

STATE OF CALIFORNIA
BOARD OF EQUALIZATION

130.0095

BUSINESS TAXES APPEALS REVIEW SECTION

In the Matter of the Petition)
for Redetermination and Claim) DECISION AND RECOMMENDATION
for Refund Under the Sales and)
Use Tax Law of:)
T--- C--- M--- CORPORATION) Nos. SZ --- XX-XXXXXX-002
Petitioner/Claimant) SZ --- XX-XXXXXX-020

The Appeals conference in the above-referenced matters was held by Senior Staff Counsel W. E. Burkett on June 29, 1994 in Houston, Texas.

Appearing for Petitioner/Claimant: Mr. O--- L. G---
--- Financial Services

Mr. H. C. P---
Tax Analyst
--- Financial Services

Appearing for the Sales and Use Tax Department: Mr. Sidney Zigelman
Area Administrator

Mr. Joe Clayton
Supervising Tax Auditor

Mr. Donald Packard
Senior Tax Auditor

Protested Item

The protested tax liability for the period April 1, 1990 through June 30, 1990 is measured by:

<u>Item</u>	<u>State, Local and County</u>
Credit denied for bad debt written off	\$1,749,463

Contention of Petitioner/Claimant

File -020 - The Petition for Redetermination

The bad debt was properly written off and qualifies for the deduction provided by law.

File -002 - The Claim for Refund

The measure of tax and contention for the claim for refund are the same as set forth above for File -020.

Summary

This decision involves a petition for redetermination and a claim for refund resulting from a single sale at retail. T--- C--- M--- Corporation, (Petitioner/Claimant hereafter), was, at the time of the sale, engaged in the business of selling medical equipment. It has since merged with G--- M--- Systems (G---) and has been liquidated. G--- is pursuing these matters as the successor in interest.

The petition and claim arose as a result of a single sale of medical equipment to S--- N. A---, M.D., dba V--- D--- Center (VDC). The purchaser, VDC, obtained the funds to purchase the property from Wells Fargo Bank. Petitioner agreed to guarantee the note to Wells Fargo in order for the purchaser to obtain the purchase funds. VDC subsequently defaulted on the note and the petitioner paid off the note as required by the terms of the guarantee contract. The bad debt was written off against a reserve set up in 1989.

The Sales and Use Tax Department (Department) denied credit for the bad debt written off on the basis that the debt was not from a credit sale but rather from the guarantee contract. Petitioner the paid the tax under protest and filed a timely claim for refund.

The petitioner/claimant contends that the bad debt write-off should be allowed because the debt arose from a retail sale by the petitioner. Several rulings allowing deductions for debts assigned with recourse and subsequently paid off by the retailer have been cited in support of the claim.

Analysis & Conclusions

It is our conclusion that the petitioner/claimant was not entitled to a bad debt deduction for the subject sale. A retailer is entitled to a bad debt deduction for accounts found to be worthless and written off for income tax purposes. (Revenue and Taxation Code Section 6055.) However, the foundation for the claim must, in each instance, be a credit sale made by the

retailer. In this matter, the petitioner/claimant received cash for the sale from the purchaser. Therefore, its subsequent liability arose not from the sale but from the guarantee contract with the bank.

A guaranty is a collateral undertaking that cannot exist without a principal or substantive liability to which it is collateral. (See Powers Regulator Co. v. Seaboard Surety Co., 204 Cal.App.2d 338, 347 (1962).) If there is no primary obligation on the part of a third party, there is nothing to guarantee and hence no contract of guaranty. (Somers v. United States F. & G. Co., 191 Cal. 542.) It is thus clear that the debt paid off by petitioner/claimant was not from a credit sale made by it.

While there are a number of rulings which have allowed the retailer to take a deduction for an account which was written off after performing on a recourse obligation, in each case the source of the obligation was a credit sale by the retailer. Since the source of this debt was not a credit sale at retail by the petitioner/claimant, it is not entitled to a deduction or to a refund of the taxes paid on this amount.

Recommendation

It is recommended that the petition for redetermination and claim for refund be denied.

W. E. BURKETT, SENIOR STAFF COUNSEL

8-4-94

DATE