Inland Revenue
Te Tari Taake

FX 20/01: Approval – foreign residential rental property amounts – currency conversion

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

Introduction

2. The Act requires foreign currency amounts to be converted to New Zealand dollars to calculate a taxpayer's New Zealand income tax liability.

3. 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 or exchange rate source 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 methods and rates to use (s YF 1(5)) to minimise compliance costs.

4. This Approval approves an annual and a monthly currency conversion method and exchange rate sources that may be used instead of or in conjunction with the spot rate (s YF 1(5)).

Application

5. This Approval only applies to:

- individuals who own foreign residential rental property, which for the purposes of this Approval include:
    - an individual partner of a partnership who has an interest, as a partner, in a foreign rental property;
    - an individual acting in their capacity as trustee;
- individuals who are:
    - New Zealand residents; or
    - non-resident trustees to whom s HC 25(2) applies (see Interpretation Statement "IS 18/01: Taxation of Trusts – income tax" *Tax Information Bulletin* Vol 30, No 7 (August 2018): 17); and
- foreign currency amounts derived from or incurred on residential rental property, including rent, premiums, inducements, early termination payments, rates, insurance, levies, repairs and maintenance costs, acquisition costs, sale proceeds, improvement costs and construction costs.

6. This Approval does not apply where the Act prescribes a currency conversion method or exchange rate source for a particular transaction or arrangement. For example, for financial arrangements, currency conversion methods and exchange rate sources specified in the financial arrangements rules must be used. Note that a foreign loan used to finance a foreign residential rental property may be a financial arrangement.

Currency conversion methods and exchange rate sources approved

7. You may use one of the currency conversion methods or exchange rate sources in this Approval instead of the spot rate (s YF 1(5)).

8. An example showing the use of the methods and exchange rate sources is provided at the end of this Approval.

9. If you want to use a method or exchange rate source not outlined in this Approval, apply to the Commissioner for approval to use that method or source (email fxconversions@ird.govt.nz).

Currency conversion methods

10. The Commissioner approves the annual and the monthly currency conversion methods for converting foreign currency amounts related to foreign residential rental properties to New Zealand dollars. These methods are explained below.

11. Use of the annual and monthly methods is subject to the conditions outlined in [24] to [27]. The Commissioner approves the use of these methods in conjunction with amounts converted to New Zealand dollars during the year at the spot rate.

Exchange rate sources

12. The Commissioner approves the following exchange rate sources under s YF 1(5):

    - the foreign exchange rates published by Inland Revenue on its website (www.ird.govt.nz/managing-my-tax/overseas-currency-conversion-to-nz-dollars);
    - foreign exchange rates from another reputable source.

13. Use of these exchange rate sources is subject to conditions outlined in [30] to [36].

Currency conversion methods

14. You may use either the annual method or the monthly method for converting foreign currency amounts derived from, or incurred on, your foreign residential rental property.

15. If you choose to use the annual method or monthly method you must use it consistently. However, you may use it in conjunction with amounts converted to New Zealand dollars at the spot rate on the day of the relevant transaction. For example, the annual method or monthly method may be suitable for rental income streams and recurring rental expenditure. The spot rate may be suitable for one-off rental income and expense amounts, such as a gain derived on the sale of a residential rental property, annual tax payments, or the purchase of an item of depreciable property.

Annual method

16. Under the annual method, instead of converting foreign currency amounts on a daily basis, amounts are aggregated and converted at the end of the income year using an annual rate.

17. If using the exchange rates published by Inland Revenue, and the relevant period is a period of 12 months, you can use the rolling 12-month average of mid-month rates provided by Inland Revenue as the annual rate.

18. Otherwise, the annual rate is calculated by adding together the exchange rates for the 15th day of each month in the relevant period (usually 12 months) and then dividing that total by the number of months in the relevant period (usually 12) to arrive at a single annual exchange rate.

19. If you are using an exchange rate source that does not provide exchange rates for the 15th day of each month, then an alternative monthly rate can be used, eg end-of-month or monthly average.

Monthly method

20. Under the monthly method, instead of converting foreign currency amounts on a daily basis, amounts are aggregated and converted at the end of each month using a monthly rate.

21. The monthly rate is based on the exchange rate for the 15th day of the month.

22. If you are using an exchange rate source that does not provide exchange rates for the 15th day of each month, then an alternative monthly rate from the same exchange rate source can be used, eg end-of-month or monthly average.

Amounts converted to New Zealand dollars during the year

23. You may use the annual method or monthly method in conjunction with amounts converted to New Zealand dollars during the income year using spot rates. For example:

- If you paid foreign tax and converted the amount to New Zealand dollars using the spot rate on the day it was paid, you may use the converted amount;
- If you purchased an item of depreciable property in foreign currency and converted the foreign currency amount using the spot rate on the day you paid it, you may use the converted amount;
- If you used a New Zealand credit card to pay a foreign rental expense you may use the New Zealand dollar amount charged to your credit card.

Conditions for use of currency conversion methods

24. You do not need to notify the Commissioner that you will be using the annual method or monthly method to convert your foreign currency amounts to New Zealand dollars.

25. If you choose to use the annual method or monthly method you must use it consistently. For example, if you choose the annual method and use it for residential rental income and recurring residential rental expenditure, you must use it every year for all such income and expenditure. If, in conjunction with the annual method, you use spot rates for residential rental property related tax payments and amounts paid for items of depreciable property, you must use spot rates every year for all such payments and amounts.

26. You must use the method you choose for all:

- residential rental properties you may purchase in the future;
- your foreign residential rental properties if you own more than one.

27. However, you can ask the Commissioner for approval to change to a different method (email fxconversions@ird.govt.nz).

Exchange rate sources

Approval of exchange rate sources

28. For the purposes of this Approval, the Commissioner has approved the following foreign exchange rate sources under s YF 1(5):

- Foreign exchange rates published by Inland Revenue on its website (www.ird.govt.nz/managing-my-tax/overseas-currency-conversion-to-nz-dollars) which include mid-month and rolling 12-month average rates.
- Foreign exchange rates from another reputable source. For example, exchange rates published on the Reserve Bank of New Zealand website (www.rbnz.govt.nz) or rates obtained from a registered bank. Registered banks are listed on the Reserve Bank of New Zealand website (www.rbnz.govt.nz/regulation-and-supervision/banks/register).

Non-trading days

29. Some of the foreign exchange rate sources listed may provide rates for only trading days. If the relevant day of the month is not a trading day, you must use the foreign exchange rate on the preceding trading day.

Conditions

30. Foreign exchange rates from another reputable source must be appropriate given the nature of your rental activity. For example, this will normally mean using retail rather than wholesale rates.

31. Cash and foreign cheque rates must not be used.

32. Where the other reputable source provides exchange rates in the form of buy and sell rates, the average of the corresponding buy and sell rates must be used.

33. You must 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.

34. An exchange rate source must be applied consistently. This means that once you have chosen a source you must, if possible, use that source:

- for all future conversions, including for properties you may purchase in the future.
- for all of your foreign rental properties (if you own more than one).

35. If this is not possible (eg, 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.

36. In other cases, you can ask the Commissioner for approval to change to a different exchange rate source (email fxconversions@ird.govt.nz).

Example

Lucy is a New Zealand tax resident who is not a transitional resident. She has an apartment in France that she rents out.

She has the following income and expenditure (excluding interest on the foreign loan she used to buy the apartment) for the property during the income year in Euro (EUR):

		Annual
Income		
Rent (50 weeks)	€400 a week	€20,000
Expenses		
Rates	€75 a month	€900
Levies and insurance	€300 a month	€3,600
Repairs and maintenance	€500 one-off	€500
Total expenses		€5,000
Net rental income (excluding interest and depreciation)		**€15,000**

Lucy bought a new fridge for the apartment half-way through the year using her New Zealand credit card. The fridge cost EUR3,000 and NZD5,242.54 was charged to her credit card.

Lucy chooses to use the annual method to convert the rental income and expenses (excluding interest and depreciation). She uses the rates published on Inland Revenue's website, which include rates for converting Euro into New Zealand dollars.

The average of the exchange rates for each month during the income year is NZD0.5714 to EUR1. This is already calculated in the rates published by Inland Revenue in the "Rolling 12-month average" table.

Because she is using an annual method, Lucy can aggregate each income and expenditure type for the year and apply the annual rate to the aggregated amounts:

Income: Lucy has EUR20,000 of rental income for the year: EUR20,000 divided by 0.5714 = NZD35,001.75.

Expenses: Lucy has EUR5,000 of rental expenses for the year (excluding interest and depreciation): EUR5,000 divided by 0.5714 = NZD8,750.44.

Lucy also needs to calculate the depreciation deduction on the fridge. Lucy chooses to do this using the actual conversion amount of NZD5,242.54 charged to her credit card instead of the annual method.

Lucy claims a depreciation deduction for the fridge (for 6 months' use) using a diminishing value rate of 25%:

NZD5,242.54 multiplied by 6/12 multiplied by 25% = NZD655.32

Lucy also needs to calculate her interest deduction on the loan she used to buy the apartment. To do this Lucy needs to apply the financial arrangements rules, including the foreign exchange method and source required by those rules. Doing so, Lucy calculates she has an interest deduction of NZD12,513.56. Note that Lucy may also have a non-resident withholding tax obligation on the interest she pays to the lender.

As a result, Lucy's net rental income (NZD) is:

Income	$35,001.75
Expenses (other)	$8,750.44
Depreciation	$655.32
Interest	$12,513.56
Net rental income	**$13,082.43**

Lucy paid EUR2,370 tax in France on income derived from the rental property.

She converts this using the spot rate on the day she paid the tax in France:

EUR2,370 divided by 0.5732 = NZD4,134.68

Lucy may be allowed foreign tax credits for some or all of this amount under the provisions of the DTA with France and subpart LJ.

References

Subject references

Currency conversion
Exchange rate
Foreign currency amount

Legislative references

Income Tax Act 2007, ss YA 1, YF 1

Related rulings/statements

"IS 18/01: Taxation of Trusts – income tax" *Tax Information Bulletin* Vol 30, No 7 (August 2018): 17

"IS 20/06: Income tax – Tax issues arising from ownership of foreign residential rental property" *Tax Information Bulletin* Vol 32, No 7 (August 2020)

"IS 20/07: Income tax – Application of the financial arrangements rules to foreign currency loans used to finance foreign residential rental property" *Tax Information Bulletin* Vol 32, No 7 (August 2020)