

Updated US list of foreign currency futures contracts - starting point for Section 1256

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This Tax Alert provides an updated list of foreign currencies that are traded on qualified boards or exchanges for purposes of beginning the analysis of whether an over-the-counter contract (OTC) with respect to those currencies should be marked to market under Internal Revenue Code¹ Section 1256.² The list contained in this Alert updates the list of foreign currency futures contracts that was provided in EY Global Tax Alert, [Updated US list of foreign currency futures contracts - starting point for Section 1256](#), dated 29 January 2020.

This list is retrospective; currencies can begin (or cease) trading in futures at any time. Thus, it is imperative for taxpayers to examine contemporaneous futures trading to determine whether a specific contract will qualify as a Section 1256 contract.

Warning: This Alert lists all currencies for which there was a known regulated futures contract (RFC) offered for trading. A lack of actual trading in the RFC affects whether an OTC contract can be considered a Section 1256 contract. Some RFCs on the list appear to have had no trades in 2020. A complete lack of RFC trades (or perhaps only sporadic trades or limited volume) would prevent OTC contracts from qualifying as Section 1256 contracts. **Therefore, the list should not be viewed as definitive, but rather as a starting point in the analysis.**

Under Section 1256(a)(1), each Section 1256 contract held by a taxpayer at the close of the tax year must be marked-to-market. The term Section 1256 contract includes, among other things, any foreign currency contract.³ The term foreign currency contract is defined under Section 1256(g)(2)(A) as a contract that:

1. Requires delivery of, or whose settlement depends on the value of, a foreign currency that is a currency in which positions are also traded through regulated futures contracts
2. Is traded on the interbank market
3. Is entered at an arm's-length price determined by reference to the price in the interbank market

The legislative history provides that the statutory definition is intended to describe the characteristics of bank forward contracts used for trading currencies.

The following is a list of currencies in which positions are currently listed through regulated single futures contracts, or cross currency pairs, as of the date of this Alert. As noted later, although each of these contracts is listed, some show little or no trading in the past year.

1. Australian dollar
2. Brazilian real
3. British pound
4. Canadian dollar
5. Chilean peso
6. Chinese renminbi (offshore)⁴
7. Colombian peso
8. Czech koruna
9. Euro
10. Hungarian forint
11. Israeli shekel
12. Indian rupee
13. Japanese yen
14. Korean won
15. Mexican peso

16. New Zealand dollar
17. Norwegian krone
18. Polish zloty
19. Russian ruble
20. South African rand
21. Swedish krona
22. Swiss franc
23. Turkish lira

As described previously, provided there is sufficient trading of these currencies through regulated futures contracts, and the additional conditions described in Section 1256(g)(2)(A) are satisfied, foreign currency contracts for these currencies should be marked to market under Section 1256(a)(1).

Certain currencies, while listed previously as being offered for trading, had little or no actual trading in 2020. For example, the Chilean peso and Colombian peso had limited trading. While there was minimal trading in the Norwegian krone, Swedish krona, Israeli shekel, Czech koruna, and Hungarian forint single futures contracts, there was active trading in the cross-currency pair contracts that involved those currencies. Therefore, taxpayers need to understand the RFC trading environment around the time of entry into any OTC foreign currency contract, as well as the trading environment throughout the life of the contract.

Please consult with one of the individuals listed below before adopting the position that Section 1256 does or does not apply to any particular foreign currency contract. As described previously, this list is subject to change on an ongoing basis as new foreign currencies begin to trade in the regulated futures market and as trading in other foreign currencies becomes thin or nonexistent.

Scope

This list does not immediately reflect changes in the status of foreign currencies but is generally updated only annually. Please contact one of the individuals listed below before adopting or changing a position with respect to whether Section 1256 applies to a particular currency.

Endnotes

1. All “Section” references are to the Internal Revenue Code of 1986, and the regulations promulgated thereunder.
2. Historically, many practitioners believed that only foreign currency forwards, not options, could constitute a foreign currency contract. See Notice 2007-71 in which the Internal Revenue Service states that it and the Treasury Department do not believe that foreign currency options are foreign currency contracts as defined in Section 1256(g)(2). Whether foreign currency options are included in Section 1256 is now uncertain given *Wright v. Commissioner*, 809 F.3d 877 (6th Cir. 7 Jan. 2016), in which the Sixth Circuit held that OTC foreign currency options could be foreign currency contracts.
3. Section 1256(b)(1)(B).
4. While there is a single currency, renminbi, there are both offshore and onshore rates, and it is not clear whether these should be considered separate currencies for Section 1256 purposes. We found limited trading for the onshore currency rate on a Section 1256 qualified board or exchange.

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