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By PwC Deutschland | 11 June 2015

Non-deductible loss on investment can include exchange loss

The ECJ has held that if a country excludes capital gains and losses on investments from taxation, the exclusion may also extend to that part of the loss that directly resulted from exchange rate fluctuations.

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A Swedish company wished to close down its UK subsidiary. Over the course of time it had progressively increased its investment with cash contributions to the subsidiary's working capital. Since the Swedish crown had strengthened against the pound, the return of the capital invested (or the sale of the investment) led to a book loss for the parent. The tax authorities refused to allow a deduction for this loss on the grounds that it was a capital loss on liquidation of an investment non-deductible for a corporation in parallel with the exemption for corresponding capital gains.

The ECJ has now held that the lack of a deduction for the foreign exchange element of a capital loss is not a hindrance on a company's freedom of establishment. The non-deductibility of capital losses is balanced by the exemption for gains. This applies to investments at home and abroad and is non-discriminatory. The fact that an exchange gain or loss is only likely in respect of an investment abroad is not discrimination, but, rather, a consequence of separate currencies. Neither of the two countries involved is required to adjust its tax system to conform to that of the other. A non-deductible expense (in this case) must therefore be accepted.

The ECJ case reference is C-686/13 *X* judgment of June 10, 2015.

Keywords

capital gain, capital loss, exchange gain or loss, exchange rate, loss on investment