

## TO BE RESCINDED

5703-9-44 **Bad debts.**

(A) In reporting gross sales and net taxable sales a vendor may exclude an amount equal to the sum of the vendor's bad debts arising from sales occurring on or after July 1, 1980 and charged off as uncollectible on the vendor's books during the sales tax reporting period. The tax collected for the current period may be adjusted by deducting therefrom the amount of tax previously reported and paid as tax collected on the sale giving rise to the bad debt.

"Bad debt" means any debt or account receivable arising from the sale of tangible personal property or a taxable service by the vendor upon which sales or use tax has been reported and paid in a prior reporting period which has become worthless or uncollectible during the period between the vendor's preceding tax return and the present return and which has been uncollected for at least six months. The bad debt must be of a type that is properly deductible pursuant to the "Internal Revenue Code of 1954" 68a Stat. 50, 26 U.S.C. 166, as amended, and the regulations adopted pursuant thereto, or would be so deductible if the vendor kept his accounts on an accrual basis.

The amount of the bad debt is equal to the price, or portion thereof, of the tangible personal property that is uncollectible. No amount can be excluded as a bad debt that represents:

- (1) Interest or finance charges on the debt or account;
  - (2) Sales tax charged on the purchase price;
  - (3) Uncollectible amounts on property that remains in the possession of the vendor until the full purchase price is paid;
  - (4) Expenses incurred in attempting to collect the debt or account;
  - (5) Any portion of the debt or account that is, in fact, collected; or
  - (6) Any debt or account that is sold to a third party for collection; or
  - (7) Any uncollectible amount on property repossessed by or on behalf of the vendor.
- (B) The burden of establishing the right to, and the validity of, a bad debt deduction is on the vendor claiming such deduction. For each bad debt excluded from gross sales, the vendor must maintain a record of:
- (1) The name of the purchaser/debtor;

- (2) The date of the sale or sales giving rise to the bad debt;
- (3) The price of the property and the amount of sales tax charged thereon;
- (4) The amount of interest, finance and service charges charged to the debt or account;
- (5) Whether or not the property was retained by the vendor or repossessed;
- (6) Any amounts charged to the debt or account representing costs of collection;
- (7) The dates and amounts of any payments made on the debt or account; and
- (8) Any portion of the debt or account which represents a charge that was not subjected to tax in the original transaction.

All records must be preserved for four years after the filing of the return upon which the bad debt deduction is taken, unless the commissioner consents in writing to a shorter period or requires by order a longer period.

- (C) In the event that the commissioner determines that a vendor has not maintained adequate records, the commissioner may test check the vendor's business in order to verify the amounts deducted as bad debts.

In the absence of adequate records showing the contrary, it is presumed that any payments made on a debt or account are applied first to the price of the property and sales tax thereon and secondly to interest, service charges and any other charges. The amount of interest charged to the account is presumed to be computed at the maximum rate of interest charged by the vendor on that type of account that gives rise to the bad debt.

If the vendor maintains a reserve for bad debts, only actual charges against the reserve representing uncollectible debts or accounts may be deducted for sales tax bad debt purposes. Contributions to the reserve are not deductible as a sales tax bad debt.

- (D) The tax due on any bad debt found to have been improperly or illegally deducted may be recovered by assessment in the manner provided in section 5739.13 of the Revised Code.
- (E) A bad debt may only be deducted on the return for the sales tax reporting period during which the uncollectible debt was written off on the books of the vendor. In the event that the bad debt deduction exceeds the net taxable sales of the vendor for that period, the tax attributable to the excess amount can only be recovered by refund claim pursuant to sections 5739.07 and 5741.10 of the Revised Code. If all or a portion of a bad debt is subsequently paid by the consumer or any other person, the vendor

must include the amount paid in gross sales and net taxable sales on the return for the period during which the payment was made and he must remit the tax thereon.

- (F) If the vendor's business consists of taxable and nontaxable sales of tangible personal property, and if the vendor is unable to document whether the sale of the property that gives rise to the bad debt was a taxable or nontaxable sale, the amount of the bad debt deduction shall not exceed the amount of the bad debt multiplied by the quotient obtained by dividing the vendor's taxable sales for the preceding calendar year by his gross sales for the preceding calendar year. In the event that the vendor was not engaged in business during at least six months of the preceding calendar year, the amounts of his taxable sales and gross sales for the preceding twelve months, or the amounts for each of the months that he has been engaged in business, whichever period is shorter, shall be the amounts used in computing the bad debt deduction pursuant to this paragraph.

In order to ensure that a bad debt deduction accurately reflects the tax imposed on the sale which gave rise to the bad debt, whenever the sales tax rate applicable to the vendor's place of business changes, such as by statutory change or the enactment of county or transit authority sales and use tax, the amount of the bad debt deduction must be adjusted before it is excluded from gross sales and net taxable sales. The amount to be excluded shall be the amount of the bad debt multiplied by the quotient obtained by dividing the tax rate applicable at the time of the sale by the tax rate applicable at the time of the deduction.

In case the vendor receives payment after the bad debt deduction has been excluded, the amount that must be included in gross sales and net taxable sales is the amount of the payment multiplied by the quotient of the tax rate applicable at the time of sale divided by the tax rate applicable at the time of the payment. This will assure that the vendor only remits the amount of tax that he previously recovered by excluding the bad debt.

In addition to all other records required to be kept by this rule, the vendor must maintain a record of any computation and adjustments made pursuant to this paragraph.

- (G) The provisions of this rule also apply to sellers registered with the tax commissioner pursuant to section 5741.17 of the Revised Code.
- (H) In situations where the books and records of the vendor or seller claiming the bad debt allowance support an allocation of the bad debt allowance among multiple states, the vendor or seller may make the allocation and claim the appropriate share of the bad debt with this state.

- (I) In situations where the vendor has assigned the account receivables to a third party or where the vendor uses a third party to facilitate the financing of the taxable sale, to qualify for the bad debt deduction, the claimant must be the vendor and the bad debt deduction must appear on the books and records of the vendor.

Effective:

Five Year Review (FYR) Dates: 1/30/2024

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Certification

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Date

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Statutory Authority: 5703.05  
Rule Amplifies: 5739.01(I), 5739.121, 5741.17  
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