

EXPOSURE DRAFT - FOR COMMENT AND DISCUSSION ONLYDeadline for comment: **11 October 2021**Please quote reference: **PUB00401**Send your feedback to Public.Consultation@ird.govt.nz**DETERMINATION > FOREIGN CURRENCY APPROVAL**

Foreign Exchange Rates

Issued: dd mmm 2021

FX 21/XX

This approval approves sources for foreign exchange rates that may be used by any person who is required to convert a foreign currency amount into its New Zealand Dollar (NZD) equivalent for the purposes of determining their tax liability, unless the Act requires otherwise. It also approves the use of mid-month, end of month and rolling average rates. In addition, this approval explains how the relevant exchange rate should be used to convert foreign currency amounts to their NZD equivalent.

All legislative references are to the Income Tax Act 2007 (the Act) unless otherwise stated.

Introduction

1. The Act requires foreign currency amounts to be converted to NZD to calculate a taxpayer's New Zealand income tax liability.
2. In some cases, the Act prescribes a currency conversion method or exchange rate source to use, but in most cases it does not. Where the Act does not prescribe a currency conversion method, the default method is the close of trading spot exchange rate on the date the amount is required to be measured or calculated (s YF 1(2)). However, the Commissioner can approve other rates and methods to use (s YF 1(5)) to minimise compliance costs.¹
3. The Commissioner publishes foreign currency exchange rates for certain currencies on the Inland Revenue website at <https://www.ird.govt.nz/managing-my-tax/overseas-currency-conversion-to-nz-dollars>.² The Commissioner publishes mid-month, end-of-month and rolling average rates for each currency. From 1 April 2021, the Commissioner changed the source from which she obtains the rates to the Reserve Bank of New Zealand. As a result, the number of rates published has decreased.
4. This approval approves sources from which you can obtain foreign currency exchange rates if the rates you need are not published by the Commissioner or you choose not to use them. This approval also approves the use of mid-month, end of month and rolling average rates.
5. This approval **does not apply** where the Act or Commissioner prescribes a currency conversion method, rate or source for a particular transaction or arrangement. For example, you must use currency conversion methods and exchange rate sources specified in the financial arrangements rules for financial arrangements.
6. You can choose to use other sources for foreign currency exchange rates. However, if you use a rate that is not from a source approved in this approval, you need to show that the exchange rate you are relying on is from a reputable source (such as a registered trading bank) and is appropriate given the nature of your transaction. You must also keep sufficient records in case you later need to verify the exchange rates used. This is especially important where the source of rates is not published or readily available.

¹ See for example, Inland Revenue, [FX 20/01 Approval - foreign residential rental property amounts - currency conversion \(2020\)](#).

² Inland Revenue, Ngā moni o tāwāhi – te tahuri kia tāra Aotearoa | Overseas currency – conversion to NZ dollars (webpage, last updated 20 July 2021).

7. Finally, this approval provides guidance on how foreign currency exchange rates should be used to convert foreign currency into its NZD equivalent.

Application

8. This approval applies to persons who are required to convert a foreign currency amount into its NZD equivalent for the purposes of determining their tax liability where the Act or Commissioner has not otherwise prescribed a source, conversion method or rate for that transaction.

Exchange rate sources approved

9. The Commissioner approves the following exchange rate sources under s YF 1(5):
 - the rates the Commissioner publishes on the Inland Revenue website at www.ird.govt.nz/managing-my-tax/overseas-currency-conversion-to-nz-dollars.³
 - foreign exchange rates published by a country's central bank.
10. If you use appropriate rates from these sources, those rates will be considered acceptable for converting your foreign currency amounts to NZD.
11. However, you may continue to choose to use foreign exchange rates from sources other than those approved above. If you choose to use a different source for your foreign exchange rates, the risk exists that the Commissioner will not accept the rate you selected as correctly reflecting the NZD amount for your tax position. For instance, foreign exchange rates from other sources must be appropriate given the nature of your transaction. You must not use cash or foreign cheque rates. You may need to consider other issues depending on the source of the exchange rates. These issues do not arise for the exchange rate sources approved at [9].
12. You must apply your exchange rate source consistently. This means that once you have chosen a source, you must use that source for obtaining rates for converting all foreign currency amounts for that year and in the future. If this is not possible (for example, if the exchange rate source you have been using ceases to be available), you can use a different source without notifying the Commissioner. However, you must keep a record of the change and the reasons for it.

³ Inland Revenue, Ngā moni o tāwāhi – te tahuri kia tāra Aotearoa | Overseas currency – conversion to NZ dollars (webpage, last updated 20 July 2021).

Approval of mid-month, end of month and rolling average rates

13. The default method of converting a foreign amount into its NZD equivalent involves applying the close of trading spot exchange rate on the date the amount is required to be measured or calculated. The Commissioner also approves the use of mid-month, end of month and rolling average rates where this is appropriate and allowed under the Act.
14. For currencies other than those the Commissioner publishes, these rates can be obtained as follows:
 - **Mid-month rate:** This is the exchange rate on the 15th day of the month, or if no exchange rates were quoted on that day, on the preceding working day on which they were quoted. Obtain the mid-month rates for the foreign currency from one of the foreign exchange rate sources approved at [9].
 - **End of month rate:** This is the exchange rate for the last day of the month. Obtain the end of month rate from one of the foreign exchange rate sources approved at [9].
 - **Rolling average rate:** This is the average of the mid-month exchange rate for the relevant month and the previous months in the relevant period. For example, a rolling 12-month average would be the mid-month exchange rate for the relevant month and the previous 11 months. You can obtain the mid-month rates for the foreign currency from one of the foreign exchange rate sources approved at [9]. You calculate the rolling average rate by adding together the mid-month rates for all the months in the period, and then dividing by the total number of months in the period. This calculation is illustrated in Example 1.

Example 1: Rolling average rates

Jamie needs to find the rolling 12-month average rate for the Samoan tala (SAT⁴) for March 2021 because Inland Revenue no longer publishes it.

She goes to the Central Bank of Samoa website, selects "Statistics", "Exchange Rates", "Daily Exchange Rates" (www.cbs.gov.ws/statistics/exchange-rates/daily-exchange-rates/) and downloads the Historical Daily Rates schedule. From that

⁴ Some publications use the abbreviation WST, which reflects the country's earlier name of Western Samoa (used up to 1997).

schedule she identifies the mid-month SAT/NZD exchange rate for March 2020 and the preceding 11 months, as follows:

Month	Rate (for 1SAT)
March 2021	0.5516
February 2021	0.5502
January 2021	0.5492
December 2020	0.5532
November 2020	0.5619
October 2020	0.5718
September 2020	0.5709
August 2020	0.5786
July 2020	0.5770
June 2020	0.5802
May 2020	0.6034
April 2020	0.5953
Total	6.8433

To determine the rolling average rate for March 2021, Jamie needs to add the rates for March 2021 and the preceding 11 months together and then divides the resulting number by 12 ($6.8433 \div 12$).

This gives rise to a rolling 12-month average rate for March 2021 of 1SAT = 0.5703NZD.

Currency conversion methods

Finding the mid-rate

15. Before you convert a foreign currency amount to NZD, you need to determine the right exchange rate. Inland Revenue quotes only one rate per currency, but other foreign exchange rate sources may list two rates for the relevant currency. These rates are:
 - a **Bid Rate** or **Buy Rate**, which is the exchange rate at which the service provider is willing to purchase the foreign currency; and
 - an **Offer Rate** or **Sell Rate**, which is the exchange rate at which the service provider is willing to sell the foreign currency.
16. In this case, you need to calculate the "mid-rate" by adding the two rates together and then dividing that number by two. You then use the mid-rate in our calculations.

Currency conversion calculations

17. Foreign exchange rates are quoted in two ways, which gives rise to two methods of calculating the currency conversion.

New Zealand Dollar as the base currency

18. Exchange rates can be quoted with the NZD as the base currency. This is the way Inland Revenue expresses its rates. This means the exchange rate is expressed based on the amount of foreign currency that it would take to purchase one NZD. For example, on 31 March 2020, the Reserve Bank of New Zealand was quoting the:
- NZD/USD (United States Dollar) foreign exchange rate as 1NZD = 0.5997USD
 - NZD/AUD (Australian Dollar) foreign exchange rate as 1NZD = 0.9740AUD.
19. **Where the exchange rate is quoted with NZD as the base currency**, you need to **divide** the foreign currency amount by the exchange rate to calculate the NZD equivalent of the foreign currency amount.
20. This means that based on the above AUD rate as at 31 March 2020 the NZD equivalent of AUD50,000 is:

$$\begin{aligned}\text{NZD equivalent} &= \text{AUD}50,000/0.9740 \\ &= \text{NZD}51,334.70\end{aligned}$$

21. This is illustrated in Example 2 and Example 3.

Example 2: Converting a United States dollar amount to its New Zealand dollar equivalent

On 1 April 2021 Madison enters into an USD100,000 term investment for one year with a US bank. Madison needs to calculate the NZD opening balance equivalent amount of her investment.

Madison goes to the Reserve Bank of New Zealand's website www.rbnz.govt.nz, selects "Statistics", "B1 Exchange rates and TWI" and downloads the spreadsheet "Exchange rates and TWI – B1 Daily (2018-current)". In column C of that spreadsheet, Madison identifies the NZD/USD exchange rate of 0.6981 for 1 April 2021. Madison could also have obtained the same rate from the Inland Revenue website.

The exchange rate is quoted with the NZD as the base currency (that is, it will take 1NZD to purchase 0.6981USD). Therefore, Madison must divide the opening balance by the exchange rate. Madison's opening balance is calculated as:

$$\begin{aligned}\text{Opening balance} &= \text{USD}100,000/0.6981 \\ &= \text{NZD}143,245.95\end{aligned}$$

Example 3: Converting an Australian dollar amount to its New Zealand dollar equivalent

Having recently come into some money, Madison (from Example 2) enters into an AUD500,000 term investment for one year with an Australian bank. She also needs to calculate the NZD opening balance equivalent amount of this investment.

Madison follows the same steps as described in Example 2 and in column E of the spreadsheet identifies a NZD/AUD exchange rate of 0.9195 as at 1 April 2021.

This exchange rate also quotes the NZD as the base currency. Therefore, Madison must divide the opening balance by the exchange rate. Madison's opening balance is calculated as:

$$\begin{aligned}\text{Opening balance} &= \text{AUD}500,000/0.9195 \\ &= \text{NZD}543,773.79\end{aligned}$$

Foreign currency is the base currency

22. Alternatively, exchange rates can be quoted with the foreign currency as the base currency. This means the exchange rates are expressed on the basis of the amount of NZD it takes to purchase one unit of a foreign currency. This is likely to be the case on other central bank webpages where the local currency is expressed as the base currency. For example, on 31 March 2020 the Reserve Bank of Australia quoted the AUD/NZD exchange rate as 1AUD = 1.0257NZD.
23. **Where the exchange rate is quoted with the foreign currency as the base currency**, you need to **multiply** the foreign currency amount by the relevant exchange rate to calculate the NZD equivalent of the foreign currency amount.

24. This means that based on the above AUD rate as at 31 March 2020 the NZD equivalent of AUD50,000 is:

$$\begin{aligned}\text{NZD equivalent} &= \text{AUD}50,000 \times 1.0257 \\ &= \text{NZD}51,285\end{aligned}$$

25. This is illustrated in Example 4.

Example 4: Converting an Australian dollar amount with the Australian dollar as the base rate

On 1 April 2021 Jarli enters into an AUD100,000 term investment for one year with an Australian bank. Jarli needs to calculate the NZD opening balance equivalent amount of his investment.

Because Jarli has used rates from the Reserve Bank of Australia for amounts he has needed to convert to NZD in other years, he continues to use that bank's website (www.rba.gov.au). He selects "Statistics", then "Exchange Rates", and then scrolls down to "Historical Data" and downloads the spreadsheet "Exchange rates – Daily – 2018 to Current". He identifies in column L of that spreadsheet an AUD/NZD exchange rate of 1.0849 for 1 April 2021.

Jarli notes that the AUD/NZD exchange rate is quoted with the AUD as the base currency. Therefore, Jarli must multiply the opening balance by the exchange rate. Jarli's opening balance is calculated as follows:

$$\begin{aligned}\text{Opening balance} &= \text{AUD}100,000 \times 1.0849 \\ &= \text{NZD}108,490\end{aligned}$$

Finding a rate where NZD is not quoted

26. For some currencies, a rate may not be quoted where the foreign currency is expressed in terms of the NZD. In that case, you need to manually calculate the exchange rate against the NZD for that currency. The method for calculating the NZD exchange rate is as follows:

- **Step 1:** Determine the NZD/USD exchange rate
- **Step 2:** Determine the exchange rate for the foreign currency against the USD
- **Step 3:** Use the rates expressed against the USD to calculate the NZD rate against the other currency. The method for doing this last step will depend on

whether the USD/foreign currency rate is expressed with the USD or the foreign currency as the base rate.

27. You should use this method only when no rate is quoted for the foreign currency in NZD. Most of New Zealand's usual trading partners do quote a NZD exchange rate. Where that is not the case, the USD is usually expressed as the base rate. Example 5 below shows how to calculate the exchange rate where this is the case.
28. Where **the foreign currency is expressed against the USD with the USD as the base rate**, you need to **multiply** this rate by the NZD/USD exchange rate on the same day to determine the exchange rate against the NZD for that currency.
29. For example, to find the NZD/NGN (Nigerian naira) exchange rate on 31 March 2021 take the following steps:
 - **Step 1:** Determine the NZD/USD exchange rate. On 31 March 2021, the Reserve Bank of New Zealand quoted the NZD/USD Foreign Exchange Rate as 1NZD = 0.6989USD.
 - **Step 2:** Determine the exchange rate for the foreign currency against the USD. On 31 March 2021, the Central Bank of Nigeria quoted the USD/NGN as 1USD = 379.50NGN.
 - **Step 3:** Use the rates expressed against the USD to calculate the NZD rate against the other currency. Because the USD/NGN exchange rate is expressed with the USD as the base rate, it is necessary to **multiply**, as follows:
$$\begin{aligned}\text{NZD/NGN exchange rate} &= \text{USD/NGN exchange rate} \times \text{NZD/USD exchange rate} \\ &= 379.50 \times 0.6989 \\ &= 265.23\end{aligned}$$
30. This means that as at 31 March 2021, 1NZD = 265.23NGN.

Example 5: Calculating a New Zealand dollar cross rate

On 31 May 2021 Yasmin needed to calculate the NZD equivalent amount of income she had received in Nigerian naira (NGN) in exchange for helping a Nigerian prince. She went to the Central Bank of Nigeria website (www.cbn.gov.ng) selected "Statistics", then "Exchange rates", but could not find an NGN exchange rate expressed against the NZD. However, the NGN was expressed against the USD as 1USD=409.50NGN.

As the USD/NGN rate was expressed with the USD as the base rate Yasmin multiplied this rate against the NZD/USD foreign exchange rate of 0.7252 as at

31 May 2021. Having done so she found a NZD/NGN exchange rate as at 31 May 2021 of 1NZD=296.97NGN.

References

Legislative references

Income Tax Act 2007, s YF 1(2), (5)

Other references

Inland Revenue, *FX20/01: Approval – foreign residential rental property amounts – currency conversion* (2020), www.taxtechnical.ird.govt.nz/determinations/foreign-currency/foreign-residential-rental-properties/fx-20-01.

Inland Revenue, *Ngā moni o tāwāhi – te tahuri kia tāra Aotearoa | Overseas currency – conversion to NZ dollars* (webpage, last updated 20 July 2021), www.ird.govt.nz/managing-my-tax/overseas-currency-conversion-to-nz-dollars

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