

ST 13-18
Tax Type: Sales Tax
Tax Issue: Bad Debt Write-Off

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS**

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

v.

**ABC BUSINESS, LLC/
XYZ CO., LLC,
Taxpayer**

No. XXXX
Account ID XXXX
XXXX
XXXX
XXXX
XXXX
XXXX
XXXX
BDN XXXX
XXXX

**Ted Sherrod
Administrative Law Judge**

RECOMMENDATION FOR DISPOSITION

Appearances: Special Assistant Attorney General George Foster on behalf of the Illinois Department of Revenue (“Department”); Brian R. Harris of Akerman Senterfitt on behalf on behalf of XYZ Co., LLC.

Synopsis:

This matter involves the denial of a refund claim that XYZ Co., LLC (“XYZ”) filed to claim a refund of Retailers’ Occupation Tax (“ROT”) related to bad debts acquired by XYZ from retailers that XYZ wrote off on its federal income tax returns during 2004 through 2006. Accordingly, the issue in this case is whether XYZ is entitled to a refund of tax that is equal to a portion of the ROT remitted to the Illinois Department of Revenue (“Department”) by retailers from whom certain of XYZ’s credit account customers made retail purchases of automobiles which accounts were later written off by XYZ as bad debts. An evidentiary hearing was held in

this matter on March 27, 2013 during which testimony on behalf of the taxpayer was received from Jane Doe, the taxpayer's tax consultant. James Barborka, a Department Revenue Auditor, also testified on behalf of the Department. During the hearing, the parties submitted a Stipulation of Facts and exhibits. I am including in this recommendation findings of fact and conclusions of law. I recommend the Department's refund claim denial be finalized as issued.

Findings of Fact:

1. On December 30, 2007, XYZ Company, LLC (" XYZ ") submitted a claim for refund or credit pursuant to Illinois Administrative Code section 130.1960 for the period January 1, 2004 through November 30, 2006 in the amount of \$1,049,349. Taxpayer's Exhibit ("Ex.") 1. This claim is for the portion of the balances of consumer accounts that XYZ deducted as bad debts on its federal tax returns that is attributable to the Illinois Retailers Occupation Tax. Stipulation of Facts ("Stip.") ¶ 1.
2. XYZ financed the purchase of motor vehicles from various motor vehicle retailers in Illinois. Stip. ¶ 3. XYZ , however, is not the retailer that made the installment sales that are the subject of its refund claim. *Id.* Rather, for those sales, XYZ financed both the purchase price of the automobiles and the Retailers' Occupation Tax on the sales. Stip. ¶ 5.
3. At the time of the sales, the purchasers entered into retail installment contracts with various motor vehicle retailers to purchase vehicles. Stip. ¶ 4. Pursuant to these contracts, the purchasers agreed to pay the entire amount financed over time in fixed installment of specific sums. Stip. ¶ 5. The amount financed was the total purchase price of the vehicle plus the total Retailers' Occupation Tax due on the sale minus any down payment. *Id.* If the purchaser made a down payment, it was applied pro rata

between the total purchase price and the total Retailers' Occupation Tax due on the sale.

Id.

4. At the time of the sales, the motor vehicle retailers contemporaneously assigned to XYZ all of the motor vehicle retailers' rights, titles and interest in these contracts. Stip. ¶ 6. These assignments included the right to enforce the debt and to repossess the collateral in the event of a default by the purchaser. *Id.*
5. In exchange for the assignments, XYZ paid to the motor vehicle retailers the entire amount financed under the contracts. Stip. ¶ 7. The amount financed under each of the contracts included a full amount of the Retailers Occupation Tax on the vehicle, but, if the purchaser made a down payment, then the amount of Retailers Occupation Tax that was financed was reduced by the portion of the down payment attributable to the tax. Stip. ¶¶ 5, 7. The motor vehicle retailers then reported on form ST-556 and remitted to the State of Illinois the Retailers' Occupation Tax due, which had been reimbursed to the motor vehicle retailers by XYZ. Stip. ¶ 7.
6. Some of these customers defaulted on their contracts, and it is these defaulted contracts that are the basis of XYZ's claim in this case. Stip. ¶ 8. When the purchasers defaulted on the contracts, they did not repay the full amount of the purchase price and the Retailers' Occupation Tax, and a portion of these amounts remained unpaid. *Id.*
7. In some instances, the vehicles were repossessed and sold. Stip ¶ 9. When the vehicles were repossessed and sold, XYZ applied the sale proceeds pro rata to what remained of the purchase price and Retailers' Occupation Tax. *Id.* Many times, even after the application of sale proceeds, the contracts still had unpaid balances. *Id.*

8. After reasonable attempts to collect the balances that remained on the defaulted contracts, XYZ determined that they were worthless. Stip. ¶ 10. That is, all of the surrounding circumstances indicated that the debts were uncollectible and that legal action to enforce payment would not result in the satisfaction of execution on a judgment. *Id.* XYZ claimed the remaining balances on these contracts as bad debts, pursuant to section 166 of the Internal Revenue Code, on its federal income tax returns. Stip. ¶ 9.
9. On December 30, 2007, XYZ filed a claim for a refund or credit pursuant to Illinois Administrative Code §130.1960 in the amount of \$1,049,349. Taxpayer's Ex. 1. This amount is the portion of balances that were written off as bad debts that are attributable to the Retailers' Occupation Tax. Stip. ¶ 1.
10. Over the course of the next three years, the Department audited XYZ's claim for a refund or credit. Taxpayer's Ex. 7. Because XYZ's total claim of \$1,049,349 was comprised of hundreds of discrete transactions, the Department only audited a subset of those total transactions. *Id.*
11. On October 27, 2010, the Department issued a Notice of Tentative Denial of Claim for Sales Tax. Department Ex. 1; Stip. Ex. 1.¹ This notice tentatively denied XYZ's claim. *Id.* The Department's Notice of Tentative Denial did not act upon XYZ's full claim of \$1,049,349. *Id.* Instead, the Notice of Tentative Denial of Claim only referenced 29 transactions totaling \$12,935.95. Transcript ("Tr.") pp. 15, 20, 26, 27, 45; Department Ex. 1; Stip. Ex. 1. The portion of XYZ's refund claim not covered by the Notice of

¹ The Notice of Tentative Denial of Claim for Sales Tax was issued to ABC Business, LLC. Department Ex. 1. ABC Business, LLC is XYZ's tax consultant which filed a refund claim on behalf of XYZ. Tr. pp. 11-13. The refund claim at issue pertains solely to amounts claimed by XYZ to be owed to it as a result of bad debts XYZ accrued through the financing of retail sales in Illinois. *Id.*

Tentative Denial of Claim issued totaling \$12,935.95 remains pending before Department. Taxpayer's Brief p. 5.

12. On December 27, 2010, XYZ filed a protest and request for an administrative hearing. Stip. ¶ 2.

Conclusions of Law:

Background

The issue presented in this case is whether XYZ Corp., LLC ("XYZ ") is entitled to a refund for sales taxes paid on defaulted consumer credit accounts it acquired from motor vehicle dealers with respect to motor vehicle sales made by these retailers during the 2004 through 2006. Section 6b of the Retailers' Occupation Tax Act ("ROTA"), 35 ILCS 120/6b, provides that the Department's denial of a taxpayer's refund claim constitutes *prima facie* proof that the taxpayer is not entitled to a refund. The Department's *prima facie* case is a rebuttable presumption. Copilevitz v. Department of Revenue, 41 Ill. 2d 154, 157 (1968); DuPage Liquor Store, Inc. v. McKibbin, 383 Ill. 276, 279 (1943). This presumption is overcome and the burden shifts back to the Department to prove its case, only after the taxpayer has presented documentary evidence to show that the Department's determination is not correct. A.R. Barnes & Co. v. Department of Revenue, 173 Ill. App. 3d 826, 833-34 (1st Dist. 1988).

A taxpayer cannot overcome the statutory presumption merely by denying the accuracy of the Department's assessment. *Id.* Rather, the taxpayer's burden is to present evidence that is consistent, probable and closely identified with its books and records, to show that the Department's determination is not correct. Copilevitz, *supra* at 157; A.R. Barnes & Co., *supra* at 833-34.

The Department has express authority to make, promulgate and enforce reasonable rules and regulations relating to the administration and enforcement of the ROTA. 35 ILCS 120/12. Here, XYZ relies on Retailers' Occupation Tax regulation § 130.1960(d) as the authority for its claim for refund. 86 Ill. Admin. Code § 130.1960(d) (hereinafter "ROT regulation §130.1960(d)"). The applicable regulation, cited above, provides, in pertinent part:

Section 130.1960 Finance Companies and Other Lending Agencies -- Installment Contracts -- Bad Debts ...

d) Bad Debts

1) In case a retailer repossesses any tangible personal property and subsequently resells such property to a purchaser for use or consumption, his gross receipts from such sale of the repossessed tangible personal property are subject to Retailers' Occupation Tax. He is entitled to a bad debt credit with respect to the original sale in which the default has occurred to the extent to which he has paid Retailers' Occupation Tax on a portion of the price which he does not collect, or which he is not permitted to retain because of being required to make a repayment thereof to a lending agency under a "with recourse" agreement. Retailers of tangible personal property other than motor vehicles, watercraft, trailers and aircraft that must be registered with an agency of this State may obtain this bad debt credit by taking a deduction on the returns they file with the Department for the month in which the federal income tax return or amended return on which the receivable is written off is filed, or by filing a claim for credit as provided in subsection (d)(3) of this Section. Because retailers of motor vehicles, watercraft, trailers and aircraft do not pay Retailers' Occupation Tax to the Department on retail sales of motor vehicles, watercraft, trailers, and aircraft with monthly returns, but remit the tax to the Department on a transaction by transaction basis, they are unable to take a deduction on the returns that they file with the Department, but may file a claim for credit with the Department, as provided in subsection (d)(3), on any transaction with respect to which they desire to receive the benefit of the repossession credit.

2) Retailers who incur bad debt on any tangible personal property that is not repossessed may also obtain bad debt credit as provided in subsections (d)(1) and (3).

3) In the case of tax paid on an account receivable that becomes a bad debt, the tax paid becomes a tax paid in error, for which a claim for credit may be filed in accordance with Section 6 of the Retailers' Occupation Tax Act, on the date that the Federal income tax return or amended return on which the receivable is written off is filed.

ROT regulation §130.1960(d)

Taxpayer's Contentions

XYZ argues that ROT regulation §130.1960(d) allows a claimant to claim a refund or deduction where: (1) Retailers' Occupation Tax ("ROT") was remitted on the sale and (2) the account is written off as uncollectible for federal income tax purposes. Taxpayer's Brief, p. 7. XYZ claims that it meets each requirement because it is undisputed that ROT was remitted to the State of Illinois on each of the motor vehicle sales, and it is also undisputed that XYZ wrote off the defaulted accounts as uncollectible on its federal income tax returns. *Id.* (citing Stip. ¶¶ 7, 10). XYZ also argues that it is entitled to a refund as the assignee of the rights of the retailers who made the sales. Taxpayer's Brief, p. 10. It asserts that pursuant to assignments it received from the automobile retailers whose sales it financed, it is the assignee of the rights of the retailers who made the sales to seek refunds under ROT regulation §130.1960, the regulation authorizing a refund for bad debt write-offs.

Whether Illinois Statutory Law Authorizes XYZ's Refund Claim

While the taxpayer premises its refund claim upon the Department's ROT regulation §130.1960(d), it must be noted that the Department lacks the power to create a refund by regulation that is not expressly authorized by statute. Ruby Chevrolet, Inc. v. Department of Revenue, 6 Ill. 2d 147, 151 (1955). The only ROTA statutory provision authorizing tax refunds is section 6 of the ROTA, which states, in pertinent part, as follows:

§ 6. Credit memorandum or refund. If it appears, after claim therefor filed with the Department, that an amount of tax or penalty or interest has been paid which was not due under this Act, whether as the result of a mistake of fact or an error of law, except as hereinafter provided, then the Department shall issue a credit memorandum or refund to the person who made the erroneous payment or, if that person died or became a person under legal disability, to his or her legal representative, as such. ... Claims submitted by the retailer are subject to the same restrictions and procedures provided for in this Act. ... However, as to any claim for credit or refund filed with the Department on and after each January 1 and July 1 no amount of tax or penalty or interest erroneously paid (either in total or partial liquidation of a tax or penalty or amount of interest under this Act) more than 3 years prior to such January 1 and July 1, respectively, shall be credited or

refunded, except that if both the Department and the taxpayer have agreed to an extension of time to issue a notice of tax liability as provided in Section 4 of this Act, such claim may be filed at any time prior to the expiration of the period agreed upon.

... No credit may be allowed or refund made for any amount paid by or collected from any claimant unless it appears (a) that the claimant bore the burden of such amount and has not been relieved thereof nor reimbursed therefor and has not shifted such burden directly or indirectly through inclusion of such amount in the price of the tangible personal property sold by him or her or in any manner whatsoever; and that no understanding or agreement, written or oral, exists whereby he or she or his or her legal representative may be relieved of the burden of such amount, be reimbursed therefor or may shift the burden thereof; or (b) that he or she or his or her legal representative has repaid unconditionally such amount to his or her vendee (1) who bore the burden thereof and has not shifted such burden directly or indirectly, in any manner whatsoever; (2) who, if he or she has shifted such burden, has repaid unconditionally such amount to his own vendee; and (3) who is not entitled to receive any reimbursement therefor from any other source than from his or her vendor, nor to be relieved of such burden in any manner whatsoever. No credit may be allowed or refund made for any amount paid by or collected from any claimant unless it appears that the claimant has unconditionally repaid, to the purchaser, any amount collected from the purchaser and retained by the claimant with respect to the same transaction under the Use Tax Act.

35 ILCS 120/6.

Since section 6 is the only ROTA provision that authorizes refunds, ROT regulation §130.1960 must be construed to authorize refund claims only to the extent that such a refund is permitted by section 6 of the ROTA. Ruby Chevrolet, Inc., *supra*.

Section 6 of the ROTA “is a special remedial statute[.] Its general purpose is limited to those who have paid a tax pursuant to the ROTA which, by reason of some mistake of law or fact, they should not have paid.” Peoples Store of Roseland v. McKibbin, 379 Ill. 148, 152 (1942). ROT is imposed only upon “persons engaged in the occupation of selling at retail tangible personal property ...[.]” 35 ILCS 120/2.

Rather than engaging in any occupation that is taxed by the ROTA, XYZ engaged in the occupation of financing others’ purchases and/or sales of motor vehicles at retail for use in Illinois, using the credit that XYZ agreed to extend regarding such sales. Stip. ¶¶ 3-7. The

ROTA does not impose a tax on persons engaged in that occupation. 35 **ILCS** 120/2. Since XYZ was not subject to the ROTA regarding others' sales of motor vehicles, it is not within the class of persons to whom the legislature intended to provide the special remedy authorized by ROTA § 6. 35 **ILCS** 120/6; Peoples Store of Roseland, *supra* at 152.

Further, since XYZ was not engaged in any occupation that is taxed pursuant to the ROTA, it never paid any tax that is imposed by the ROTA to the Department. Stip. ¶¶ 3-7. While XYZ was indeed the source of the money that each individual borrowed to purchase a motor vehicle, and that each individual retailer received regarding each individual sale of a motor vehicle (including the amounts required to pay the Illinois sales tax) XYZ's act of extending credit did not make XYZ subject to the ROTA imposed on motor vehicle purchases it financed. Nor does its financing activity constitute evidence that it actually paid the ROTA it stipulates the retailers reported and remitted to the Department from the proceeds received from XYZ in financing the purchased motor vehicles. Stip. ¶ 7. In short, XYZ was not a retailer, it never bore the burden of paying ROT, and it did not pay any ROT to the Department.

As the stipulations in this matter reflect, each retailer paid *its* respective and corresponding amount of ROT liability to the Department. *Id.* Since XYZ never paid any ROT to the Department, it cannot have paid any such tax in error. XYZ, therefore, is not entitled to any refund expressly authorized by ROTA § 6. 35 **ILCS** 120/6; Peoples Store of Roseland, *supra* at 152.

Moreover, even if XYZ were, itself, the retailer in the transactions for which it claims a refund, the stipulated record does not contain evidence which shows that it is entitled to a credit or refund in the amounts claimed because XYZ has wholly failed to provide the detailed information in the claim form (ST-557 Claim for Repossession of Motor Vehicles, Watercraft,

Aircraft, Trailers and Motor Homes) it submitted as required by section 6 of the ROTA to support a properly completed claim form. The claim form that XYZ filed with the Department requires the retailer preparing it to report detailed facts and information to show that a credit is due, and the amount claimed. Taxpayer's Ex. 1. The claim form is divided into four numbered parts, and each part requires the retailer to provide different information. *Id.* Part 1 asks the claimant to "Identify your business[;]" Part 2 asks the claimant to "Describe your finance contract information[;]" Part 3 asks the claimant to "Figure the amount of overpaid tax[;]" and Part 4 requires the claimant to sign the return, under the following statement: "Under the penalties of perjury, I state that I have examined this claim and, to the best of my knowledge, it is true, correct and complete." *Id.*

Part 3 of the Claim form requires the retailer to report information, described in 10 separate column headings, to identify the specific transactions, and the specific amounts of gross receipts and tax actually collected, to support the retailer's assertion that it paid a certain amount of tax in error. *Id.*

When reviewing the type of information required to be reported on the claim form, i.e. the ST-557, it helps to recall that the form is designed for use by a retailer of motor vehicles that is required to prepare and file a separate original return to report each and every retail sale of a distinct motor vehicle. 35 ILCS 120/3; 86 Ill. Admin. Code § 130.540 (Returns on a transaction by transaction basis). Thus, on the ST-557 form, each row of horizontal lines, viewed from left to right, allows the retailer to detail the required information for each specific transaction for which the retailer is seeking a refund of tax claimed to have been paid in error. Taxpayer's Ex. 1. Further, the rows of lines begin on the first page and continue onto the second page of the form. *Id.* This allows a retailer to identify, on a single return, many transactions

regarding which it asserts it paid tax in error. For ease, the form includes an additional line under the tenth column on each page, so that the preparer can enter subtotals and a “Grand total” for the refund requested regarding all of the specific transactions identified on each page. *Id.*

It is important to note that the detail asked for on the face of form ST-557 is required by the express text of ROTA § 6a. 35 **ILCS** 120/6a. That section provides, in pertinent part:

§ 6a. Claims for credit or refund shall be prepared and filed upon forms provided by the Department. Each claim shall state: (1) The name and principal business address of the claimant; (2) the period covered by the claim; (3) the total amount of credit or refund claimed, giving in detail the net amount of taxable receipts reported each month or other return period used by the claimant as the basis for filing returns in the period covered by the claim; (4) the total amount of tax paid for each return period; (5) receipts upon which tax liability is admitted for each return period; (6) the amount of receipts on which credit or refund is claimed for each return period; (7) the tax due for each return period as corrected; (8) the amount of credit or refund claimed for each return period; (9) reason or reasons why the amount, for which the claim is filed, is alleged to have been paid in error; (10) a list of the evidence (documentary or otherwise) which the claimant has available to establish his compliance with Section 6 as to bearing the burden of the tax for which he seeks credit or refund; (11) payments or parts thereof (if any) included in the claim and paid by the claimant under protest; (12) sufficient information to identify any suit which involves this Act, and to which the claimant is a party, and (13) such other information as the Department may reasonably require.

35 **ILCS** 120/6a.

The legislature’s use of the word “shall” reflects that a retailer seeking a credit for ROT claimed to have been paid in error is required to specifically identify the different amounts and items of information described in ROTA § 6a. It is not the

Department, therefore, but the legislature that has determined that the specific items of information detailed in ROTA § 6a constitute a material part of the retailer's claim for credit. The legislature has determined that the retailer's provision of this detailed information is the way the retailer identifies the particular gross receipts regarding which it claims to have paid tax in error, as well as the way for the Department to ensure that the refund claimed be no greater than the tax money the retailer actually paid in error to the Department. 35 **ILCS** 120/6a.

Completely ignoring the mandate of section 6a, on the claim form XYZ filed, XYZ failed to identify any specific transactions for which it claims it paid tax in error, let alone every transaction that, added together, would total the amount of credit or refund XYZ claimed as being due. Taxpayer's Ex. 1. All XYZ has done on this form is enter a number on the line provided for a retailer to identify the "Grand total" claimed as a credit or refund. *Id.* There are no transactions identified on pages 1 or 2 of XYZ's claim form. *Id.* As a consequence of XYZ's failure to provide complete information as required by section 6a of the ROTA, XYZ is barred from claiming a statutory right to a refund under section 6 of the ROTA in this case.²

Moreover, in this contested case, XYZ bears the burden to show, with documentary evidence closely identified with its books and records, that it was entitled to the refund being sought. PPG Industries, Inc. v. Department of Revenue, 328 Ill. App. 3d 16, 33 (1st Dist. 2002) (agreeing that a taxpayer "had the burden of overcoming [the Department's] *prima facie* case

² While XYZ has provided examples of documentation related to the motor vehicle sales it financed (at Ex. 3 through 7), I find that this limited documentation is insufficient to meet the statutory requirements of section 6a.

through documentary evidence, meaning books and records, and not mere testimony.”). That burden extends not just to the type of evidence which shows that XYZ was, in fact, a retailer that paid ROT in error to the Department, but it also extends to XYZ ’s burden to show that it is entitled to a refund in the amount claimed. A.R. Barnes & Co., *supra* at 833-34. Because XYZ never submitted the required information, or sufficient evidence from which such data might be discerned, I am left without any factual basis to conclude that XYZ ’s bad debt caused it to pay some specific amount of tax in error.

In sum, even if XYZ were a retailer subject to ROT on its business of extending credit to customers who used that credit to purchase motor vehicles from retailers in Illinois, and even if it had, in fact, paid ROT to the Department, XYZ would still not have shown, in this case, that it was entitled to the amount of refund claimed on the claim form it filed because this form does not contain the information required by section 6a of the ROTA. Moreover, the record in this case includes insufficient competent evidence from which a fact-finder might discern the information showing that XYZ ’s calculation of the refund claimed due is correct. As a consequence of XYZ ’s failure to provide the information required by section 6 of the ROTA, it has not only forfeited its right to rely on this measure as a basis for its refund claim, but has also failed to provide sufficient evidence to rebut the presumed correctness of the Department’s refund claim denial. PPG Industries, *supra*. In conclusion, for the reasons enumerated above, I find that XYZ has failed to establish that its refund claim is authorized by Illinois statutory law.

Whether XYZ ’s Claim is Authorized by 86 Ill. Admin. Code § 130.1960(d)

As previously noted, XYZ argues that ROT regulation §130.1960(d) allows a claimant to recover a refund for bad debts where: (1) ROT was remitted on the sale giving rise to a bad debt upon the purchaser’s default; and (2) the bad debt is written off as uncollectible for federal

income tax purposes. Taxpayer's Brief p. 7. Because the parties have stipulated that both of these prerequisites with respect to the bad debt write-off have been satisfied, XYZ contends that its bad debt write-off is authorized by ROT regulation §130.1960(d), which, as previously noted, provides as follows:

Section 130.1960 Finance Companies and Other Lending Agencies -- Installment Contracts -- Bad Debts ...

d) Bad Debts

1) In case a retailer repossesses any tangible personal property and subsequently resells such property to a purchaser for use or consumption, his gross receipts from such sale of the repossessed tangible personal property are subject to Retailers' Occupation Tax. He is entitled to a bad debt credit with respect to the original sale in which the default has occurred to the extent to which he has paid Retailers' Occupation Tax on a portion of the price which he does not collect, or which he is not permitted to retain because of being required to make a repayment thereof to a lending agency under a "with recourse" agreement. Retailers of tangible personal property other than motor vehicles, watercraft, trailers and aircraft that must be registered with an agency of this State may obtain this bad debt credit by taking a deduction on the returns they file with the Department for the month in which the federal income tax return or amended return on which the receivable is written off is filed, or by filing a claim for credit as provided in subsection (d)(3) of this Section. Because retailers of motor vehicles, watercraft, trailers and aircraft do not pay Retailers' Occupation Tax to the Department on retail sales of motor vehicles, watercraft, trailers, and aircraft with monthly returns, but remit the tax to the Department on a transaction by transaction basis, they are unable to take a deduction on the returns that they file with the Department, but may file a claim for credit with the Department, as provided in subsection (d)(3), on any transaction with respect to which they desire to receive the benefit of the repossession credit.

2) Retailers who incur bad debt on any tangible personal property that is not repossessed may also obtain bad debt credit as provided in subsections (d)(1) and (3).

3) In the case of tax paid on an account receivable that becomes a bad debt, the tax paid becomes a tax paid in error, for which a claim for credit may be filed in accordance with Section 6 of the Retailers' Occupation Tax Act, on the date that the Federal income tax return or amended return on which the receivable is written off is filed.

Notwithstanding XYZ's assertion that it satisfies all of the requirements of ROT regulation §130.1960(d), it is undisputed that XYZ fails to meet the first requirement of this

regulation; namely the requirement that the person claiming the credit or refund be the retailer who paid ROT regarding a sale in the first place. 35 **ILCS** 120/6; ROT regulation § 130.1960(d)(1). As the court notes in Jones v. Department of Revenue, 60 Ill. App. 3d 886 (5th Dist. 1978):

[T]he Illinois legislature has provided in the ROTA ... that the only person entitled to receive a refund or credit is the remitter of the tax. (Citation omitted) The reason for this provision was stated by the court in Snyderman v. Isaacs, as follows:

“(A) refund procedure without safeguards might result in refunds of taxes that had not actually been remitted, or in the unjust enrichment of persons who had not themselves paid the tax, but had passed its burden on to another. To protect the real taxpayer and to prevent unjust enrichment of any other party, the legislature has provided ... in the Retailers’ Occupation Tax Act that the only person entitled to receive credit is the remitter of the tax.” (Citation omitted).
Id. at 889.

XYZ contends that its status as a retailer bearing the burden of the ROT as required by the regulation arises from the fact that it: (1) reimbursed the retailers actually making sales for all sales taxes due; (2) deducted the bad debts on its federal income tax returns; and (3) owned the accounts and receivables that defaulted. Taxpayer’s Brief p. 8. XYZ bases its contention on the court’s holding in Home Depot USA, Inc. v. Brian Hamer, Case No. 4-09-0611, Illinois Appellate Court, 4th Dist. 2010. As a threshold matter, it must be noted that Home Depot, *supra* is not a published opinion, but rather an unpublished order issued by the Illinois Appellate Court pursuant to Illinois Supreme Court Rule 23. Rule 23(e) provides in relevant part that “an unpublished order of the court is not precedential and may not be cited by any party ...[.]” Moreover, even if Home Depot were precedent in this state, for the reasons enumerated below I find that this ruling does not support the taxpayer’s contentions.

In Home Depot, *supra*, the court found that Home Depot USA, Inc., a retailer, did not bear the burden of the ROT and therefore could not claim a bad debt write-off for sales tax

purposes for uncollected ROT it reported and paid to the Department. XYZ 's argument assumes that the reasoning in Home Depot authorizes a bad debt write-off to any entity that bears the burden of a default whether or not that entity is a retailer. For the reasons enumerated below, I disagree with this construction of the ruling in Home Depot.

In addition to requiring that the person claiming the debt bear the burden of the bad debt write-off, ROT regulation §130.1960(d) of the bad debt regulation expresses two additional requirements which XYZ would have to satisfy in order to be entitled to a bad debt refund or credit. First, XYZ would have to be a retailer, and second XYZ would have to be the remitter of the tax. 86 Ill. ROT regulation § 130.1960(d)(1) (“[A] retailer ... is entitled to a bad debt credit with respect to the original sale in which the default has occurred to the extent to which he has paid Retailers’ Occupation Tax on a portion of the price which he does not collect ...[.]”). See also Snyderman v. Isaacs, 31 Ill. 2d 192, 196 (1964) (“[T]he only person entitled to receive credit is the remitter of the tax.”). In the instant case, XYZ did not remit ROT on the defaulted accounts giving rise to the bad debt write-offs it is claiming; the retailers it financed did. Stip. ¶ 7.

In sum, the only persons authorized to obtain a credit under the bad debt regulation are the retailers who remitted ROT in the first place. ROT regulation § 130.1960(d). Had Home Depot USA, Inc. borne the burden of the loss on the ROT it paid but never collected, it would have satisfied all of the requirements of the aforementioned regulation because it also was a retailer that remitted the ROT. However, because XYZ is not a retailer and did not remit any ROT, the requirements spelled out in section 130.1960(d) cannot be met even though it may have borne the burden of the bad debt loss as required by the court’s order in Home Depot. Consequently, the fact that XYZ ultimately may have borne the loss that arose from the bad debt

is insufficient in and of itself to show that it met all of the requirements of ROT regulation §130.1960(d). In sum “[s]ince XYZ was not the party that remitted the taxes in question to the Department, [it] was not entitled to the claims [it] seek(s), and it is of no import whether [it] may have borne the ultimate burden of the tax.” Department’s Brief p. 3.

In Home Depot, *supra*, Home Depot USA, Inc. failed to show that it bore the burden of the tax and therefore was determined not to be entitled to a bad debt write off for sales tax purposes. However, Home Depot USA, Inc. otherwise satisfied the requirements of ROT regulation §130.1960(d). Because XYZ is not a retailer and did remit any ROT, it did not satisfy these requirements. Therefore, the reasoning in Home Depot does not support XYZ’s contention that ROT regulation §130.1960(d) provides a sound legal basis for its refund claim.

Whether XYZ is Entitled to Refund as Assignee of Rights of Retailers who Made Sales

In addition to its claims that it is entitled to relief under Illinois’ statutory and regulatory scheme governing the ROTA’s bad debt write-off refund or credit, XYZ argues that it is also entitled to relief because it possesses the same rights that the retailers it financed possessed – i.e. that “it is the assignee of the rights of retailers who made sales to seek refunds under the Bad Debt Regulation [ROT Regulation §130.1960].” Taxpayer’s Brief p. 10. As previously noted, XYZ’s arguments regarding its acquisition of the rights of the retailers it financed ignore the express statutory and regulatory conditions set forth within ROTA § 6 and ROT regulation § 130.1960(d). Moreover, before a credit may be assigned, the Department must first determine that one is due to a particular retailer. 35 ILCS 120/6; 86 Ill. Admin. Code §130.1505. Yet the parties’ stipulations do not establish that any of the retailers in the instant case paid tax in error on any particular transaction for which XYZ extended financing. Specifically, there is nothing to suggest that: (1) some sales of motor vehicles by retailers to purchasers using financing

provided by XYZ were not subject to sales tax; or that (2) some specific retailer — as opposed to XYZ — incurred some bad debt as a result of the sales for which XYZ extended financing. The record in this case indicates that the tax the retailers paid was due; the retailers actually received all of the gross receipts due regarding the sale through their financing arrangements with XYZ ; and none of the retailers ever incurred any bad debt from the customers’ defaults to XYZ because XYZ did not exercise any right of recourse with any of the retailers. Stip. ¶¶ 7, 9, 10.

The assignment rights granted by the ROTA pertain only to the assignment of credits that have been determined to be due by the Department, which the ROTA allows to be issued in another taxpayer’s name. 86 Ill. Admin. Code §130.1505. This statutory assignment right is not applicable here because the Department never determined any credits were due to any of the retailers XYZ received assignments from.

Given that XYZ can rely upon no statutory or regulatory authority for the assignment rights it claims, XYZ ’s contention must be viewed as nothing more than an attempt to create, through its contractual rights as an assignee, a right to a refund or credit that is not granted by statute or regulation. Section 6 authorizes a credit or refund to be made available to retailers who have both borne the burden of paying ROT, and actually paid ROT to the Department in error. 35 ILCS 120/6; Snyderman, *supra* at 196; Peoples Store of Roseland, *supra* at 152. XYZ , however, would expand the scope of ROTA’s special statutory remedy for bad debt write-offs accorded to retailers into a much broader grant of a credit that would be available to financiers who are not retailers, who were never subject to the tax imposed by the ROTA, and who never paid ROT to the Department. No such credit is authorized by the express text of ROTA § 6. 35 ILCS 120/6; Peoples Store of Roseland, *supra* at 152. As noted by the Department, “private

parties cannot contractually agree between themselves to change state statutes, or a state regulatory framework.” Department’s Brief p. 3.

In sum, according relief to XYZ based solely upon rights it claims were assigned to it by the retailers it financed would completely defy the state’s statutory and regulatory scheme for according bad debt relief from ROT to retailers that suffer bad debt losses. Parties to contracts cannot accord to themselves powers and rights that defy state laws. Progressive Universal Insurance Co. of Illinois v. Liberty Mutual Fire Insurance, 215 Ill. 2d 121, 129 (2005)(“[A] statutes requirements cannot be avoided through contractual provisions.”). Irrespective of its contractual agreements as an assignee, since XYZ does not meet the statutory requirements for availing itself of relief from bad debt write-offs under this state’s statutes and regulations, it is not entitled to a refund or credit for bad debts.

XYZ ’s claim based on its status as the assignee of the retailers it financed also assumes that the retailers it financed had rights to cede to XYZ in the first place. For the reasons enumerated below, I find that this assumption is incorrect.

The only way the retailers that assigned their rights to XYZ would have been entitled to a bad debt refund or credit under ROT regulation §130.1960(d) was if the customers’ defaults to XYZ caused the retailers themselves to incur a bad debt. ROT regulation §130.1960(d) of the bad debt regulation expresses two requirements that must be met in order for the retailers in the instant case to have been entitled to a bad debt refund or credit. First, the retailers would have been entitled to a bad debt refund or credit had they been the ones that extended financing to their customers, and had the customers’ subsequent defaults thereby actually caused the retailers to incur a bad debt. See ROT regulation §130.1960(d)(1)(“[The retailer] is entitled to a bad debt credit with respect to the original sale in which the default occurred to the extent to which he has

paid Retailers' Occupation Tax on a portion of the price which he does not collect ...[.]"). In the instant case, the retailers did not finance their retail sales; XYZ did. Stip. ¶3.

Alternatively, the retailers would have been entitled to a bad debt credit if any of their assignments to XYZ were "with recourse." ROT regulation §130.1960(d)("The retailer is entitled to a bad debt credit with respect to the original sale in which the default has occurred to the extent to which he has paid the Retailers' Occupation Tax on a portion of the price which ... he is not permitted to retain because of being required to make repayment thereof to a lending agency under a 'with recourse' agreement."). In the instant case, the evidence of record indicates that XYZ took assignment of the retailers' accounts without recourse. Specifically, the parties have stipulated that, upon default, the burden of protecting itself from loss fell exclusively upon XYZ. Stip. ¶¶ 7-10.

In sum, the persons authorized to obtain a credit or refund under ROT regulation §139.1960(d) are the retailers who remitted ROT in the first place, and who themselves incurred a bad debt as a result of not having collected the entire selling price for the tangible personal property sold. ROT regulation §130.1960(d). Since the retailers in this case did not meet these requirements they were not entitled to a refund or credit for bad debts. An assignee can obtain no greater right or interest than that possessed by the assignor and can assert no greater rights than the assignor could assert. A.J. Maggio Co. v. Willis, 316 Ill. App. 3d 1043 (1st Dist. 2000); Owens v. McDermott, Will & Emery, 316 Ill. App. 3d 340 (1st Dist. 2000); Sabath v. Mansfield, 60 Ill. App. 3d 1008 (1st Dist. 1978). Because the retailers that assigned their rights to XYZ were not entitled to a bad debt write-off, they could not cede a right to such relief to XYZ. *Id.*

Whether XYZ is Entitled to Relief Based Upon Unjust Enrichment to the State

Finally, XYZ argues that the denial of its refund claim results in unjust enrichment to the Department. “Denial of XYZ’s claim would result in the Illinois Department of Revenue retaining taxes paid even though the consumer never paid the entire purchase price of the motor vehicle, thereby unjustly enriching the Illinois Department of Revenue and forcing XYZ to bear not only the burden of the bad debt but to bear the burden of paying taxes on a full purchase price it never received.” Taxpayer’s Brief p. 17. XYZ argues that, by refusing to allow its claim for refund, the Department is retaining a tax paid in error, resulting in unjust enrichment to the Department.

As a threshold matter, the record contains insufficient evidence to prove that XYZ bore the entire burden of the bad debts that resulted from defaults on accounts it acquired. It can reasonably be assumed that XYZ was aware that it was not going to be paid on some of the accounts it acquired and that it protected itself from all or some portion of this anticipated loss through income components (e.g. service fees, late fees) contained in its financing arrangements. However, the types of arrangements XYZ made to reimburse itself for all or some portion of its anticipated loss are not in evidence. For reasons that have previously been enumerated, the burden of proving the extent of its actual economic loss in this case rested with XYZ. A.R. Barnes, supra.

Even if XYZ could prove that a windfall to the state was the practical result of a default of debt financed by XYZ, this taxpayer still must satisfy all of the requirements of section 6 of the ROTA and ROT regulation §130.1960(d) to be entitled to a refund. XYZ’s “unjust enrichment” argument ignores the fact that, just as its obligation to pay taxes can only be justified by a statute, its right to a refund or credit for taxes paid exists only because of a statute.

People ex rel Eitel v. Lindheimer, 371 Ill. 367 (1939). Consequently, “[I]n the absence of an authoritative statute, taxes voluntarily, though erroneously paid, cannot be recovered ... [.]” *Id.* at p. 371.

As is clearly evident from the foregoing analysis of section 6 of the ROTA and ROT regulation §130.1960(d), the provisions at issue in this case, no section within the Retailers’ Occupation Tax Act or the Department’s administrative regulations authorizes a credit to be given to XYZ under the circumstances described within the parties’ stipulation and the testimony and documents contained in the record. Simply put, this state’s statutes and regulations deny the relief the taxpayer seeks on unjust enrichment grounds.

While XYZ desires that, as a matter of equity, Illinois provide tax relief for defaulted debt under its financing agreements, to date the Illinois legislature has not done so. Accordingly, XYZ’s claim of unjust enrichment remains an issue of public policy rather than a legal issue and can only be addressed by the General Assembly. Until the legislature addresses this matter, this Tribunal does not possess the authority to ignore the mandates of the current law and accord the relief from “unjust enrichment” the taxpayer seeks.

Conclusion:

For all of the foregoing reasons, I recommend that the Director finalize the Department’s refund claim denial at issue in this case, as issued.

Ted Sherrod
Administrative Law Judge

Date: September 11, 2013