
BAD DEBT

The *Arvada Sales and Use Tax Return* allows a retailer a deduction for Bad Debts Charge Off as well as an addition to Gross Sales for Bad Debts Collected.

Bad debts that are found to be worthless and are actually and properly charged off as bad debts for Federal income tax purposes may be deducted from gross sales (line 3D) by the retailer who collected and remitted the tax, provided those transactions were included in gross sales on the current or on a prior return and to the extent that the statute of limitations has **not expired** from when the original taxes were paid to the City of Arvada.

In establishing worthlessness, the retailer has the burden of providing adequate evidence that the usual remedies available in collecting the debt have been exhausted. Collection attempts, such as phone calls, correspondence, and pursuit via litigation, must be adequately documented in addition to documentation supporting that the sale was included on a current or previous return, and that the debt has been charged off for Federal income tax purposes. If the retailer is not required to file income tax returns then the debt is to be charged off in accordance with generally accepted accounting principles. A retailer may claim a bad debt deduction on (line 3D) provided that the sales tax was actually paid to the City. If the debt is subsequently collected, the purchase price and related tax must be reported on the next periodic City sales/use tax return (line 2).

AMOUNT SUBJECT TO DEDUCTION

TAXABLE RECEIPTS. If the amount of an account found to be worthless and charged off is comprised in part of nontaxable receipts such as tax, interest, insurance, repair, or installation labor and in part of taxable receipts upon which tax has been paid, a bad debt deduction may be claimed only with respect to the unpaid amount upon which tax has been paid. In determining that amount, all payments and credits to the account may be applied ratably against the various elements comprising the amount the purchaser contracted to pay (pro rata method), may be applied as provided in the sale.

EXPENSES OF COLLECTION. No deduction is allowable for expenses incurred by the retailer in attempting to enforce collection of any account receivable, or for that portion of a debt recovered that is retained by or paid to a third party as compensation for services rendered in collecting the account.

WORTHLESS ACCOUNT SUBSEQUENTLY COLLECTED. If any account found worthless and charged off is thereafter collected by the retailer, in whole or in part, the taxable percentage of the amount so collected shall be included in the first return filed after such collection and tax shall be paid on such amount with the return. The same percentage of the account which the retailer claimed as an allowable bad debt deduction or refund shall be used to determine the taxable percentage of the recovery.

RECORDS. In support of deductions or claims for refund for bad debts, retailers must maintain adequate and complete records showing:

- (1) Date of original sale.
- (2) Name and address of purchaser.
- (3) Amount purchaser contracted to pay.
- (4) Amount on which retailer paid tax.
- (5) The jurisdiction(s) where the taxes were allocated.

(6) All payments or other credits applied to account of purchaser.

(7) Evidence that the uncollectible portion of gross receipts on which tax was paid actually has been legally charged off as a bad debt for income tax purposes (whether or not the income tax return has yet been filed) or, if the retailer is not required to file income tax returns or charged off in accordance with generally accepted accounting principles.

(8) The taxable percentage of the amount charged off as a bad debt properly allocable to the amount on which the retailer reported and paid tax.

EXAMPLE:

Max's Sporting Goods sells uniforms to public and charitable high school sports teams. The schools provide their exemption certificated and are not charged sales tax. The sales are deducted on the return as Governmental / Charitable Sales. At the end of the year Max is to determine the bad debt amount and discovered that one of the charitable schools did not paid for an order for \$150.00 after many attempts to collect. Max will **not** be able to deduct on 3B Bad Debt the \$150.00 amount because taxes were never paid on the sales initially.

ARVADA MUNICIPAL CODE – Chapter 98 - Taxation

Sec. 98-94. Statute of limitations.

Unless the limitation period has been extended as provided in this section, the statutes of limitations for provisions contained in this chapter shall be as follows:

(1) *Refunds:*

c. Any other claim for refund shall be filed on or before three years after the date such overpayment was paid to the city.

THE ABOVE INFORMATION IS A SUMMARY IN LAYMAN'S TERMS OF THE RELEVANT ARVADA TAX LAW FOR THIS SUBJECT, INDUSTRY OR BUSINESS SEGMENT. IT IS NOT INTENDED FOR LEGAL PURPOSES TO BE SUBSTITUTED FOR THE FULL TEXT OF THE ARVADA MUNICIPAL CODE. HOWEVER, THE TAX GUIDE SHALL BE USED IN CONJUNCTION WITH THE ARVADA MUNICIPAL CODE (CHAPTER 98) IN DETERMINING TAX LIABILITY.