Exchange) Regulations and which has been authorised by the Reserve Bank of Australia to engage in foreign currency transactions:

"Australian foreign currency market" means the Australian market in spot contracts and forward contracts:

"Contributor page" means a page of information provided by an approved foreign exchange dealer that is displayed on a screen provided by Reuters New Zealand Limited or Telerate New Zealand Limited or an organisation in Australia or New Zealand that provides a similar service:

"Cut-off time" , in relation to a person and an income year, means the time at the end of the income year when all financial arrangements held or issued by the person are valued in order to determine the assessable income of the person for the income year:

"Forward contract" means a contract, other than a futures contract or a spot contract, for the sale or purchase of a foreign currency for delivery at a specified future time:

"Futures contract" means a contract traded on a Futures Exchange:

"Income year" means—

- (a) Where a taxpayer furnishes a return of income under section 15 of the Act for an accounting year ending with an annual balance date other than the 31st day of March, the annual accounting period ending on that balance date:
- (b) In respect of the income of any other person, the year in which that income has been derived by that person:

"Multicontributor page" means a multicontributor page of information that is displayed on a screen provided by Reuters New Zealand Limited or Telerate New Zealand Limited or an organisation in Australia or New Zealand that provides a similar service:

"New Zealand foreign currency market" means the New Zealand market in spot contracts and forward contracts:

"Spot contract" means a contract for the sale or purchase of a foreign currency for delivery in 2 days.

2. Any reference in this determination to another determination made by the Commissioner shall be construed as referring to any fresh determination made by the Commissioner to vary, rescind, restrict, or extend that determination.

6 Method

1. APPROVED MARKETS

The New Zealand foreign currency market and the Australian foreign currency market in European Currency Units and in the currencies of the following countries and territories are approved:

Japan	The Independent State of
Canada	Papua New Guinea
French Republic	Republic of Ireland
The Territory of Hong Kong	Portuguese Republic
Commonwealth of Australia	Republic of Austria
Republic of Singapore	Kingdom of Sweden
The Swiss Confederation	Kingdom of Denmark
Federal Republic of Germany	Republic of Italy
The United States of America	Kingdom of Norway
Kingdom of the Netherlands	Kingdom of Spain
United Kingdom of Great Britain and Northern Ireland	Republic of Turkey
The Federation of Malaysia	The Hellenic Republic
New Zealand	Finland

2. SOURCES OF INFORMATION

The following sources of information for foreign currency rates are approved:

- a) In relation to spot contracts, a multicontributor page that quotes rates for spot contracts;
- b) In relation to forward contracts, a multicontributor page or a contributor page that quotes rates for forward contracts; and
- c) Where a person does not have access to a multicontributor page or a contributor page or where the rates for a forward contract are not available from a multicontributor page, advice as to the buy and sell rates for a forward contract or spot contract given to that person by an approved foreign exchange dealer, which rates shall be derived from an approved source and shall be the rates at which the approved foreign exchange dealer would perform the foreign exchange transaction.

3. SPOT CONTRACTS

- a) Where, for the purposes of determining the income or expenditure of a person in respect of a financial arrangement, it is necessary to determine the rate for a

spot contract at the end of an income year, the rate for the spot contract shall be the midpoint between the buy and sell rates for that spot contract.

- b) Where, for the purposes of determining the income or expenditure of a person in respect of a financial arrangement, it is necessary to ascertain in New Zealand currency the value of a cashflow paid or received in a foreign currency, the rate of exchange to be applied shall be,—
 - (i) Where the cashflow is not converted to New Zealand currency on the day it is paid or received, the midpoint between the buy and sell rates for a spot contract for that currency at any time on that day; or
 - (ii) Where the cashflow is converted to New Zealand currency on the day it is paid or received, the rate of exchange obtained in relation to the cashflow.
- c) Where a buy and sell rate for a spot contract is not quoted on a multicontributor page, the rate for the spot contract shall be the cross rate calculated by reference to—
 - (i) The rate quoted on a multicontributor page for the foreign currency against the United States Dollar; and
 - (ii) The rate quoted on a multicontributor page for the United States Dollar against the New Zealand Dollar.

4. FORWARD CONTRACTS

Where, for the purposes of determining the income or expenditure of a person in respect of a financial arrangement, it is necessary to determine the rate for a forward contract at the end of the income year and,—

- a) Where the buy and sell points for the forward contract are quoted on a multicontributor page, the rate for the forward contract shall be the midpoint between the buy and sell rates for that forward contract obtained by reference to the multicontributor page;
- b) Where the buy and sell points for the forward contract are not quoted on a multicontributor page, but the buy and sell points for similar forward contracts of shorter term ("the shorter contract") and of longer term ("the longer contract") are quoted on a multicontributor page, the rate shall be the rate obtained by reference to the multicontributor page using straight line interpolation of the midpoints between the buy and sell rates for the shorter contract and the longer contract which have terms closest to the term of the forward contract;

- c) Where the rate cannot be obtained by reference to points on a multicontributor page and where the rate for that forward contract is available by reference to contributor pages, then the rate shall be the arithmetic mean of the midpoints of not less than 3 buy and sell rates for the forward contract obtained from contributor pages; and
 - d) Where the rate cannot be obtained by reference to paragraphs 6(4)(a) to (c) of this determination, the rate shall be the arithmetic mean of not less than three rates being any of—
 - (i) The midpoints of the buy and sell rates quoted for the forward contract by one or more approved foreign exchange dealers; or
 - (ii) Where the points for similar forward contracts of shorter term (“the shorter contract”) and of longer term (“the longer contract”) are quoted on a contributor page, then the rate shall be the rate obtained by reference to the contributor page using straight line interpolation of the midpoints between the buy and sell rates for the shorter contract and the longer contract which have terms closest to the forward contract.
5. A person applying paragraphs 6(3)(a) or 6(4) of this determination may obtain the rate for a spot contract or forward contract using the method prescribed in those paragraphs at any time on the last day of the income year:
- Provided that—
- a) The rate applied is the rate obtained at the cut-off time in relation to the person and the income year; and
 - b) The method for determining the cut-off time adopted by that person is consistently applied in respect of each income year:
- Provided also that where there is no market at the cut-off time, the rate shall be—
- c) The rate obtained at the later of—
 - (i) The end of trading in forward contracts or spot contracts by that person in the income year; and
 - (ii) 3.00 pm New Zealand Standard Time on the last day in the income year on which there was a market; or
 - d) The rate for the earlier of—
 - (i) The commencement of trading in forward contracts or spot contracts by that person in the following income year; and

- (ii) 7.30 am New Zealand Standard Time on the first day in the following income year on which there was a market.

7 Example

This is an example of the application of the averaging process and straight line interpolation required for certain forward foreign exchange contracts under the determination.

On its balance date of 30 June 1991 a New Zealand corporate had a forward foreign exchange contract for delivery of 1.2 million New Zealand Dollars for 612,000 United States Dollars on 1 August 1992.

The contract therefore is to be fulfilled in approximately 13 months time.

At the balance date the foreign exchange quotations for the New Zealand Dollar against the United States Dollar were (from the multicontributor page ASAP on the Reuters system):

Spot Rate	Buy 0.6095	Sell 0.6100
-----------	---------------	----------------

Also at that date the quotations of forward foreign exchange points for the United States Dollar against the New Zealand Dollar by three market participants were (as provided on their Reuters screens):

Forward Points

FX DEALER 1:		
Delivery in 1 year	585	555
Delivery in 2 years	1030	960
FX DEALER 2:		
Delivery in 1 year	580	530
Delivery in 2 years	1040	970
FX DEALER 3:		
Delivery in 1 year	575	540
Delivery in 2 years	1035	965

Note that to obtain the forward rates the forward points need to be subtracted from the spot rate.

The mid-rates for use in the interpolation formula are therefore:

	Buy	Sell	Mid-Rate
Forward Rate			
FX DEALER 1:			
Delivery in 1 year	0.5510	0.5545	0.55275
Delivery in 2 years	0.5065	0.5140	0.51025
FX DEALER 2:			
Delivery in 1 year	0.5515	0.5570	0.55425
Delivery in 2 years	0.5055	0.5130	0.50925
FX DEALER 3:			
Delivery in 1 year	0.5520	0.5560	0.55400
Delivery in 2 years	0.5060	0.5135	0.50975

The arithmetic mean of the midpoints of the forward rates is calculated to be:

Delivery in 1 year	0.55366
Delivery in 2 years	0.50975

A suitable formula for straight line interpolation to obtain the required rate is:

$$\text{So } P_x = P_1 + \frac{(T_x - T_1)}{(T_2 - T_1)} * (P_2 - P_1)$$

P1 is the mid-rate for the forward contract with the shorter term (= 0.55366).

P2 is the mid-rate for the forward contract with the longer term (= 0.50975).

Px is the required rate.

T1 is the term till delivery (expressed in days) of the forward contract with the shorter term (= 365).

T2 is the term till delivery (expressed in days) of the forward contract with the longer term (= 730).

Tx is the term till delivery of the contract held (= 398).

The required rate is therefore calculated as follows:

$$\begin{aligned}\text{So } P_x &= P_1 + \left\{ \frac{(T_x - T_1)}{(T_2 - T_1)} * (P_2 - P_1) \right\} \\ &= 0.55366 + \left\{ \frac{(398 - 365)}{(730 - 365)} * (0.50975 - 0.55366) \right\} \\ &= 0.55366 \pm \left\{ \frac{33}{365} * (-0.04391) \right\} \\ &= 0.54969\end{aligned}$$

The current value of the 612,000 United States Dollars receivable on 1 August 1992 is therefore 1,113,354.80 New Zealand Dollars.

About this document

General determinations set out the Commissioner's view on how the financial arrangements rules apply to a specific type of financial arrangement. All general determinations are binding on the Commissioner and some are also binding on taxpayers.