



STATE BOARD OF EQUALIZATION

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November 10, 1997

E. L. SORENSEN, JR.
Executive Director

Mr. R--- G. R---
Vice President & General Manager
D--- R. R--- Co.
P. O. Box XXXXXX
---, CA XXXXX

Dear Mr. R---:

This is in response to your request of October 28, 1997, made at the Culver City meeting of the State Board of Equalization, that we advise you as to how you should take a bad debt deduction for sales and use tax purposes, when you maintain your general financial records on a cash basis.

First, as you know, for sales and use tax purposes, all retailers must report sales tax liability on an accrual basis. See Sales and Use Tax Regulation 1642, "Bad Debts," paragraph (c), copy enclosed for your reference.

Second, the regulation provides that a bad debt deduction will not be disallowed retailers solely for the reason that they are on a cash reporting basis for income tax purposes. A bad debt deduction with respect to tax previously paid may be taken when all collection activities have ceased and the obligation is treated by the retailer as no longer subject to collection. Evidence of the indebtedness should be marked as "uncollectible" or "bad debt" or the records of the sale transaction should otherwise be segregated and identified for audit verification.

In the case where a receivable is sold without recourse, neither the retailer nor the assignee is entitled to a bad debt deduction where collection does occur. In the case where a receivable is sold with recourse, the retailer may take a bad debt deduction when the obligation is reassigned to the retailer and all collection activities cease.

If any accounts found worthless and charged off are thereafter in whole or in part collected by the retailer, the amount so collected must be included in the first return filed after such collection and the amount of the tax thereon paid with the return.

Sincerely,

Gary J. Jugum
Assistant Chief Counsel

GJJ:sr

cc: Ms. Jennifer Willis
Taxpayers' Rights Advocate Office