Procedures for Retailers Claiming Credit for Sales Tax Previously Paid On Worthless Accounts Receivable

Purpose: The purpose of this supplement to **PS 2001(1)** is to provide an update as to the method and manner in which payments made by a purchaser are to be applied by the retailer for purposes of determining a credit under Conn. Gen. Stat. § 12-408(2). As explained more fully herein, any payments made by a purchaser are to be first applied by a retailer to the sales tax.

Supplemental Guidance: PS 2001(1) was originally issued by the Department of Revenue Services ("Department") on or about February 22, 2002. The purpose of **PS 2001(1)** was to provide retailers with guidance as to the scope and application of Conn. Gen. Stat. § 12-408(2), which is commonly referred to as the "Bad Debt" provision. More specifically, through **PS 2001(1)**, the Department set forth the procedure for retailers to claim a credit for sales tax paid on worthless accounts receivable. Since its issuance, the General Assembly amended Conn. Gen. Stat. § 12-408(2). As the legislative amendments directly impact how retailers are to calculate a credit under Conn. Gen. Stat. § 12-408(2), the Department is updating **PS 2001(1)** to reflect these changes. To that end, and as explained below, the General Assembly clarified the method and manner in which payments made by a purchaser are to be applied by the retailer for purposes of determining a credit under Conn. Gen. Stat. § 12-408(2).

It has long been a question as to how retailers are to apply payments that they receive from a purchaser in connection with a worthless accounts receivable. Based on the Department's experience, this is typically an issue in circumstances where a retailer extends credit to the purchaser. Under the law, although the purchaser generally makes no payment at the time of purchase of a taxable item or service, the retailer is nonetheless required to remit the sales tax due and owing on said items on the return covering the period in which the transaction occurred. In such circumstances, the retailer often remits the sales tax before receiving any payment from the purchaser. The provisions of Conn. Gen. Stat. § 12-408(2) are implicated when the purchaser fails to pay the retailer and the retailer determines that that liability owed to it by a purchaser is worthless and writes said account off for federal tax purposes. In such circumstances, when a purchaser made a payment or payments toward said liability to the retailer prior to such a determination, the Department had long been of the position that said payments are to be applied toward the amount of the sales tax the retailer remitted at the time of the transaction and for which it is seeking credit under Conn. Gen. Stat. § 12-408(2) and not to charges the retailer may impose on the purchaser, like penalty, interest, or other fees connected to the purchaser's failure to pay its liability to the retailer. Although the Department had consistently taken that position with retailers, the General Assembly clarified this issue through an amendment to Conn. Gen. Stat. § 12-408(2).

To that end, the General Assembly added the following language to Conn. Gen. Stat. § 12-408(2):

If any payment is made by a consumer with respect to an account, such payment shall be applied first toward the sales tax, and if any account with respect to which such credit is allowed is thereafter collected by the retailer in whole or in part, the amount so collected, up to the amount of the sales tax for which the credit was claimed, shall be included in the sales tax return covering the period in which such collection occurs.

Based on the above, the General Assembly has made it clear that any payments a retailer receives must be applied toward the sales tax. In other words, and stated simply, any payments a retailer receives must be applied toward the amount of the sales tax the retailer remitted at the time of the transaction. In many cases, retailers have been applying such payments first to their own charges like penalty, interest, or other fees and not the sales tax. Given the clear language the General Assembly added to Conn. Gen. Stat. § 12-408(2), retailers are now precluded from first applying payments to such charges. Accordingly, through this supplemental guidance, the Department is hereby updating the procedure set forth in **PS 2001(1)** so as to reflect the amendment to Conn. Gen. Stat. § 12-408(2) described herein.

Consistent with the above, and starting with any claims for "Bad Debt" that are submitted on and after July 8, 2019, such claims must be calculated in such a manner that all payments received by a retailer are

first applied towards the sales tax. Any claims that do not conform with the provisions of Conn. Gen. Stat. § 12-408(2) will be adjusted and potentially denied by the Department.

Effective Date: Effective for transactions occurring on and after July 8, 2019.

Statutory Authority: Conn. Gen. Stat. § 12-408(2).

Effect on Other Documents: Policy Statement 2001(1), *Procedure for Retailers Claiming Credit for Sales Tax Previously Paid on Worthless Accounts Receivable*, is modified and superseded in part.

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