

DETERMINATION > FINANCIAL ARRANGEMENTS > SPECIAL

Issue of Capital Guaranteed Growth Notes and Related Financial Arrangements

Issued: 14 February 1997

S4

This determination may be cited as "Determination S4: Issue of Capital Guaranteed Growth Notes and Related Financial Arrangements".

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

Structure

1. BNZ proposes to establish FundCo, a vehicle which will issue notes to investors, the return on which is linked to an investment in futures contracts, derivative contracts and foreign exchange contracts. FundCo will be a wholly owned subsidiary of BNZ. In addition, repayment of a certain amount, being at least equal to the initial capital invested on subscription of the notes, is guaranteed by BNZ.
2. The structure of the notes issued by FundCo is as follows:
 - a) **Issue of Notes:** FundCo will issue a series of notes to investors. Each note will represent an agreement to sell, on a cash settled basis, to the investor, on a specified future date, a stated proportion of FundCo's assets on that date. The notes will constitute debt securities under the Securities Act 1978. Accordingly, FundCo will appoint a trustee and enter into a trust deed for the benefit of noteholders, as required by the Securities Act.
 - b) **Termination:** On the termination date, instead of physical delivery of FundCo's assets in settlement of all outstanding notes, there will be a cash settlement of each note equal to the value of the specified proportion of the assets being purchased.
 - c) **Variable Payments:** During the term of the notes, progress payments are to be made to investors based upon a fixed percentage of the increase in value of the net assets of TradeCo (see (g) below). Restrictions are placed on payments which would reduce the value of the original investment.
 - d) **Capital Guarantee Fund:** FundCo uses a proportion of the amount received on issue of the notes to invest in a deposit with BNZ. On maturity, the value of the deposit is equal to the aggregate amount subscribed by the investors on the original issue of the notes plus an additional amount (which will be known with certainty prior to issue of the notes) equal to a fixed percentage of the amount received on issue. This enables FundCo to satisfy its obligations to repay, at least, the aggregate amount originally invested by the investors (the capital guaranteed amount).
 - e) **Investment linked to futures contracts, derivative contracts and foreign exchange contracts:** FundCo makes an investment of the balance of the amount received on issue of the notes (i.e. after investing in the deposit and meeting certain expenses) by way of an agreement for sale with TradeCo, a company owned by the trustees of a trust established for charitable purposes in New Zealand. TradeCo

makes investments in futures contracts, derivative contracts and foreign exchange contracts (see (h) below). The agreement provides for a sale of all of TradeCo's assets, with settlement at a stated time, being a number of years after entry into the agreement.

- f) **Cash Settled Sale:** Instead of physical delivery of TradeCo's assets on settlement, there will be a cash settlement of the agreement equal to the value of the assets of TradeCo. It is not intended that TradeCo's assets will be physically delivered to FundCo except in the event of a default by TradeCo to make the cash settlement payment. The cash proceeds will form part of the assets of FundCo subject to the settlement referred to in paragraph (b).
- g) **Variable Payments:** During the term of the notes progress payments are to be made by TradeCo to FundCo based upon a fixed percentage of the increase in value of TradeCo's net assets (thereby enabling FundCo to make the payments described in paragraph (c) to investors during the term of the agreements).
- h) **Futures contracts, derivative contracts and foreign exchange contracts:** TradeCo then uses the moneys received by it under the agreement for sale with FundCo to invest in futures contracts, derivative contracts and foreign exchange contracts. These contracts will be managed by members of the ED & F Man group of companies.
- i) **Guarantee:** TradeCo will enter into a guarantee agreement with BNZ under which BNZ will agree to guarantee repayment of the capital guaranteed amount.

Overall effect of arrangements

3. The amount of expenditure incurred by TradeCo in relation to the TradeCo Agreement (as calculated pursuant to this Determination and under sections EH 1 to EH 9 of the Act) after allowing for other expenditure incurred by TradeCo will be equivalent on an annual basis to the income derived by TradeCo with respect to its investment in futures contracts, derivative contracts and foreign exchange contracts (as calculated pursuant to this Determination and under sections EH 1 to EH 9 of the Act) and vice versa.
4. The amount of expenditure incurred by FundCo in relation to the FundCo Agreement (as calculated pursuant to this Determination and under sections EH 1 to EH 9 of the Act) will be equivalent on an annual basis to the income derived by FundCo with respect to the TradeCo Agreement and the Deposit (as calculated pursuant to this Determination and under sections EH 1 to EH 9 of the Act) and vice versa.

Determination

5. BNZ has applied for a determination that:

a) The agreements for sale between the investors and FundCo (represented by the notes) are treated under the accruals regime as follows:

i For investors who are not cash basis holders the agreement must be marked to the value of the agreement (as calculated in accordance with this Determination) at each balance date. The change in value together with any payments received during that year will be income to the investors (or expenditure, as the case may be).

However, for this purpose, if the market value of the agreement at a balance date has fallen below the amount of the capital floor (as defined in this Determination), the market value at that balance date will be deemed to be equal to the capital floor. The amount of the capital floor, at any particular balance date, will be calculated as being equal to the amount originally paid on entry at issue of the agreement for sale, together with accrued interest calculated up to that balance date, according to the yield to maturity method, as if the investor were to receive at settlement date only the capital guaranteed amount under the agreement for sale.

ii FundCo will account for the agreements with the investors by marking the agreements to their value (as calculated in accordance with this Determination) at each balance date. The change in value together with any payments made by FundCo during that year will constitute expenditure (or income, as the case may be).

b) Income from the deposit issued by BNZ to FundCo will be required under the accruals regime to be returned by FundCo on a yield to maturity basis.

c) The agreement for sale between FundCo and TradeCo is treated under the accruals regime as follows:

i TradeCo will account for the agreement on a basis that has regard to market valuation. The change in value together with any payments made by TradeCo during an income year will be expenditure or income (as the case may be);

ii FundCo will similarly account for the agreement on a basis that has regard to market valuation. The change in value together with any payments made by TradeCo to FundCo during an income year will constitute accrual income (or, expenditure, as the case may be).

- d) The futures contracts, derivative contracts and foreign exchange contracts to which TradeCo is a party, will be required to be accounted for by TradeCo under the accruals regime using the method specified in this Determination that has regard to market valuation.
 - e) The guarantee entered into between TradeCo and BNZ will be accounted for by TradeCo using a straight-line method.
6. This Determination applies to all the financial arrangements mentioned in paragraph 1.2 and is to provide the method for recognition of income and expenditure by parties to each of those financial arrangements (other than investors who are cash basis holders) in accordance with the Act.

2 Reference

1. This Determination is made pursuant to section 90(1)(c) of the Tax Administration Act 1994.

3 Scope of the Determination

1. This Determination shall apply to the following arrangements (a description of which is set out below):
 - a) the FundCo Agreements;
 - b) the Deposit;
 - c) the TradeCo Agreement;
 - d) the futures contracts, derivative contracts and foreign exchange contracts to which TradeCo is a party;
 - e) the Guarantee.
2. This determination is restricted in scope to FundCo, TradeCo and Investors who are subject to the accruals rules and are not cash basis holders

FundCo agreements

3. Parties: Investor
FundCo
4. FundCo will enter into a number of FundCo Agreements with Investors. Each FundCo Agreement will provide that FundCo agrees to sell a stated percentage of its assets, with settlement to occur at a stated time after the date of entry into the FundCo Agreement.
5. Each FundCo Agreement will be represented by a Note issued by FundCo to an Investor.
6. The principal terms of each FundCo Agreement will be that:
 - a) on payment of the purchase price, each Investor purchases a proportion of FundCo's assets;
 - b) settlement of the FundCo Agreement will take place on the Settlement Date;
 - c) instead of a transfer of the actual assets held by FundCo on the Settlement Date, FundCo must pay to each Investor an amount in cash equal to the value of the assets purchased under the FundCo Agreement in satisfaction of FundCo's obligations on settlement;
 - d) each FundCo Agreement will be supported by a guarantee from BNZ, so that on Settlement Date an Investor will receive, at least, an amount equal to the purchase price plus an amount equal to an agreed percentage of the purchase price, such percentage to be set prior to Issue Date;
 - e) FundCo will also make FundCo Variable Payments to an Investor on each anniversary of the Issue Date until the Settlement Date. The aggregate FundCo Variable Payments made on such an anniversary date will:
 - i on the first anniversary of the Issue Date, be equal to 25 percent of the increase in the value of the TradeCo Agreement during the 12 month period prior to the relevant TradeCo Variable Payment being made (such increase being adjusted for any payments made to Investors by way of early settlement); and
 - ii on every other anniversary of the Issue Date, be equal to 25 percent of the extent to which the value of the TradeCo Agreement prior to making the TradeCo Variable Payment, as at the date of that anniversary, exceeds the previous highest value of the TradeCo Agreement prior to the making of the relevant TradeCo Variable Payment (such increase being adjusted for any payments made to Investors by way of early settlement);

Provided that no FundCo Variable Payment is to be made on any such an anniversary day if:

- iii the percentage increase in the value of TradeCo's net assets for the relevant year is negative;
- iv the value of TradeCo's net assets is less than the value of the net assets of TradeCo as at the Issue Date (such net assets being adjusted to account for Investors who have elected for early settlement).

Provided further that the aggregate FundCo Variable Payments made on a particular anniversary of Issue Date shall not exceed the TradeCo Variable Payment made to FundCo on that date;

- f) An Investor may call for early settlement of the FundCo Agreement upon giving 12 business days written notice. However an early settlement charge will be deductible from the amount otherwise payable to an Investor. The charges will be equal to the aggregate of:
 - i the early settlement charges imposed upon FundCo in relation to early settlement of a proportion of the TradeCo Agreement; and
 - ii early settlement charges imposed on FundCo in relation to early settlement of an amount of the Deposit —

in each case where those early settlement charges are incurred by FundCo for the purposes of enabling it to redeem Notes held by that particular Investor.
- g) Early settlement of the FundCo Agreement may also occur upon the occurrence of an event of default. No early settlement charge may be required in that event;
- h) BNZ shall publish the "total asset value" attributable to each FundCo Agreement on a monthly basis. The total asset value attributable to each FundCo Agreement will be equal to the Market Value of each FundCo Agreement;
- i) the FundCo Agreement will be transferable by transfer of the Notes representing it.

Deposit

7. Parties: FundCo

BNZ

8. The terms of the Deposit are:
 - a) the Deposit is to be for a term of 10 years equal to the term of the FundCo Agreements;
 - b) the Deposit will yield on the Settlement Date the aggregate amount paid to FundCo by all Investors (other than those Investors who have elected for early settlement) on the Issue Date, plus a fixed percentage of this amount (such percentage to be set prior to Issue Date).
9. FundCo may call for early settlement of a proportion of an amount of the Deposit upon notice to BNZ, provided, that in the event of early settlement, an early settlement charge will be deductible from the amount otherwise payable to FundCo and such early settlement charges will be as determined by BNZ.

TradeCo Agreement

10. Parties: FundCo
TradeCo
11. TradeCo will enter into the TradeCo Agreement with FundCo. The TradeCo Agreement will provide that TradeCo agrees to sell all of its assets, with settlement to occur at a stated time after the date of entry into the TradeCo Agreement.
12. The principal terms of the TradeCo Agreement will be that:
 - a) on payment of the purchase price, FundCo will receive rights to purchase all of TradeCo's assets;
 - b) settlement of the TradeCo Agreement will take place on the Settlement Date;
 - c) instead of a transfer of the actual assets held by TradeCo on the Settlement Date, TradeCo shall pay to FundCo an amount in cash equal to the value of the assets purchased under the TradeCo Agreement, in satisfaction of TradeCo's settlement obligations;
 - d) TradeCo will make TradeCo Variable Payments to FundCo on each anniversary of the Issue Date until the Settlement Date. A TradeCo Variable Payment will:
 - i on the first anniversary of the Issue Date be equal to 25 percent of the increase in the value of the TradeCo Agreement during the 12 month period prior to the relevant TradeCo Variable Payment being made (such increase being adjusted for any payments made to FundCo on early settlement of a proportion of the TradeCo Agreement); and
 - ii on every other anniversary of the Issue Date, be equal to 25 percent of the extent to which the value of the TradeCo Agreement prior to making the TradeCo

Variable Payment, as at the date of that anniversary, exceeds the previous highest value of the TradeCo Agreement prior to the making of the relevant TradeCo Variable Payment (such increase being adjusted for any payments made to FundCo on early settlement of a proportion of the TradeCo Agreement);

provided that no TradeCo Variable Payment is to be made on any such anniversary day if:

- iii the percentage increase in the value of TradeCo's net assets for the relevant year is negative;
- iv the value of TradeCo's net assets is less than the value of the net assets of TradeCo as at the Issue Date (such net assets to be adjusted to account for Investors who have elected for early settlement under the FundCo Agreements);

Provided further that a TradeCo Variable Payment shall only be made to the extent that it can be made without reducing the net assets of TradeCo below the value of TradeCo's net assets as at Issue Date (such net assets to be adjusted to account for Investors who have elected for early settlement under the FundCo Agreements);

- e) FundCo may call for early settlement of a proportion of the TradeCo Agreement upon giving 10 days written notice (enabling FundCo to satisfy its obligations to an Investor on such an Investor calling for early settlement of a FundCo Agreement) provided that in the event of early settlement an early settlement charge will be deductible from the amount otherwise payable to FundCo. The charges will be as follows:
 - i 5 percent of the amount otherwise payable by FundCo to an Investor where early settlement occurs prior to the first anniversary of the Issue Date;
 - ii 4 percent of the amount otherwise payable by FundCo to an Investor where early settlement occurs prior to the second anniversary of the Issue Date;
 - iii 3 percent of the amount otherwise payable by FundCo to an Investor where early settlement occurs prior to the third anniversary of the Issue Date;
 - iv 2 percent of the amount otherwise payable by FundCo to an Investor where early settlement occurs prior to the fourth anniversary of the Issue Date;
 - v 1 percent of the amount otherwise payable by FundCo to an Investor where early settlement occurs prior to the fifth anniversary of the Issue Date.

Provided further that if TradeCo has insufficient assets from which it is able to deduct such a penalty, the shortfall between TradeCo's assets (if any) and the penalty will be payable by FundCo to TradeCo;

- f) Early settlement may also occur on the occurrence of an event of default.

Guarantee

13. Parties: BNZ

TradeCo

- a) BNZ will guarantee the repayment of the purchase price paid on subscription for the Notes for Investors plus the fixed additional percentage by FundCo on Settlement Date;
- b) TradeCo will pay to BNZ a fee of 0.5 percent of such guaranteed amounts calculated on a day to day basis from the Issue Date through to the Settlement Date;
- c) The fees payable by TradeCo to BNZ will be payable quarterly.

4 Principle

Fundco Agreements

1. FundCo is the issuer and each of the Investors is a holder under the FundCo Agreements.
2. The core acquisition price in relation to the Investors who subscribe for the Notes is the amount subscribed for on issue of the Notes. For Investors who do not subscribe for Notes on their issue but acquire Notes from other Investors, the core acquisition price in relation to such Investors shall be the price paid in acquiring the Notes.
3. With respect to FundCo and Investors who are not cash basis holders and are subject to the accruals regime, income or expenditure in respect of the FundCo Agreements will be returned for the purposes of section EH 1 of the Act using the method specified in this Determination which has regard to changes in value of the FundCo Agreement. That method will require, in any particular year, that an Investor and FundCo return as income, or expenditure, the difference between the value of the FundCo Agreement at the beginning of the year and the value of the FundCo Agreement at the end of the year, together with payments received by Investors, or made by FundCo, in relation to the FundCo Agreement during the particular year, subject to operation of the Capital Floor, in relation to income derived or expenditure incurred by Investors, as explained below. The value of the FundCo Agreements, at any time, will be the aggregate of the:
 - a) the value of the Deposit, being the amount initially paid by FundCo to BNZ in making the deposit and any income which has been derived, up to the relevant point in time, such income being calculated according to the yield to maturity method less the aggregate payments received by FundCo from BNZ in relation to the Deposit on account of early settlement of FundCo Agreements; and

- b) the market value of the TradeCo Agreement, at the relevant time as calculated in accordance with this Determination.

Provided that in relation to the calculation of income or expenditure by an Investor in any income year, where the market value of the FundCo Agreement at the end of any income year has fallen below the Capital Floor for that income year, the market value at the end of that year will be equal to the Capital Floor (as calculated for that income year). Conversely, in relation to the calculation of income or expenditure by that Investor in the immediately subsequent income year, the market value of that FundCo Agreement at the beginning of that immediately subsequent income year will be deemed to be equal to that Capital Floor for the immediately preceding income year.

Deposit

- 4. BNZ is the issuer and FundCo is the holder in relation to the Deposit.
- 5. FundCo will return income or expenditure in respect of the Deposit for the purposes of section EH 1 of the Act using the yield to maturity method.

TradeCo Agreement

- 6. TradeCo is the issuer and FundCo is the holder in relation to the TradeCo Agreement.
- 7. The core acquisition price in relation to the TradeCo Agreement is the amount paid to TradeCo by FundCo on entry into the TradeCo Agreement.
- 8. FundCo and TradeCo will return income or expenditure in respect of the TradeCo Agreement for the purposes of section EH 1 of the Act using the method specified in this Determination which has regard to market valuation. That method will require, in any particular year, that FundCo and TradeCo return as income, or expenditure, the difference between the market value of the TradeCo Agreement at the beginning of the year and the market value of the TradeCo Agreement at the end of the year, together with payments received by FundCo, or paid by TradeCo, in relation to the TradeCo Agreement during that particular year. The market value of the TradeCo Agreement on any particular day will be:
 - a) the aggregate of the market value of the futures contracts, derivative contracts and foreign exchange contracts to which TradeCo is a party at the relevant time (the method for determining the market value of those financial arrangements is set out in paragraphs 4.10 below); less
 - b) any accrued liabilities or expenses of TradeCo on that particular day.

Futures contracts, derivative contracts and foreign exchange contracts

9. Income or expenditure in relation to the futures contracts, derivative contracts and foreign exchange contracts to which TradeCo is a party will be accounted for by TradeCo under the accruals regime using the method specified in this Determination, which has regard to market valuation.
10. For the purposes of that method, the market value of those contracts will be determined as follows:
 - a) the market value of the underlying investments to which the contracts relate where those investments are quoted, listed, traded or dealt in or on any futures exchange shall be determined by reference to the last quoted price (or, in the absence of any trades, at the average of the last bid and offer prices) on the principal market for such investments as at the close of business on the day for which such calculation is to be made. All calculations based on the value of investments traded or dealt in on any market which is the principal market therefor shall be made by reference to the mean between the latest bid and offer prices quoted thereon. Provided however that:
 - I. where the prices ruling on a market other than the principal market provide in all the circumstances a fairer value in relation to any such investment, those other prices may be used;
 - II. an alternative method may be used if it better reflects the fair value of these investments;
 - b) foreign exchange contracts will be valued by reference to the price at a particular valuation date at which a new foreign exchange contract of the same type, size and maturity could be undertaken;
 - c) in relation to derivatives contracts, and if no price quotations are available as provided above, the value thereof shall be the value which most fairly reflects the market value of the relevant contract as determined by BNZ, in consultation with the Valuer and/or the directors of TradeCo, as applicable; and
 - d) any value (whether of a security or cash) otherwise than in New Zealand dollars shall be translated into New Zealand dollars in accordance with Determination G6D.

Guarantee

11. TradeCo is the issuer under the Guarantee.
12. TradeCo will return expenditure in respect of the Guarantee in accordance with a straight-line method.

5 Interpretation

1. In this Determination, unless the context otherwise requires:
 - a) words and expressions shall have the same meaning as in the Act, except that, where there is a conflict between the meaning of an expression in sections EH 1 to EH 9 of the Act and the meaning of an expression elsewhere in the Act, the expression shall have the meaning as if the said sections EH 1 to EH 9;
 - b) the singular includes the plural and vice versa.

"Act" means the Income Tax Act 1994.

"BNZ" means the Bank of New Zealand.

"Capital Guaranteed Amount", in relation to an Investor and a FundCo Agreement to which that Investor is a party, means the amount which BNZ has guaranteed will be repaid to the Investor in relation to that FundCo Agreement on Settlement Date.

"Capital Floor" in relation to an Investor and a FundCo Agreement to which an Investor is a party, and for any particular income year, means the aggregate of:

- I. the amount which was paid to FundCo in relation to that FundCo Agreement on Issue Date by the first investor to be a party to that FundCo Agreement; and
- II. the aggregate of the amounts of interest that would be deemed to accrue in that income year and in all previous years since Issue Date, in respect of that FundCo Agreement, if such amounts of interest were calculated according to the yield to maturity method on the basis that the Investor had paid to FundCo on Issue Date the amount referred to in (i) of this definition and that the only payment that the Investor was to receive in relation to that FundCo Agreement was the payment at Settlement Date of the Capital Guaranteed Amount in relation to that FundCo Agreement.

"Deposit" means the deposit made by FundCo with the BNZ.

"E D & F Man" means E D & F Man International Limited.

"FundCo" means BNZ Capital Guaranteed Growth Fund Limited.

"FundCo Agreements" means the agreements for sale, as documented by the Notes, entered into between the Investors and FundCo.

"FundCo Variable Payments" means the payments made by FundCo to the Investors during the term of the FundCo Agreements, as a result of FundCo receiving any TradeCo Variable Payments.

"Guarantee" means the guarantee between BNZ and TradeCo.

"Investors" means the investors who have entered into the FundCo Agreements.

"Issue Date" means:

- a) in relation to a FundCo Agreement, the date of entry into the FundCo Agreement by FundCo; and
- b) in relation to the TradeCo Agreement, the date of entry into the TradeCo Agreement.

"Market Value" means:

- a) in relation to all FundCo Agreements which are on issue at any particular time, the value of those FundCo Agreements, as notified by BNZ, being equal to the aggregate of:
 - I. an amount equal to the core acquisition price of the Deposit and income derived in relation to the Deposit up to the relevant point in time, determined in accordance with the yield to maturity method less the aggregate payments received by FundCo from BNZ in relation to the Deposit on account of early settlement of FundCo Agreements; and
 - II. the Market Value of the TradeCo Agreement at that point in time—

Provided that in determining the value of any particular FundCo Agreement, such an agreement shall have a value which is proportional to the aggregate value of all FundCo Agreements (having regard to the total number of FundCo Agreements on issue at that particular time).

- b) in relation to the TradeCo Agreement, the value of the TradeCo Agreement as notified to FundCo by BNZ from time to time and pursuant to the terms of the TradeCo Agreement, being the market value of the futures contract, derivative contracts and foreign exchange contracts to which TradeCo is a party (such market value being determined in accordance with paragraph 4.10 of this Determination), less any accrued liabilities or expenses of TradeCo at the relevant time.

"Notes" means the notes issued to the Investors by FundCo which document the terms of the FundCo Agreements.

"Settlement Date" means the date of settlement under the FundCo Agreements.

"TradeCo" means AHL Guaranteed Trading (NZ) Limited.

"TradeCo Agreement" means the agreement for sale entered into between FundCo and TradeCo.

"TradeCo Variable Payments" means the payments made by TradeCo to FundCo during the term of the TradeCo Agreement.

"**Valuer**" means E D & F Man Valuation Services Limited, a member of the E D & F Man group of companies, appointed to provide assistance to BNZ for valuations in relation to the FundCo Agreements and TradeCo Agreement.

6 Method

FundCo Agreements

1. The amount of the core acquisition price of each FundCo Agreement is to be determined in accordance with paragraph (e)(i) of the definition of "core acquisition price" in section OB 1 of the Act. The core acquisition price in relation to the Investors who subscribe for the Notes is the amount subscribed for on issue of the Notes. For Investors who do not subscribe for Notes on their issue but acquire Notes from other Investors, the core acquisition price in relation to such Investors shall be the price paid to acquire the Notes.
2. Expenditure incurred or income derived with respect to a FundCo Agreement shall be calculated using the method specified in this Determination, which has regard to the Market Value of a FundCo Agreement at a particular time.
3. The amount of income derived or expenditure incurred by FundCo, in any year in relation to a FundCo Agreement, other than the year in which a base price adjustment is required to be made by FundCo, shall be calculated in accordance with the formula:

$$a + b - c$$

where

a = the Market Value of the FundCo Agreement as at the end of that year (such Market Value to be determined after the making of FundCo Variable Payments required to be made on that particular day); and

b = payments made to an Investor by FundCo, in relation to the particular FundCo Agreement, during that year; and

c =

- I. in the year in which FundCo enters into the FundCo Agreement, the core acquisition price for FundCo in relation to the particular FundCo Agreement; and
- II. in every year, other than the year in which FundCo enters into the FundCo Agreement, the Market Value of the FundCo Agreement at the end of the immediately preceding year (such Market Value to be determined after the making of FundCo Variable Payments required to be made on that particular day).

The amount so calculated shall:

- a) Where it is a positive amount, be deemed to be expenditure incurred by FundCo in the relevant income year; and
- b) Where it is a negative amount, be deemed to be income derived by FundCo in the relevant income year.

4. The amount of income derived or expenditure incurred by an Investor, in any year in relation to a FundCo Agreement, other than the year in which a base price adjustment is required to be made by that Investor, shall be calculated in accordance with the formula:

$$a + b - c$$

where

a = the Market Value of the FundCo Agreement as at the end of that year (such Market Value to be determined after the making of FundCo Variable Payments required to be made on that particular day); Provided that if the Market Value of that FundCo Agreement is less than the Capital Floor for that income year, then item "a" for the purposes of this formula shall be equal to the Capital Floor for that year and not the Market Value of the FundCo Agreement as at the end of that year; and

b = payments made to that Investor by FundCo during that year; and

c =

- I. in the year in which that Investor becomes a holder in relation to the FundCo Agreement, the core acquisition price for that Investor in relation to the particular FundCo Agreement; and
- II. in every year, other than the year in which that Investor becomes a holder in relation to the FundCo Agreement, item "a" of this formula for the immediately preceding year.

The amount so calculated shall:

- a) Where it is a positive amount, be deemed to be income derived by an Investor in the relevant income year; and
- b) Where it is a negative amount, be deemed to be expenditure incurred by an Investor in the relevant income year;

Deposit

5. In any year other than the year of repayment of the Deposit, the amount of income derived or expenditure incurred by FundCo as holder in respect of the Deposit shall be calculated in accordance with the yield to maturity method.

TradeCo Agreement

6. The amount of the core acquisition price of the TradeCo Agreement is to be determined in accordance with paragraph (e)(i) of the definition of "core acquisition price" contained in section OB 1 of the Act. The core acquisition price for TradeCo and FundCo in relation to the TradeCo Agreement is the amount paid to TradeCo by FundCo on entry into the TradeCo Agreement.
7. Expenditure incurred or income derived with respect to the TradeCo Agreement shall be calculated using the method specified in this Determination, which has regard to market valuation.
8. The amount of income derived or expenditure incurred by TradeCo as issuer, or FundCo as holder, under the TradeCo Agreement, other than the year in which a base price adjustment is required to be made by TradeCo or FundCo (as the case may be), shall be calculated in accordance with the formula:

$$a + b - c$$

where

a = the Market Value of the TradeCo Agreement as at the end of that year (such Market Value to be determined after the making of TradeCo Variable Payments required to be made on that particular day); and

b = payments made to FundCo by TradeCo during that year in relation to the TradeCo Agreement; and

c =

- I. in the year of entry into the TradeCo Agreement, the core acquisition price for FundCo or TradeCo in relation to the TradeCo Agreement; and
- II. in every year, other than the year of entry into the TradeCo Agreement, the Market Value of the TradeCo Agreement at the end of the immediately preceding year (such Market Value to be determined after the making of TradeCo Variable Payments required to be made on that particular day) together with any payments made by FundCo to TradeCo during that year.

The amount so calculated shall:

- a) Where it is a positive amount be deemed to be expenditure incurred by TradeCo and income derived by FundCo in the relevant income year; and
- b) Where it is a negative amount be deemed to be income derived by TradeCo and expenditure incurred by FundCo in the relevant income year.

Futures contracts, derivative contracts and foreign exchange contracts

9. In any year, other than the year in which a base price adjustment is required to be made in relation to futures contracts, derivative contracts or foreign exchange contracts, the income derived or expenditure incurred by TradeCo with respect to the futures contracts, derivatives contracts and foreign exchange contracts shall be calculated using the method specified in this Determination which has regard to market valuation. Under that method, the income or expenditure in relation to such a contract shall be calculated in accordance with the following formula.

$$a + b - c$$

where

a = the market value of the contract as at the end of the year (as calculated in accordance with paragraph 4.10 of this determination);

b = payments made to TradeCo, if any, in relation to that contract during the particular year;

c = the aggregate of:

(A)

- I. in the case of a contract which was on hand at the beginning of the year, the market value of the relevant contract at that time (as calculated in accordance with paragraph 4.10 of this determination); or
- II. in the case of any other contract, the core acquisition price, if any, in relation to that contract; and

(B)

payments made by TradeCo (other than the core acquisition price), if any, in relation to that contract during the particular year.

The market value of the futures contracts, derivative contracts and foreign exchange contracts will be determined in the manner set out at paragraph 4.10.

Guarantee

10. TradeCo will account for expenditure in relation to the guarantee using a straight-line method.
11. Guarantee fees paid by TradeCo in any year will be dependent on the aggregate Capital Guaranteed Amounts at any one particular time. The guarantee fee is fixed at 0.5 percent of the aggregate Capital Guaranteed Amounts on a daily basis, and is payable quarterly. TradeCo will be treated as having incurred accrual expenditure in relation to the Guarantee in an income year, on a straight-line basis, equal to the guarantee fees which have accrued on a daily basis during that year.

7 Examples

1. Assume:
 - a) On 31 March 1997 investor A and investor B enter into FundCo Agreements under which each pay FundCo \$5,000 to purchase 50 percent of FundCo's net assets, with settlement to occur 10 years from the date of entry into the FundCo Agreements (i.e. 31 March 2007). The relevant terms of the FundCo Agreements are:
 - I. settlement is to be by way of a cash settlement equal to the value of the assets purchased, as opposed to physical delivery of the assets;
 - II. FundCo agrees to make progress payments in satisfaction of its obligations on settlement. The progress payments are to be made at the end of each year during the term of the FundCo Agreement (on the terms set out at paragraph 3.6 above).
 - b) FundCo deposits \$6,000 with BNZ on 31 March 1997. The deposit is for 10 years and matures on 31 March 2007 with a repayment of \$11,500, i.e. an agreed additional amount of \$1,500;
 - c) On 31 March 1997, FundCo enters into the TradeCo Agreement with TradeCo under which FundCo pays \$4,000 to purchase 100 percent of TradeCo's net assets, with settlement to occur 10 years from the date of entry into the TradeCo Agreement (i.e. on 31 March 2007). The relevant terms of the TradeCo Agreements are:
 - I. settlement is to be by way of a cash settlement equal to the value of the assets purchased, as opposed to physical delivery of the assets;
 - II. TradeCo agrees to make progress payments in satisfaction of its obligations on settlement. The progress payments are to be made at the end of each year during the term of the TradeCo Agreement and equal to 25 percent of the increase in the Market Value of the TradeCo Agreement over the previous 12 months (on the terms set out at paragraph 3.12 above).

- d) Assume Investors A and B, FundCo and TradeCo all have 31 March balance dates for tax purposes.
- e) Investor A does not qualify as a cash basis holder. Investor B is a cash basis holder.

2. The Deposit made by FundCo with the BNZ has the following profile:

	Value of Deposit at end of period	YTM income for the period	Principle accretion for the period
31 March 97	6,000		
31 March 98	6,403	403	403
31 March 99	6,834	431	431
31 March 00	7,293	459	459
31 March 01	7,783	490	490
31 March 02	8,307	524	524
31 March 03	8,865	558	558
31 March 04	9,461	596	596
31 March 05	10,097	636	636
31 March 06	10,776	679	679
31 March 07	11,500	724	724

3. The TradeCo Agreement between TradeCo and FundCo has the following profile:

	Purchase Price	Value of TradeCo Agreement prior to TradeCo Variable Payments	TradeCo Variable Payments	Value of TradeCo Agreement after TradeCo Variable Payments
31 March 97	4,000			
31 March 98		5,400	350	5,050
31 March 99		6,818	442	6,376

31 March 00	7,970	399	7,571
31 March 01	9,085	378	8,707
31 March 02	11,319	653	10,666
31 March 03	9,599	0	9,599
31 March 04	10,599	0	10,599
31 March 05	13,727	765	12,962
31 March 06	16,850	972	15,878
31 March 07	21,435	1,389	20,046

4. The Value of each of the FundCo Agreements, being 50 percent of the value of the Deposit and the value of the TradeCo Agreement (after payment of the FundCo Variable Payments), is as follows:

	Value of each FundCo Agreement after payment of FundCo Variable payments
31 March 97	5,000
31 March 98	5,727
31 March 99	6,605
31 March 00	7,432
31 March 01	8,245
31 March 02	9,486
31 March 03	9,232
31 March 04	10,010
31 March 05	11,529
31 March 06	13,327
31 March 07	15,773

5. The value of TradeCo's futures portfolio as at the end of each income year, after payment of the TradeCo Variable Payments is as follows:

	Value of futures portfolio prior to TradeCo Variable Payments	Value of futures portfolio after TradeCo Variable Payments
31 March 98	5,400	5,050
31 March 99	6,818	6,376
31 March 00	7,970	7,571
31 March 01	9,085	8,707
31 March 02	11,319	10,666
31 March 03	9,599	9,599
31 March 04	10,559	10,559
31 March 05	13,727	12,962
31 March 06	16,850	15,878
31 March 07	21,435	20,046

6. By way of example, calculations of the income derived/expenditure incurred by TradeCo, FundCo and Investor A and B for the year ending 31 March 2005 are set out below. The position for each such party over all years in question is then set out in table form.

Position of TradeCo for the year ending 31 March 2005

7. Income derived with respect to TradeCo's portfolio of futures contracts is \$3,168 (being the difference between the futures contracts, prior to the making of progress payments, on hand at 31 March 2005 and those on hand as at 31 March 2004, after having made progress payments).

8. Income derived/expenditure incurred with respect to the TradeCo Agreement:

$$a = \$12,962$$

$$b = \$765$$

$$c = \$10,559$$

$$\$12,962 + \$765 - \$10,559 = \$3,168 \text{ expenditure incurred}$$

Position of FundCo for the year ending 31 March 2005

9. Income derived/expenditure incurred with respect to the TradeCo Agreement:

$$a = \$12,962$$

$$b = \$765$$

$$c = \$10,559$$

$$\$12,962 + \$765 - \$10,559 = \$3,168 \text{ income derived}$$

10. Income derived under the Deposit:

$$\$636 \text{ (refer profile at paragraph 7.2)}$$

11. Income derived/expenditure incurred with respect to each FundCo Agreement:

$$a = \$11,529$$

$$b = \$383$$

$$c = \$10,010$$

$$\$11,529 + \$383 - \$10,010 = \$1,902 \text{ expenditure incurred}$$

Position of Investor A for the year ending 31 March 2005

12. Income derived/expenditure incurred with respect to the FundCo Agreement

$$a = \$11,529$$

$$b = \$383$$

$$c = \$10,010$$

$$\$11,529 + \$383 - \$10,010 = \$1,902 \text{ income derived}$$

Position of Investor B for the year ending 31 March 2005

13. As investor B is a cash basis holder the income derived with respect to the FundCo Agreement is \$383, being the only receipt for that year.

Position of TradeCo for all years

14. The tax position for TradeCo over the years in question is:

	Income from futures contracts	Expenditure in respect of TradeCo Agreement
31 March 98	1,400	(1,400)
31 March 99	1,768	(1,768)
31 March 00	1,594	(1,594)
31 March 01	1,514	(1,514)
31 March 02	2,612	(2,612)
31 March 03	(1,067)	1,067
31 March 04	960	(960)
31 March 05	3,168	(3,168)
31 March 06	3,888	(3,888)
31 March 07	5,557	(5,557)

Position of FundCo for all years

15. The tax position for FundCo over the years in question is as follows:

	Income from TradeCo Agreement	Income from Deposit	Expenditure in respect of FundCo Agreements
31 March 98	1,400	403	(1,803)
31 March 99	1,768	431	(2,199)
31 March 00	1,594	459	(2,053)
31 March 01	1,514	490	(2,004)
31 March 02	2,612	524	(3,136)
31 March 03	(1,067)	558	509
31 March 04	960	596	(1,556)

31 March 05	3,168	636	(3,804)
31 March 06	3,888	679	(4,567)
31 March 07	5,557	724	(6,281)

Position of Investors A & B for all years

16. The tax position for Investor A and Investor B:

	INVESTOR A Income with respect to FundCo Agreement	INVESTOR B Income with respect to FundCo Agreement
31 March 98	901	175
31 March 99	1,099	221
31 March 00	1,026	199
31 March 01	1,002	189
31 March 02	1,568	326
31 March 03	(254)	0
31 March 04	778	0
31 March 05	1,902	383
31 March 06	2,284	486
31 March 07	3,141	11,468
Total income	13,447	13,447

Example 2

17. Assume that the facts of example 1 are the same with the difference that on 31 March 2005, Investor B requires early settlement of the FundCo Agreement, and accordingly, in addition to receiving FundCo Variable Payments (of \$383) for the year ending 31 March 2005, Investor B also receives \$11,529.

18. The base price adjustment with respect to the FundCo Agreement will be:

$$a = \$13,022$$

b = \$5,000

c = \$1,110

$\$13,022 - (\$5,000 + \$1,110) = \$6,912$ income derived.

- \$13,022 is the sum of all amounts received by Investor B up to and including settlement, being the value of the FundCo Agreement at 31 March 05 — i.e. \$11,529 — and the aggregate FundCo Variable Payments received from 31 March 98 to 31 March 04 — i.e. \$1,110 and the FundCo Variable Payment made on 31 March 05 of \$383 (refer to the table at paragraph 7.16).
- \$5,000 is the core acquisition price.
- \$1,110 is income previously returned by Investor B to 31 March 04 (refer to the table at paragraph 7.16).

This determination is signed by me on the 14th day of February 1997.

Martin Smith

General Manager (Adjudication & Rulings)