

ORDER OF THE DEPARTMENT OF REVENUE CREATING RULES

The Wisconsin Department of Revenue adopts an order to: **create** Tax 9.70; **relating to** cigarette and tobacco products tax bad debt deductions.

Analysis by the Department of Revenue

Statutes interpreted: ss. 139.362 and 139.801, Stats.

Statutory authority: s. 227.11 (2) (a), Stats.

Explanation of agency authority: Each agency may promulgate rules interpreting the provisions of any statute enforced or administered by it, if the agency considers it necessary to effectuate the purpose of the statute.

Related statute(s) or rule(s): There are no other applicable statutes or rules.

Plain language analysis: This rule clarifies the following as to when and how a person who pays cigarette taxes or a distributor who pays tobacco taxes is to claim the deduction allowed under ss. 139.362 and 139.801, Stats. for cigarette and tobacco products tax attributable to bad debt:

- The deduction shall be claimed on the monthly tax report for the month in which the debt is written off as uncollectible and is eligible to be deducted as a bad debt under s. 166 of the Internal Revenue Code. A claimant shall complete Form CT-117, *Cigarette Distributor Bad Debt Deduction for Uncollectible Wisconsin Cigarette Tax*, or Form TT-117, *Tobacco Products Distributor Bad Debt Deduction for Uncollectible Wisconsin Tobacco Products Tax*, for all amounts claimed.
- Payments and credits applied to a debt before it is written off as uncollectible shall be apportioned to the amount of such debt attributable to cigarette or tobacco products tax using the ratio of the total cigarette or tobacco tax to be paid per the invoice to the total amount to be paid per the invoice. The amount so apportioned shall reduce the amount of debt attributable to cigarette or tobacco tax to arrive at the amount of the deduction.
- If the deduction is claimed for a month when the cigarette or tobacco products tax rate is different from the rate in effect when the cigarettes or tobacco products were sold, the tax rate in effect when the cigarettes or tobacco products were sold shall be used to determine the deduction.
- A deduction shall not be allowed for cigarette and tobacco products tax attributable to bad debt incurred on illegal sales of cigarettes or tobacco products.
- A recovery of a bad debt for which a deduction was claimed shall be included in the monthly tax report for the month in which the recovery occurs, and the tax shall be paid with the report.

Summary of, and comparison with, existing or proposed federal regulation: There is no existing or proposed federal regulation that is intended to address the activities to be regulated by the rule.

Comparison with similar rules in Illinois, Iowa, Michigan, and Minnesota:

- Illinois – No similar rule exists.
- Iowa – No similar rule exists.
- Michigan – Michigan has a provision for a tobacco products tax bad debt deduction.

The amount deducted must be charged off as uncollectible on the books of the licensee and must be eligible to be claimed as a bad debt deduction for federal income tax purposes. A recovery of any amount that has been deducted must be paid back by the licensee. Only the portion of the bad debt attributable to tobacco products tax is deductible.

- Minnesota – Minnesota has a provision for a credit for cigarette taxes attributable to a bad debt. The taxes must have been included in a transaction the consideration for which was a debt owed to the taxpayer and which became uncollectible, but only in proportion to the portion of debt that became uncollectible. The debt must qualify as a bad debt for federal income tax purposes. A recovery of the cigarette taxes claimed as a refund must be paid back by the taxpayer.

Summary of factual data and analytical methodologies: 2005 Wisconsin Act 25 created ss. 139.362 and 139.801, Stats., which allow a deduction for cigarette and tobacco products tax attributable to bad debt. In reviewing the statutory language providing for the deduction, the department concluded that it would need to provide clarification as to when and how the deduction may be claimed. Starting with language from s. Tax 4.12, which clarifies when and how a supplier required to be licensed by the department may recover the motor vehicle fuel tax from the department when a purchaser is unable to pay the tax to the supplier, the department developed this rule.

Analysis and supporting documents used to determine effect on small business:

The rule provides clarification that will help determine the allowable amount of the deduction for cigarette and tobacco products tax attributable to bad debt under ss. 139.362 and 139.801, Stats., and when the deduction may be claimed. As the rule does not impose any significant financial or other compliance burden, the department has determined that it does not have a significant effect on small business.

Anticipated costs incurred by private sector: This rule does not have a significant fiscal effect on the private sector.

Effect on small business: This rule does not have a significant effect on small business.

Agency contact person: Please contact Dale Kleven at (608) 266-8253 or dkleven@dor.state.wi.us, if you have any questions regarding this rule.

SECTION 1. Tax 9.70 is created to read:

Tax 9.70 Cigarette and tobacco products tax bad debt deductions. (1) PURPOSE.

This section clarifies when and how a person who pays cigarette taxes or a distributor who pays tobacco taxes may claim a deduction under ss. 139.362 and 139.801, Stats., for cigarette and tobacco products tax attributable to bad debt.

(2) DEFINITIONS. In this section:

(a) "Bad debt" has the meaning given in ss. 139.362(1) and 139.801(1), Stats.

(b) "Cigarette" has the meaning given in s. 139.30(1m), Stats.

(c) "Distributor" has the meaning given in s. 139.75(4), Stats.

(d) "Tobacco products" has the meaning given in s. 139.75(12), Stats.

(3) BAD DEBTS. (a) *Deduction from measure of tax.* Using form CT-117, titled "Cigarette Distributor Bad Debt Deduction for Uncollectible Wisconsin Cigarette Tax," or form TT-117, titled "Tobacco Products Distributor Bad Debt Deduction for Uncollectible Wisconsin Tobacco Products Tax," a person who pays cigarette taxes or a distributor who pays tobacco taxes may claim a deduction on the monthly tax report for the cigarette and tobacco products tax attributable to bad debt that is written off as uncollectible in their books and records and that is eligible to be deducted as bad debt under s. 166 of the internal revenue code.

(b) *When to report the deduction.* The deduction under par. (a) shall be claimed on the monthly tax report that is submitted for the month in which the amount of the deduction is written off as uncollectible and in which such amount is eligible to be deducted as a bad debt under s. 166 of the internal revenue code.

Example: A distributor writes off a debt attributable to tobacco products tax on September 10, 2005. At the time the debt is written off it is eligible to be deducted as a bad debt under s. 166 of the internal revenue code. The distributor may claim a bad debt deduction by attaching a completed form TT-117 to the monthly tobacco products tax report filed for the month of September 2005.

(c) *Recovery of bad debt.* If a person who pays cigarette taxes or a distributor who pays tobacco taxes subsequently collects in whole or in part any bad debt for which a deduction is claimed under par. (a), they shall include the amount collected in the monthly tax report filed for the month in which the amount is collected and shall pay the tax with the report.

(d) *Payments and credits.* Payments and credits applied to a debt before it is written off as uncollectible shall be apportioned to the amount of such debt attributable to cigarette or tobacco products tax on the basis of the ratio of the cigarette or tobacco products tax to be paid per the invoice to the total amount to be paid per the invoice. The amount so apportioned shall reduce the amount of debt attributable to cigarette or tobacco products tax to arrive at the deduction under par. (a).

Examples: 1) At a time when the cigarette tax rate is 3.85¢ per stick, Person A sells cigarettes to Customer B. The amount of the invoice is \$10,000, consisting of cigarette tax of \$1,540, cost of cigarettes of \$6,000 and sundries of \$2,460. Customer B defaults and discontinues operations, leaving a balance due to Person A of \$2,100, which includes interest of \$200 not included in the original invoice amount. The deductible tax is \$292.60, computed as follows:

Tax per invoice		\$1,540.00
Invoice amount	\$10,000.00	
Unpaid invoice amount –	<u>-1,900.00</u>	
Paid invoice amount	\$8,100.00	
Portion constituting tax*	<u> x.154</u>	
Tax paid		- <u>\$1,247.40</u>
Tax that may be deducted		\$292.60

*\$1,540 tax ÷ \$10,000 invoice amount = .154.

2) At a time when the tobacco products tax rate is 25% of the manufacturer's wholesale list price, Distributor A sells tobacco products to Customer B. The amount of the invoice is

\$9,500, consisting of tobacco products tax of \$1,250, cost of tobacco products of \$5,000 and sundries of \$3,250. Customer B defaults and discontinues operations, leaving a balance due to Distributor A of \$3,000, which includes interest of \$200 not included in the original invoice amount. The deductible tax is \$365.60, computed as follows:

Tax per invoice		\$1250.00
Invoice amount	\$9,500.00	
Unpaid invoice amount –	<u>-2,800.00</u>	
Paid invoice amount	\$6,700.00	
Portion constituting tax*	<u>x.132</u>	
Tax paid		- <u>\$884.40</u>
Tax that may be deducted		\$365.60

*\$1,250 tax ÷ \$9,500 invoice amount = .132.

(e) *Tax rate change.* If the deduction under par. (a) is claimed for a month when the cigarette or tobacco products tax rate is different from the tax rate in effect when the cigarettes or tobacco products were sold, the tax rate in effect when the cigarettes or tobacco products were sold shall be used to determine the amount of the deduction.

(f) *Illegal sales.* No deduction under par. (a) shall be allowed for cigarette and tobacco products tax attributable to bad debt incurred on sales of cigarettes or tobacco products sold in violation of state or federal law.

Example: Sales of banned products sold in violation of the directory of certified manufacturers and brands, s. 995.12, Stats.

Note: Section Tax 9.70 interprets ss. 139.362 and 139.801, Stats.

Note: Sections 139.362 and 139.801, Stats., were created by 2005 Wis. Act 25, and took effect on September 1, 2005.

The rules contained in this order shall take effect on the first day of the month following publication in the Wisconsin administrative register as provided in s. 227.22(2)(intro.), Stats.

Final Regulatory Flexibility Analysis

This rule order does not have a significant economic impact on a substantial number of small businesses.

DEPARTMENT OF REVENUE

Dated: _____

By: _____
Roger M. Ervin
Secretary of Revenue

E:Rules/970 Final Order