Foreign currency balances and transactions

If you conduct any business transactions in foreign currency, hold foreign assets or receive income from overseas, you need to consider the tax consequences flowing from these. For foreign currency transactions, you must prepare calculations and accounts of the income (or expenses) stated in New Zealand dollars (NZD) to determine the tax payable on that taxable income.

Foreign currency balances and amounts must be converted to NZD according to specific tax rules:

- Assets such as shares, life insurance, and superannuation entitlements denominated in a foreign currency may give rise to taxable income for NZ resident taxpayers and accordingly may need to be converted to NZD to determine any tax payable arising on such assets
- Any business conducted overseas through a branch (which may include staff working overseas intermittently or temporarily) may require NZ tax to be returned on this, and accordingly all foreign income and expenses will need to be converted into NZD

Further considerations arising from foreign currency balances and transactions include disclosure requirements (including under the Foreign Account Tax Compliance Act) and the calculation of withholding or approved issuer levies on interest or royalty payments paid in foreign currency.

Transactions in foreign currency

For amounts not subject to the financial arrangement/foreign investment fund or controlled foreign company rules, Inland Revenue allows the use of the following:

- Inland Revenue published exchange rates
- Foreign exchange rates published by RBNZ
- Foreign exchange rates published by another foreign central bank (the link provided is the US Federal Reserve bank as an example; Euro Reserve bank rates are another)

The accepted conversion methods are:

- Daily rate
- Mid-month rate
- End-of-month rate
- Rolling average rate

Inland Revenue will approve the rates chosen where their use is appropriate for the transactions being converted to NZD, e.g.

- Significant and one-off transactions – daily rate
- Large volume of repeated transactions – rolling average rate
- Income/expenditure incurred regularly – mid-month, end-of-month or rolling average

Where a source quotes two rates, such as the buy rate and sell rate (or bid rate and offer rate), then average these two rates:

- Exchange rates require 4 decimal place accuracy
- Where NZD are not quoted, then cross-rate calculations are required (most use the USD cross rate)

Balances in foreign currency

Determining the timing of tax payable on foreign currency bank accounts and foreign currency loans will depend on whether the accounts and/or loans are subject to the financial arrangements rules. Where foreign currency bank accounts or loans are required to be accounted for under the financial arrangement rules, then income (and expenditure) in relation to amounts are required to be spread under the accrual rules, and both unrealised and realised foreign exchange movements are required to be returned as well. Where the income/expenditure is required to be spread, then conversion rates are to be applied according to Inland Revenue determinations (for example, Determination G9A).

Where the amounts are not subject to the financial arrangements rules, then amounts received (interest etc) are returned when received/credited and foreign exchange movements are accounted for when the instrument matures (either closed/exchanged or is terminated).

Foreign currency bank accounts and foreign currency loans which are not subject to the financial arrangements include:

- All bank accounts (including NZD) amount to less than NZD$50,000
- A loan in a foreign currency which is by a cash-basis person (see below) and is for private or domestic purposes

What is a 'cash basis person'?

A 'cash basis person' also is not required to spread income/expenditure under the accruals rules, and account for unrealised foreign exchange movements. Cash-basis persons can calculate income on applicable instruments when income is received/credited and foreign exchange movements when realised (that is, when the instrument matures.

A 'cash basis person' is a person who meets one of the following:

- The absolute value of all financial arrangements is NZD$1,000,000 or less, or
- The absolute value of income and expenses is NZD$100,000 or less

In addition to falling within one of the above, to come within the requirements to be a cash basis person, there is an extra requirement that the income that would be deferred under an accrual basis compared to a cash-basis must not be more than NZD $40,000.

Foreign shares

If you hold shares in foreign companies (that is, companies that are not resident in New Zealand), then tax on any change in value of these shares may require to be calculated under either the Foreign Investment Fund (FIF) rules or the Controlled Foreign Company (CFC) rules. There are various exemptions from the FIF and CFC rules, however if no exemptions apply then FIF or CFC income is required to be calculated under one of the prescribed methods under the tax rules.

Please refer to the FIF fact sheet and calculators for more detailed information.

Foreign life insurance/superannuation

FIF investments, and distributions or receipts from foreign life insurance or superannuation may be required to be returned for New Zealand tax purposes. To determine the amount of tax payable on such instruments, a prescribed method and accepted currency conversions must be used.

Overseas branch operations

Where business is conducted overseas, then a foreign branch may exist. This may already be subject to foreign tax, but NZ tax will also be required to be returned (if this occurs, then a NZ tax credit may be available for foreign tax paid, either under the New Zealand tax rules or the relevant Double Tax Relief Treaty. Refer to IS 21/09 which sets out the IR's interpretation on calculating foreign tax credits available on foreign income. Foreign currency conversion using one of Inland Revenue's accepted methods will also be required.

Distributions from foreign trusts

Certain distributions from foreign trusts which may include beneficiary income, distributions of corpus and capital profits may be taxable when received by New Zealand beneficiaries. Refer IS 19/04 for a summary of the tax rules applying to distributions from foreign trusts. Where distributions are received and they are taxable, conversion to NZD using an IR accepted method (refer Transactions in foreign currency above) will be required.

Other implications

Disclosure obligations may also arise under the Foreign Account Tax Compliance Act (FATCA) rules. The FATCA is specific United States legislation which applies to US citizens, tax residents and entities but also certain non-US persons (which includes New Zealand persons) which have accounts in the United States.

New Zealand has entered into a FATCA intergovernmental Agreement with the United States under which New Zealand financial institutions (which includes banks) are required to provide specified identity and financial information about accounts to Inland Revenue, which in turn will be provided to the United States under the Double Tax Agreement between New Zealand and the United States.

Withholding and Approved Issuer Levy obligations may also apply to payments made overseas in foreign currency. This will depend on the nature of the payment being made. Payments of a passive nature, including interest, royalties and dividends are subject to withholding obligations regardless of whether they are paid in New Zealand dollars or a foreign currency.

Examples

The following examples are for a New Zealand resident taxpayer, who is taxable on worldwide income from:

- foreign currency bank account
- foreign currency bank account
- foreign currency loan
- purchases of stock in foreign currency

Foreign currency bank account

On 1 April 2021, you open a USD account with a NZ branch of a US bank and deposit US$500,000. During the year ended 31 March 2022, interest of US$20,000 was credited to the account on 30 September 2021. As at 31 March 2022, the balance of the USD account was US$520,000.

If you are cash basis holder (see above), then the interest credited to the account will need to be converted on the date of credit into New Zealand dollars and returned as income in your tax return. The movement in the value of the balance of the bank account, when converted into New Zealand dollars will not be required to returned in your tax return. However, when the bank account is closed, a calculation on the foreign exchange movement in the value (as it is now realised) will be required and returned as taxable income.

However, if you are not a cash basis holder then the unrealised movement of the value of the bank account in New Zealand dollars (together with the interest) is required to be returned as taxable income (or a taxable loss). Prescribed calculations under Determinations G9A and/or G9C are required to determine the taxable income of the unrealised movement in the balance and the interest accruing on the account.

Note, if the amount of this bank account together will all other bank accounts was less than NZ$50,000 then only the interest received (converted into New Zealand dollars) would be required to be returned. No unrealised or realised movement (that is, when the bank account is closed, and funds withdrawn) is required to be returned for income tax.

Foreign currency loan On 1 April 2021 you borrow AUD$700,000 from an Australian bank to fund the purchase of a commercial property investment in Australia. Interest is payable monthly and principal repayments are also made monthly. If you are a cash basis person, then exchange gains or losses are returned on a realised basis (for example, when the loan is repaid). If the interest is deductible for income tax, then the interest payments will be converted on the date of payment into New Zealand dollars. If you are not a cash basis person, then the unrealised foreign exchange movement on the loan and accrual income and expenditure must be calculated under prescribed rules (Determinations G9A and G9C). Note also withholding tax (or an approved issuer levy) may be applicable on payments of the interest.
Foreign currency rental income You own a commercial property in Australia and receive a monthly amount of AUD5,000 as rental for this property. Each monthly amount will be required to be converted into New Zealand dollars on the date of receipt. As this is the only receipt during the month, the daily rate would be the most appropriate, rather than a mid-month or end of month rate. However, if there are many foreign currency transactions relating to this property (for example expenses, or split income receipts on different days of the month), then a mid-month or end of month rate may be more appropriate. Where the foreign currency is received in New Zealand (and converted into New Zealand dollars) then the foreign exchange amount realised on conversion into New Zealand dollars will be required to be returned for New Zealand income tax purposes.
Purchases of stock in foreign currency As part of your retail business, you make purchases of stock from overseas suppliers who invoice you in foreign currency. The purchases are made at least monthly, and to ensure enough stock is held for the busy summer season, some months may involve 4 – 5 separate purchases. The foreign exchange amount required to be returned for New Zealand income tax will be the amount of foreign exchange incurred on the actual payment of each invoice. Your accounting system may convert invoice amounts on the date of receipt of the invoice, and then calculate a foreign exchange gain/loss on the payment of the invoice (which may be a later date). In this case, the amount required to be returned for income tax is the amount calculated on the payment of the invoice, that is, the amount calculated in New Zealand dollars on the receipt of the invoice together with the foreign exchange gain/loss calculated when the actual payment is made.