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# Tax-Accrual Taxpayer Must Include In Gross Income In Year of Receipt Unconstitutional Advance Payments Received From Customers

that an express warranty limiting a manufacturer's liability to replacement of defective parts, and providing that such warranty is in lieu of all other warranties, express or implied, precludes recovery by a consumer or user against a manufacturer for injuries caused by a defective product. This type of warranty has been in general use by automobile dealers and manufacturers for many years.

The California doctrine imposing strict liability on dealers and manufacturers is based upon policy considerations. It is eminently logical to hold responsible for injuries caused by defective products those parties responsible for the defective products being on the market. It is only realistic to recognize that manufacturers and dealers are in the best position to distribute the cost of injuries caused by defective products. The recent West Virginia decisions, apparently based upon privity of contract, limit a customer's or a user's recovery for injuries caused by defective products to the terms of the express warranty.

However, *William* and *Payne* were decided prior to adoption of the Uniform Commercial Code, and no cases have been decided in this area since its enactment. The West Virginia Supreme Court of Appeals indicated in *Williams,* its most recent decision concerning automobile sales contract disclaimers, that the Code brings with it policy implications extending beyond its express provisions. Perhaps adoption of the Uniform Commercial Code has opened the door to modification of West Virginia's rather harsh position in the area of product liability law.

## Tax — Accrual Taxpayer Must Include In Gross Income In Year of Receipt Unconditional Advance Payments Received From Customers

Taxpayer was a corporate manufacturer of advertising signs. Many of its customers, needing a continuous supply, made a practice of estimating their requirements and placing blanket orders covering periods of one to three years. Taxpayer commenced manufacture when the blanket order was received but did not complete a sign until later shipping instructions were received. Some customers, on their own initiative, elected to pay for all or part of these blanket orders prior to delivery. These funds were commingled with taxpayer's other receipts without restriction as to use or disposition. Taxpayer was on an accrual method of accounting. On the federal

income tax returns for the years 1960 to 1962, taxpayer deferred inclusion of advance payments in sales income until the year in which each sign was delivered. The Commissioner determined that these amounts should have been included in the taxpayer's income in the year received and accordingly assessed deficiencies. The Tax Court upheld this view and taxpayer petitioned for review. *Held,* affirmed. Unconditional advance payments which a corporate taxpayer received from its customers for merchandise on order prior to delivery were includible in its gross income in the year of receipt rather than the year of merchandise delivery, even though the taxpayer was on an accrual method of accounting. *Hagen Advertising Displays, Inc. v. Commissioner,* 407 F. 2d 1105 (6th Cir. 1969).

The court further said, in relation to the amount of such advance payments which should be reported, that inclusion of the entire amount without allowance for the related cost of goods would be taxation of return of capital. However, it was to be presumed that the taxpayer sold the merchandise for more than cost of manufacture, in absence of a contention to the contrary, and that some portion of the advances would thus constitute gross income in the year of receipt. Since the taxpayer had made no attempt to estimate the cost of goods for which advances were received, it must bear the burden of the consequences of its failure to report the proper amount.

The court gave weight to the Congressional repeal of § 452 of the Internal Revenue Code of 1954, which gave taxpayers, with respect to both goods and services, an election to defer.

This decision places the sale of goods in the same position as the sale of services which, by a line of decisions, have not been permitted to be deferred (except for prepaid subscriptions). *See, e.g., Schlude v. Commissioner,* 372 U.S. 128 (1963).