

Taxation of Foreign Exchange Gains and Losses

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Abstract

This essay explores how to deal with the risk of fluctuating foreign exchange rates from the view of tax law. This issue is worth discussing when cross-border business develops vigorously nowadays.

Firstly, in the case of “cross-border asset trading” and “cross-border financing” of profit-seeking enterprise, there is an inconsistency between financial accounting and tax accounting, which leads to a dispute of when is the “realization” of foreign exchange gains and losses between tax authority and taxpayer. That is, is it necessary to “settle” foreign currency in NTD before recognizing foreign exchange gains and losses? Concerning “Realization Principle” and “Imparity Principle” in accounting, some judicial practice should be reviewed.

Secondly, in the case of “Overseas Permanent Establishment” of profit-seeking enterprise, if there are foreign exchange gains and losses due to the settlement of the profit of overseas PE, these gains and losses should belong to domestic head office or PE itself? Concerning the exemption of foreign income from overseas PE under some tax treaty which could bring these gains and losses to a “No Man’s Land” of taxation, this issue is worth our in-depth discussion.

Also, in the case of “Overseas Investment Company” controlled by domestic profit-seeking enterprises, there are “Permanent Converting Method”

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and “Qualifying Date Method” to change the profit of “Controlled Foreign Company” into NTD. This essay analyzes the pros and cons of the two methods, and wish to provide some materials for following discussions and reflections of taxation of foreign exchange gains and losses.

Keywords: Foreign Currency, Exchange Gains or Losses, Fluctuations in Exchange Rates, Realization Principle, Imparity Principle, Permanent Establishment, Controlled Foreign Company, Permanent Converting Method, Qualifying Date Method