This Tax Alert provides an updated list of foreign currencies that are traded on qualified futures markets for purposes of beginning the analysis whether an over-the-counter contract (OTC) with respect to those currencies should be marked to market under Internal Revenue Code Section 1256. The list contained in this Alert updates the list of foreign currency futures contracts that was provided in 2017. Please note that 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 only lists currencies for which there was a known regulated futures contract (RFC) offered for trading. Trading (or lack thereof) 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 2017. A complete lack of RFC trades (or perhaps 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. The term foreign currency contract is defined under Section 1256(g)(2)(A) as a contract that:
Requires delivery of, or the settlement of which depends on the value of, a foreign currency that is a currency in which positions are also traded through regulated futures contracts

Is traded on the interbank market

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.

Although Section 1256 may govern the timing of gains and losses on foreign currency contracts, Section 988 generally treats gains and losses on those contracts as ordinary.

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. Generally, cross-currency contracts should also be marked to market under Section 1256 if such contracts are actively traded in the futures markets. Even if the specific contracts are not themselves traded, if each of the underlying currencies to a particular contract is individually actively traded in the markets, cross-currency contracts made up of those currencies may also be subject to Section 1256(a). If only one leg of a cross-currency contract is traded in regulated futures contracts, then that contract should not generally be subject to Section 1256.

Please find below the currency contracts listed or offered for trading by qualified boards or exchanges. Although each of these contracts is listed, some, as noted, 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 (CNH, the offshore Chinese currency)
7. Chinese renminbi (CNY, the onshore Chinese currency)
8. Colombian peso
9. Czech koruna
10. Euro
11. Hungarian forint
12. Indian rupee
13. Israeli shekel
14. Japanese yen
15. Korean won
16. Mexican peso
17. New Zealand dollar
18. Norwegian krone
19. Polish zloty
20. Russian ruble
21. South African rand
22. Swedish krona
23. Swiss franc
24. Turkish lira

As described previously, provided that 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 with respect to 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 2017. For example, while there was minimal trading in the Czech koruna, Hungarian forint, and Colombian peso single futures contracts, there was active trading in the cross-currency pair contracts that involved those currencies. Additionally, certain other contracts, such as the Korean won futures contract, had limited trading across all forms. Therefore, it is important that a taxpayer understand the RFC trading environment around the time it enters into any OTC foreign currency contract, as well as the trading environment throughout the life of the 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. Note that there has been an increase in the number of offered currency RFCs in recent years that end up being thinly traded or not traded at all.

Scope

Please note that this list does not immediately reflect changes in the status of foreign currencies, but is instead generally updated only annually.
Endnotes

1. All “Section” references are to the Internal Revenue Code of 1986, and the regulations promulgated thereunder.

2. What constitutes a foreign currency contract has traditionally been limited to foreign currency forwards. See Notice 2007-71, in which the IRS 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*, No. 15-1071 (6th Cir. Jan. 7, 2016), in which the Sixth Circuit held that OTC foreign currency options could be foreign currency contracts.


4. Section 1256(b)(1)(B).

5. Section 1256(f)(2).

6. Under Section 988(a)(1)(A), any foreign currency gain or loss is treated as ordinary income or loss. Under Section 988(b)(3), in the case of a forward contract on foreign currency, any gain or loss from that contract will be treated as foreign currency gain or loss. Section 988(a)(1)(B) does, however, provide for an election to treat any foreign currency gain or loss attributable to certain forward contracts on foreign currency as Section 1256(a)(3) 60/40 capital gain or loss rather than ordinary gain or loss.

7. A cross-currency contract is a forward contract in which both legs of the contract are foreign (i.e., non-US dollar) currencies. For example, a forward contract in which the parties agree to exchange a fixed amount of Euros for a fixed amount of British pounds is a cross-currency contract.

8. Listed as a Colombian peso/US$ pair on ICE Futures US.
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EYG no. 00353-181Gbl
1508-1600216 NY
ED None

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