

**BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO**

In the Matter of the Protest of	)	
	)	DOCKET NO. 25445
[Redacted],	)	
	)	
Petitioner.	)	DECISION
_____	)	

On August 30, 2012, the staff of the Sales, Use, and Miscellaneous Tax Audit Bureau (Bureau) of the Idaho State Tax Commission (Commission) issued a Notice of Refund Determination Denial (Notice) to [Redacted] (taxpayer) denying a refund of sales tax for the period January 1, 2005, through December 31, 2007, in the total amount of \$84,330.

On October 30, 2012, the taxpayer filed a timely appeal and petition for redetermination of the Notice. At the taxpayer's request, the Commission held a telephonic hearing with the taxpayer on April 10, 2013. The Commission is fully advised of the contents of the audit file, as well as information obtained at the hearing and thereafter. For the reasons that follow, the Commission upholds the audit findings denying the refund in full.

Background

This case concerns a sales tax bad debt refund claim denial. The taxpayer, [Redacted], is a bank that contracted with a large retailer to offer that retailer's customers unsecured credit. Unsecured credit means that the financial institution does not hold a security interest in the goods bought. It will seek payment from customers under the terms of a contract, but will not repossess goods in the event of default.

As customers make periodic payments to satisfy their debt, often in combination with acquiring additional debt through subsequent purchases, the amounts paid to the bank are, for the purpose of later calculating a sales tax bad debt refund, to be allocated between principle and

interest, thus satisfying a portion of the sales tax that was financed along with the purchase prices.

When a payment is allocated, a percentage of the sales tax remitted to the state is considered satisfied, and the outstanding diminished principal contains the remainder. As time progresses and payments are made, additional sales tax is considered to have been satisfied, culminating at 100 percent when the principal balance reaches zero. Should the consumer default, however, the remaining sales tax as represented in the unpaid principal is available as a refund (commonly referred to as a “sales tax bad debt refund”), within the confines of the statute of limitations for refunds.

The Commission’s refund auditors who examine sales tax bad debt refund claims require that the taxpayer provide a complete accounting of each customer’s sales transactions and how partial payments up to the time of default and write-off were applied for the purpose of determining a refund amount. For sales tax refund request purposes, partial payments are applied to the sales transaction amount and the agreed-upon interest that the customer is subject to at the time of sale. That is, each payment must be allocated between; the earliest, in-statute existing, and outstanding debt that was subject to tax; and the accrued, contracted interest up to the point when the payment was received.

The auditor repeatedly asked for substantive information which was not forthcoming. In response to the hearing rights letter, the taxpayer provided additional information which the auditor found to be a repeat of the previously provided information.

### Relevant Tax Code

In Idaho, the sale, purchase, and use of tangible personal property is subject to tax unless an exemption applies (Idaho Code § 63-3612). Retailers must collect the tax from their customers and the tax must be computed on the sales price at the time of the sale for all credit, installment, or similar conditional sales (Idaho Code § 63-3619).

It is accepted, for the purposes of this decision, that the retailer remitted the required tax to the state and that the taxpayer financed the sales. Further, it is undisputed that the taxpayer, while not the retailer, has a right under Idaho's law to seek a refund of sales tax in the event any customer defaults on a contract to pay fully for the purchase(s) over time (Idaho Code § 63-3613(d)).

The following administrative rule refers to the rights [Redacted] in seeking a refund and describes calculating a refund of sales tax for worthless accounts. It is excerpted in pertinent part:

02.c. A written claim for the refund may also be filed with the State Tax Commission within three (3) years from the time the tax was paid to the State Tax Commission. The State Tax Commission will review all such refund claims. See Rule 117 of these rules, Refund Claims...

05. Amount of Credit Allowed. The amount of credit that can be claimed is the amount of sales tax that is uncollectible. If both nontaxable and taxable items are financed, credit may be taken only for that portion of the bad debt which represents unpaid sales tax.....

07. To Claim Credit for a Bad Debt. Credit for bad debts for sales tax purposes may be claimed by the retailer that made the original sale and paid the sales tax to the state. Financial institutions or other third parties who are the assignees of the retailer may claim a bad debt for sales tax on property for which they provided financing, if the amount financed includes the sales tax remitted on the sale of the property. The person claiming the credit must be the person who ultimately bears the loss if the purchaser of the property defaults on the obligation to repay (IDAPA 35.01.02.063.)

### Summary of Taxpayer's Protest Letter

The taxpayer states that it has provided sufficient information to substantiate its claim. It also states that the Commission's requirements are both unduly burdensome and not supported by either statute or rule. The Commission is asking for payment histories going back beyond the three-year period while asserting that transactions beyond three years are out-of-statute for a refund.

At the hearing, the taxpayer stated that it applied customer payments by following [Redacted] and laws for the state in which it is incorporated. It suggests that such application should be sufficient for Idaho's purposes.

### Analysis

The Commission agrees that the auditor received information that was incomplete, as it did not contain sufficient detail of customers' accounts. Rather, the data consisted of three pertinent columns, the first showing a sale transaction amount; the second showing a "remaining amount" defined as the difference between the sale transaction amount and an applied amount; and, the third showing an applied amount, defined as the amount of bad debt for the transaction.

The taxpayer's data is inadequate to determine what approach it took in applying payments. Experience suggests that a number of factors can be in play. First, the taxpayer may be asking for a refund of sales tax on defaulted amounts that contain sales charges that were never subject to Idaho sales tax, either by transaction type, or by sale location. The auditor has data pointing to non-taxable credit purchases from his review of what was provided in this case.

Secondly, the taxpayer may be asking for a refund for debt due to transactions that are beyond the three year statute of limitations (Idaho Code § 63-3626). This, too, was an issue in the current case. Finally, the taxpayer could be asking for a refund based on a partial payment

application method that favors its own interests in maximizing recovery by inadvertently, but impermissibly, applying payments to late fees and punitive interest charges.

Without a detailed and dated record of each customer's purchases, added charges, and full payment history beginning prior to the refund period, there is no way to judge the veracity of the taxpayer's claim that it applied payments properly for the purpose of receiving a refund.

The Commission does not quarrel with the taxpayer's method of internal accounting for debt in the general sense, but sees no need to be bound by federal or state lending laws that have no bearing on Idaho sales tax transactions. The taxpayer has failed to cite any federal law that requires this state to abide by such an accounting.

It may be that the taxpayer's data is not conducive to an audit for bad debt refunds. However, the Bureau gave the taxpayer the option to provide sufficient raw data from which it would make a determination.

The taxpayer countered the Bureau's objections, stating that by the time late fees and punitive interest charges are added to delinquent customers' accounts, there are no offsetting customer payments that could have been impermissibly applied. While the Commission has no direct evidence to refute this claim, it must nevertheless hold the taxpayer to the evidentiary standard it routinely applies to similarly situated taxpayers. The Commission owes a duty to the state to judge the accuracy of sales tax liabilities and refund claims and, by statute, employs auditors to do so (Idaho Code § 63-3624). There is no prohibition in any tax statute that prevents the Commission from establishing audit guidelines that examine any aspect of a taxpayer's accounting records and seek reasonably available records. The Commission's stewardship of state funds encourages the rigorous yet fair standards outlined in this decision.

The Commission holds open the possibility that there may have been misunderstandings between the taxpayer and the auditor with respect to what was requested or guidelines to be followed. None of these misunderstandings, however, can give rise to invalidating the Bureau's request for data sufficient to make a reasonable estimate of the refund amount due to the taxpayer.

The taxpayer did not provide evidence adequate to establish that the Notice is incorrect. As a result, the Commission will uphold the Notice. A determination of the State Tax Commission is presumed to be correct (Albertson's, Inc. v. State, Dept. of Revenue, 106 Idaho 810, 814, 683 P.2d 846, 850 1984) and the burden is on the taxpayer to show that it is erroneous (Parsons v. Idaho State Tax Commission, 110 Idaho 572, 574-575 n.2 Ct. App. 1986.)

THEREFORE, the Notice dated August 30, 2012, is hereby APPROVED, in accordance with the provisions of this decision, and is AFFIRMED and MADE FINAL.

An explanation of the taxpayer's right to appeal this decision is enclosed.

DATED this \_\_\_\_\_ day of \_\_\_\_\_ 2013.

IDAHO STATE TAX COMMISSION

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COMMISSIONER

### **CERTIFICATE OF SERVICE**

I hereby certify that on this \_\_\_\_\_ day of \_\_\_\_\_ 2013, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to:

[Redacted]

Receipt No.

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