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By PwC Deutschland | 30 December 2015

No deduction for knock-out option losses

The Supreme Tax Court has held that lapsed options based on market rate movements rather than on a conscious decision by the taxpayer are not deductible from investment income.

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A taxpayer invested heavily in “knock-out” options, that is in option contracts for securities or currencies that automatically lapse once the spot price of the subject of the option passes a certain point on the given market. The tax office refused to allow a deduction for his substantial losses from the write off of the premiums paid for now unexercisable and thus worthless options, on the grounds that these option lapses were not losses from a taxable activity – investment or speculation. The Supreme Tax Court has now confirmed this view. In reaching this decision, the court drew a distinction between allowable option losses and disallowable lapses. An allowable loss follows from a conscious decision of the taxpayer to exercise or sell the option in order to avoid a further decline in value, or to allow it to expire unexercised by its due date. In the latter event, the loss is the option premium now forfeit. An irrelevant loss from an option lapse, on the other hand does not result from a decision or action by the taxpayer, but solely from market movements over which he has no control. Such losses are not connected with an income earning activity, be it investment or speculation, and cannot therefore be offset against taxable income.

Supreme Tax Court judgment IX R 20/14 of November 10, 2015 published on December 30

Keywords

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