reasonable, the method in Determination G25 may again be used to calculate expenditure incurred.

This determination is signed by me on the 28th day of May in the year 1992.

R. D. ADAIR, Deputy Commissioner of Inland Revenue.
go5696

Determination G25: Variations in the Terms of a Financial Arrangement

This determination may be cited as "Determination G25: Variations in the Terms of a Financial Arrangement".

1. *Explanation*—(1) A financial arrangement may be varied for many reasons. It may be varied by mutual agreement between the parties, by operation of the terms of the arrangement (such as an option), or by a partial remission of debt. One way of effecting a change is by terminating the existing financial arrangement and issuing a new one. That situation is straight forward and does not need a specific determination. A base price adjustment is calculated and income or expenditure under the new financial arrangement is calculated using the yield to maturity method or an appropriate alternative.

(2) This determination applies where the variation is effected by changes to the original financial arrangement. Such changes may have been contemplated or anticipated in the original financial arrangement, for example:

(a) where there are options in the financial arrangement exercisable by either party, or

(b) where the original financial arrangement contains an intent that it will be altered in certain prescribed ways (or at the agreement of the parties) on the happening of some event.

In both these cases, at the date of acquisition, an accrual method can not be applied that will last unaltered until the maturity or other sale of the financial arrangement. This determination applies in such cases, even though the financial arrangement may set out quite clearly how it is to be altered. The determination does not apply where the terms of the financial arrangement are unequivocal as to the nature, time and amount of the changes made.

(3) At the most basic level, a variation will involve a change to the cash flows or the dates upon which they are payable.

(4) The method requires an adjustment to be made in the year of variation. The effect of the variation is that the total income or expenditure up to the end of the year of variation is equal to what it would have been had the timing and exact details of the variations been known at the date of issue or acquisition.

(5) The method is similar to that used in section 64D (4) of the Act where a taxpayer becomes a cash basis holder.

It is also similar to section 64C(2B) that gives a method of changing to the straight line method of accounting for financial arrangements from another method used.

(6) This determination does not apply to variable rate financial arrangements, where the only variation is a change in the index, price, or rate (these will be dealt with by a subsequent determination entitled Variable Rate Financial Arrangements). It does apply where a variation occurs that does not result from a change in the indicator rate. For example when the amount of principal is varied without a corresponding payment or the margin above the indicator rate is varied.

2. *References*—This determination is made pursuant to section 64E (1) of the Income Tax Act 1976.

3. *Scope of Determination*—This determination applies to any financial arrangement where the amounts payable, or the dates on which they are payable, are varied after the date of issue or acquisition, but it does not apply:

(a) To a Variable Rate Financial Arrangement (as defined in this determination) under which the only variation is a change in the economic, commodity, industrial or financial indices or prices, or banking rates or general commercial rates, or

(b) Where the variation is effected by the maturity or other termination of the financial arrangement and the issue of a new financial arrangement, or

(c) Where the variation is made according to the terms of the financial arrangement, which terms are unequivocal as to the nature, time and amount of the changes made.

4. *Principle*—The adjustment in this determination is made in the year of variation. The result is that the total accumulated income or expenditure up to the end of the year of variation is equal to that that would have applied had the changes been known at the date of issue or acquisition.

5. *Interpretation*—(1) In this determination, unless the context otherwise requires:

Expressions used have the same meaning as in the Act and where a word or expression is given a particular meaning for the purposes of sections 64B to 64M of the Act it shall have the same meaning as in the said sections 64B to 64M;

the "Act" means the Income Tax Act 1976;

"Variable Rate Financial Arrangement" means a financial arrangement under which:

(a) the interest rate is determined by a fixed relationship to economic, commodity, industrial or financial indices or prices, or banking or general commercial rates; or

(b) the interest rate is set periodically by reference to market interest rates.

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

(3) For convenience, words and phrases defined in this determination are indicated by initial capital letters. However, in the absence of a capital letter shall not alone imply that the word or phrase is used with a meaning different from that given by its definition.

6. *Method*—(1) In the income year in which a financial arrangement is varied, a person who is the issuer or holder of the financial arrangement shall include, in calculating assessable income for the income year, an amount in respect of the financial arrangement calculated in accordance with the following formula:

$a - b - c + d$, where:

a is the sum of all amounts that would have been income derived by the person in respect of the financial arrangement from the date it was acquired or issued to the end of the income year, if the changes had been known as at the date the financial arrangement was acquired or issued;

b is the sum of all amounts that would have been expenditure incurred by the person in respect of the financial arrangement from the date it was acquired or issued to the end of the income year, if the changes had been known as at the date the financial arrangement was acquired or issued;

c is the sum of all amounts treated as income derived of the person in respect of the financial arrangement since it was acquired or issued to the end of the previous income year; and

d is the sum of all amounts treated as expenditure incurred of the person in respect of the financial arrangement since it was acquired or issued to the end of the previous income year.

The amount so calculated shall: