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By PwC Deutschland | 06 April 2011

No deduction for private currency speculation losses before 2009

The Supreme Tax Court has refused a taxpayer a deduction for a series of short-term losses incurred through speculating in foreign currencies.

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A taxpayer speculated in foreign currencies essentially by taking out a series of short-term loans in, typically, Yen and Swiss Franks. He used these funds to purchase short-term fixed interest notes and securities in these and other currencies. He carried out the transactions through two Luxembourg banks. His objective was to achieve an overall interest surplus and net exchange gain over the course of the year. His actual achievement was net income of DM 17,600 and total net exchange losses of DM 590,000. The tax office chose to tax the income and ignore the losses. The taxpayer claimed offset of the losses against the income as both had arisen in the context of an "overall investment concept".

The Supreme Tax Court has now held in favour of the tax office. The income was interest and its liability to tax was not in dispute. In the view of the taxpayer, the exchange losses were partly costs of earning the interest income and partly short-term capital losses in their own right. However, the court held that they were neither. Those incurred on the securities held were not costs of earning interest income, as they were unconnected with that income. Rather, they had arisen through transfers within the private sphere of the taxpayer's asset and wealth management. Those incurred on the loan liabilities did not qualify as short-term capital losses, as no asset had been acquired. Rather, a loan had been taken up and had been repaid on maturity.

The situation is now different. With the advent of the 25% flat-rate taxation of private investment income as of January 1, 2009, there is no longer any distinction between capital gains and interest earned. Exchange rate differences have also been brought into the net. Thus, the losses here at issue would be recognised under present law. However, their offset would be confined to income of like character. The balance remaining would then be carried forward.

Supreme Tax Court judgment VIII R 58/07 of November 30, 2010 published on April 6, 2011

Keywords

capital gain, exchange loss, foreign currency, investment income