

08-0588
SALES TAX
TAX YEARS: 2004, 2005, 2006
SIGNED: 09-30-2011
COMMISSIONERS: R. JOHNSON, M. JOHNSON, M. CRAGUN
EXCUSED: D. DIXON

BEFORE THE UTAH STATE TAX COMMISSION

PETITIONER, Petitioner, v. TAXPAYER SERVICES DIVISION OF THE UTAH STATE TAX COMMISSION, Respondent.	INITIAL HEARING ORDER Appeal No. 08-0588 Account No. ##### Tax Type: Sales Tax Tax Period: 11/4/04-01/31/06 Judge: Phan
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Presiding:
Jane Phan, Administrative Judge

Appearances:
For Petitioner: PETITIONER REP. 1, Sales/Use Tax Compliance, PETITIONER
 PETITIONER REP. 2, Tax Director, PETITIONER
 PETITIONER REP. 3, PETITIONER

For Respondent: RESPONDENT REP. 1, Assistant Attorney General
 RESPONDENT REP. 2, Deputy Director, Taxpayer Services Division

STATEMENT OF THE CASE

This matter came before the Commission for an Initial Hearing in accordance with Utah Code §59-1-502.5, on June 20, 2011. Petitioner (the “Taxpayer”) had filed this action to appeal a decision issued by Respondent (the “Division”) to deny the issuance of a refund to the Taxpayer. The refund claim had been for the period from November 1, 2004 through October 31, 2006. The issue before the Commission in this appeal is whether the Taxpayer was entitled to a sales tax refund pursuant to the bad debt provisions in effect during the audit period pursuant to Utah Code §59-12-107. The Taxpayer had submitted a post hearing brief in this matter on July 20, 2011 and the Division on August 3, 2011.

APPLICABLE LAW

The applicable statutory provisions were amended effective July 1, 2004 prior to the audit period and

are set out at Utah Code §59-12-107(8) (2003). The law was recodified effective July 1, 2005, to Utah Code §59-12-107(9) (2004) but the provisions appear to be substantially the same. Utah Code §59-12-107(8) states as follows:

- (a) For purposes of this Subsection (8):
 - (i) Except as provided in Subsection (8)(a)(ii), “bad debt” is as defined in Section 166, Internal Revenue Code.

* * * *

- (b) A seller may deduct bad debt from the total amount from which a tax under this chapter is calculated on a return.
- (c) A seller may file a refund claim with the commission if: (i) the amount of bad debt for the time period described in Subsection (8)(e) exceeds the amount of the seller’s sales that are subject to a tax under this chapter for that same time period; and (ii) as provided in Section 59-12-110.
- (d) A bad debt deduction under this section may not include interest.
- (e) A bad debt may be deducted under this Subsection (8) on a return for the time period during which the bad debt: (i) is written off as uncollectible in the seller’s books and records; and (ii) would be eligible for a bad debt deduction: (A) for federal income tax purposes; and (b) if the seller were required to file a federal income tax return.

* * * *

Two different Administrative Rules were in effect during the audit period. For the portion of the period prior to July 1, 2005, Utah Administrative Rule R865-19S-20 (2004) provided in pertinent part:

C. Justified adjustments may be made and credit allowed for cash discounts, returned goods, bad debts, and repossessions that result from sales upon which the tax has been reported and paid in full by retailers to the Tax Commission.

* * * *

4. Sales tax credits for bad debts are allowable only on accounts determined to be worthless and actually charged off for income tax purposes. Recoveries made on bad debts and repossessions for which credit has been claimed must be reported and the tax paid.

* * * *

Effective July 1, 2005, Utah Admin. Rule R865-19S-20 (2005) was amended in pertinent part to the following:

* * * *

C. Adjustments may be made and credit allowed for cash discounts, returned goods, and bad debts that result from sales upon which the tax has been reported and paid in full by a seller to the Tax Commission.

* * * *

Utah Code Ann. §59-1-1417 provides, “[i]n a proceeding before the commission, the burden

of proof is on the petitioner...”

DISCUSSION

During the audit period, PETITIONER had contracted with BANK to provide private label credit cards to PETITIONER customers. When a customer made a purchase at PETITIONER using the credit card, PETITIONER would be immediately reimbursed by BANK for the amount of the charge, which included both the purchase price and the sales tax. PETITIONER then filed sales tax returns claiming the amount of sales tax received on these and its other transactions and remitting the tax to the Utah State Tax Commission.

If a customer did not pay off their credit card debt to BANK, it was BANK that bore the loss. On accounts where BANK wrote off the account based on federal bad debt provisions, BANK took bad debt deductions on its federal income tax returns.

Although PETITIONER had been fully reimbursed for the sales tax at the time of the purchase transaction and did not have to bear the loss on the unpaid accounts. PETITIONER filed its claim seeking a refund of taxes it had remitted to the State Tax Commission on the tax amounts that BANK wrote off under the bad debt provisions. As of the hearing, PETITIONER had not provided the supporting documentation to prove that the amounts it was claiming for the refund tied into the bad debt. They asked for a ruling first on whether they would be entitled a refund and, if it was determined in their favor, they indicated they would produce the documentation. The Division noted that if it was determined a refund would be issued, it would need to review the books and records and the Taxpayer’s calculation as to the amount.

At the hearing the Taxpayer had originally argued that it did suffer some loss from the bad debt in a non-direct way, because it was included in a formula used to determine fees between the Taxpayer and BANK. However, the existence of this arrangement was never established at the hearing and the Taxpayer did not address this claim in its post hearing brief.

The Taxpayer argued that the Division’s interpretation of the provisions was inequitable because it would allow refunds to the retailer in situations where the retailer issued the credit directly and then the retailer had written it off under the bad debt provisions, but for retailers like the Taxpayer who contracted with a third party bank for the credit, there would be no refund on the bad debt.

The Taxpayer argues that this is a contradiction to legislative intent. In its post hearing brief the Taxpayer points to *Allisen v American Legion Post No. 134*, 763 P.2d 806, 809 (Utah 1988) that the Commission needs to look at the plain meaning of the language for legislative intent.¹ The Taxpayer argues

¹ The Taxpayer also cites to *Wasatch County Bd. Of Equalization v. State Tax Comm’n*, 944 P.2d 370,374, (Utah

that from its plain reading of the statute, the sales tax bad debt statute had two purposes. In its Brief the Taxpayer states, “One is to reduce the inequity of enforcing tax payments for a retailer that has been unable to collect the full purchase price from the buyer. The second is to reduce the burdens on those who provide credit in the retail market in order to stimulate economic activity.”² However, the plain reading of the revised statutory provisions directly refute the Taxpayer’s stated second purposes, because the Legislature specifically limits the credit to situations where the “seller” writes the debt off as uncollectable, not third party lenders. See Utah Code 59-12-107(8)(e).

The Taxpayer also argues that the Legislature amended Utah Code Sec. 59-12-107 effective July 1, 2004, to conform to the Streamlined Sales and Use Tax Agreement. It was the Taxpayer’s assertion that as part of that agreement “member states indicated they would continue to administer the bad debt provisions in the same manner in which a state had done so prior to the adoption to the Streamlined Sales Tax statutory provisions.”³ The Taxpayer goes on to assert that prior to the agreement, the Commission had allowed retailers to claim a deduction for bad debt even when the accounts were written off for income tax purposes by a lender. The Taxpayer asserted that one Tax Commission employee advised an unnamed tax department representative to claim a sales tax bad debt refund for the period of October 1, 2000 through June 30, 2003. It was the Taxpayer’s contention that the Tax Commission had issued refunds based on facts similar to those in this matter, although no specific retailer name was provided.

The Division refuted the Taxpayer’s contention that the Tax Commission position prior to the statutory revision was to allow the refund where the bad debt was actually written off by the lender and not the retailer. The Division also noted the allegation that refunds were issued were not supported by enough information and further that the action of an individual employee cannot override a decision of the Tax Commission. The Tax Commission had heard an appeal and issued a decision that was contrary to the Taxpayer’s allegations. The Division noted that the prior law had provided that a “credit is allowed for prepaid taxes and for taxes paid on a portion of an account determined to be worthless and actually charged off for income tax purposes. . .” (Utah

1997) in which that Court stated “our practice is to construe taxation statutes liberally in favor of the taxpayer, leaving it to the legislature to clarify an intent to be more restrictive if such intent exists.” The Commission should note that this is an established principle of statutory construction for “taxation statutes.” However, the issue at hand involves a deduction or credit and is not a taxation statute. See *Parson Asphalt Products, Inc. v. Utah State Tax Comm’n*, 617 P.2d 397, (Utah 1980) in which the Court stated, “even though taxing statutes should generally be construed favorably to the taxpayer and strictly against the taxing authority, the reverse is true of exemptions. Statutes which provide for exemptions should be strictly construed, and one who so claims has the burden of showing his entitlement to the exemption. Notwithstanding the foregoing, there is also to be considered the over-arching principle, applicable to all statutes, that they should be construed and applied in accordance with the intent of the Legislature and the purpose sought to be accomplished (Citations Omitted).” See also *SF Phosphates Limited Company v Auditing Division, Utah State Tax Comm’n*, 972 P.2d 384 (Utah 1998) and *MacFarlane et al. v. Utah State Tax Comm’n*, 134 P.3d 1116 (Utah 2006) (Involving a tax credit).

² PETITIONER Post-Hearing Brief, pg. 5.

³ PETITIONER Post-Hearing Brief, pg. 6.

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Code Sec. 59-12-107(7)(2003). The Division pointed out that the Tax Commission had considered the prior law and a fact situation very similar to the facts in this matter and found that no refund should be issued. The case is Findings of Fact, Conclusion of Law and Final Decision, Appeal No. 04-0919, issued by the Tax Commission on November 13, 2006. At issue in Appeal No. 04-0919 was a refund request by a retailer that had contracted with a third party bank to issue a private label credit card to its customers. As in this case the retailer in Appeal No. 04-0919 was paid by the bank for each transaction, including the cost of the goods and the sales tax. The retailer claimed the sales tax on its returns and remitted it to the Tax Commission. Credit card accounts unpaid were written off by the bank under the federal bad debt provisions. Like in this case the retailer did not bare the loss. After reviewing the facts in that case and statutory provisions, which were those in effect from 2000 to July 1, 2004, the Commission denied the refund to the retailer.

The facts in the subject appeal are very similar to those set out in Appeal No. 04-0919. However, the applicable law has been revised⁴ and further strengthens the position that the Taxpayer is not entitled to a refund in this matter. The revised provision specifically clarifies that the refund is limited to situations where the debt is “written off as uncollectible in the seller’s books and records . . .” in addition to being eligible for a bad debt deduction for federal income tax purposes. Utah Code 59-12-107(8)(e)(2003).

Reviewing the plain language of the statutory provisions, the Taxpayer does not qualify because it is the lender and not the seller that was able to write the bad debt off as uncollectable. There is no basis to issue the refund to the Taxpayer and this appeal should be denied.

Jane Phan
Administrative Law Judge

DECISION AND ORDER

Based on the foregoing, the Tax Commission denies the Taxpayer’s appeal in this matter. It is so ordered.

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall be mailed to the address listed below and must include the Petitioner's name, address, and appeal number:

Utah State Tax Commission
Appeals Division
210 North 1950 West

⁴ The Division stated in its brief that the law was revised part way through the audit period, effective July 1, 2005. However, the revision appears to have been made previously, as of July 1, 2004. Therefore, the entire period at issue in this matter is governed by the revised provisions.

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Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this _____ day of _____, 2011.

R. Bruce Johnson
Commission Chair

Marc B. Johnson
Commissioner

D'Arcy Dixon Pignanelli
Commissioner

Michael J. Cragun
Commissioner