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Receipt for repurchase obligation to be deferred until expiry

The Supreme Tax Court has held that the additional proceeds from the sale of goods with an option for the buyer to require repurchase shall be deferred until the option expires.

A motor car dealer gave bulk buyers the choice of a larger discount or a repurchase obligation. The discount differential was 4% of the list price of the vehicles; the repurchase price was agreed in advance in the form of a time-based scale for the period between sale and repurchase. If the buyer did not require repurchase by a set deadline, his right to do so lapsed. Effectively, he thus held a put option against the dealer.

The dealer honoured his repurchase obligations as demanded by his customers, but made a large loss as a result. The tax office refused to recognise this loss until the repurchased vehicles had been resold or scrapped. Its reasoning was that up to that time, the loss was merely threatening to materialise, but its actual incidence remained uncertain. Tax recognition of a threatened loss is excluded by a specific provision of the Income Tax Act.

The Supreme Tax Court has now held, following its earlier case law, that the grant of an option is a separate transaction from its exercise. It is also separate from the original sale of the goods to which it relates. Thus, its proceeds or option premium were paid to the grantor, the dealer, for his willingness to accept a repurchase obligation for a certain period of time. The option premium had not been earned until then and thus should not be taken to income. The court had previously held that an option premium of this nature cannot be taken to income over time, as in the nature of things exercise is more likely towards the end of the period than at the beginning. In the absence of other evidence, it was reasonable to estimate the option premium to be deferred on the basis of the 4% discount differential in the dealer's original offer. On the other hand, the court also held that there can be no recognition of a future loss ultimately incurred on the subsequent resale of the goods. This loss was only a threat whilst the repurchase obligation was still outstanding and thus fell under a specific statutory prohibition.

Supreme Tax Court judgment I R 83/09 of November 17, 2010 published on February 23, 2011

Schlagwörter

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