OKLAHOMA TAX COMMISSION

TAX POLICY DIVISION

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COPY

January 24, 2011

RE: LR-11-095 (Sales Tax Inquiry)

Dear

This is in response to your request on behalf of regarding the sales tax treatment of bad debts in Oklahoma under the scenarios set forth below.

Scenario 1: A 60 month Fair Market Value lease (non-cancellable / irrevocable) contract where the sales tax had been remitted to the OK Tax Commission based on each monthly lease charge. The lessee has defaulted on the lease contract prior to the end of term of the contract, leaving a deficiency balance $55,000, which is charged off to bad debt in accordance with generally accepted accounting principles. Would the subsequent receipt of $20,000 as a final judgment from litigation or the subsequent receipt of $10,000 from a third party guarantor be taxable for sales tax?

Response:

In accordance with OAC 710:65-11-2(a) a vendor may take a deduction for bad debts on the sales tax return for the period during which the bad debt is written off as uncollectible in the vendor's books and records and is eligible to be deducted for Federal Income Tax purposes, if the vendor kept accounts on a cash basis, or could be eligible to be claimed if the vendor kept accounts on an accrual basis. See also 68 O.S. § 1366. However subsequent recoveries of bad debts that have been taken as a deduction on a vendor's sales tax return are to be reported for sales tax purposes in the month of the recovery. OAC 710:65-11-2(f). For purposes of reporting a payment received on a previously claimed bad debt, any payments made on a debt or account are applied first proportionally to the taxable price of the property or service and the sales tax thereon, and secondly to interest, service charges, and any other charges. OAC 710:65-11-2(i).

In Scenario 1, if a credit was taken on sales tax return for the sales tax portion of the bad debt then the subsequent receipt of $20,000 from litigation and the $10,000 from a third party guarantor should be reported on the vendor's sales tax return in the month of recovery.

2. Scenario 2: A 60 month financing agreement (non-cancellable / irrevocable) where title is passed to the lessee at the beginning of the contract and the sales tax was remitted to the OK Tax Commission at the contract commencement date (up-front) based on the purchase price of the tangible personal property which was financed. The customer has defaulted on the contract prior to the end of the term of the contract, resulting in the equipment being sold to an unrelated third party (applicable sales tax was charged), leaving a net deficiency balance of $25,000 which is charged off to bad debt in accordance with generally accepted accounting principles. No refund request or credit has been taken for the uncollected portion of the up-front sales tax that was financed into the contract. Would the subsequent receipt of $8,000 as a final judgment from litigation or the subsequent receipt of $2,000 from a third party guarantor be taxable for sales tax?

Response:

In Scenario 2, because has not received a refund or credit for the uncollected sales tax neither the subsequent receipt of the $8,000 final judgment nor the $2,000 from a third party guarantor would be subject to sales tax.

This response applies only to the circumstances discussed in your written request of August 04, 2011. Pursuant to Oklahoma Administrative 710:1-3-73(e), this Letter Ruling may be generally relied upon only by the entity to whom it is issued, assuming that all pertinent facts have been accurately and completely stated, and there has been no change in applicable law.

Sincerely,

OKLAHOMA TAX COMMISSION

Marc Morrison

Marc Morrison
Tax Policy Analyst