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Bad Debts are Deductible for Pennsylvania Gross Receipts Tax Purposes - Provided Proper Documentation is Available

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Publication Date: July 25, 2011

The Pennsylvania Department of Revenue recently issued *Corporation Tax Bulletin 2011-02*. The *Bulletin* provides some general guidance on the accounting method that must be used for computing the gross receipt taxes that Pennsylvania imposes on electric companies, telecommunications providers, transportation companies and certain other taxpayers. Of most interest to taxpayers, however, is the guidance that the *Bulletin* also provides on what has recently been a hot topic in Pennsylvania, the deductibility of bad debts for purposes of the gross receipts tax.

Pennsylvania's gross receipts tax is imposed upon each dollar of gross receipts "received" by certain specified utility-type businesses, including electric companies, telecommunications providers, and transportation companies.[1] There is no specific provision in the gross receipts tax statute or regulations providing for a deduction for bad debts, but taxpayers have long argued that to the extent gross receipts tax is remitted for sales to customers that were ultimately written off as bad debt, that tax should be refundable because it was based on amounts that are not "receipts" includable in the tax base. In *Popowsky v. Pennsylvania Public Utility Commission*, the Commonwealth Court blessed such an adjustment by acknowledging that gross receipts tax was not due on amounts billed that proved uncollectible.[2]

In *Corporation Tax Bulletin 2011-02*, the Department states that it will be requiring gross receipts taxpayers to support bad debt deduction claims with the following: (1) the type and amount of receipts the taxpayer has written off, (2) the location of the customer whose debt was written, and (3) the tax period during which the receipts were reported as taxable to Pennsylvania.[3]

The Department's goal seems to be to force taxpayers who are making bad debt refund claims to provide documentation that would tie those claims to receipts reported for specific Pennsylvania sales, rather than allowing taxpayers to rely on general statistical studies. In a number of recent cases, Pennsylvania's administrative tax review boards (the Board of Appeals and the Board of Finance and Revenue) have refused to provide relief on gross receipts tax bad debt claims-often concluding that the taxpayer "has not proved the correct amount of bad debts," and accordingly have denied such refund claims. By clarifying the documentation needed to support a bad debt refund claim, the *Bulletin* actually increases the likelihood that taxpayers that present the proper documentation will be granted relief on their gross receipts tax bad debt refund claims at the Administrative Boards. In contrast, the issuance of the *Bulletin* makes it less likely that taxpayers with gross receipts tax bad debt refund claims supported solely by statistical studies will be granted any relief at the Administrative Boards.

If you have questions about how to recover Pennsylvania gross receipts tax submitted in connection with uncollectible accounts, or how to strengthen the documentation that has been submitted with pending gross receipts tax refund claims, please contact the author of this article, or the Reed Smith lawyer with whom you usually work. For more information on Reed Smith's Pennsylvania tax practice, visit www.reedsmith.com/patax.

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1. 72 P.S. § 8101.
2. 695 A.2d 448 (1997).

3. This is not unlike the information required to be made available in other states. See for example California SBE Publication No. 76 (3/1/2010).

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