

SECTION 45 - BASIS OF REPORTING**45-1 VENDOR'S RECORDS**

Every vendor must keep adequate and complete records as required by G.S. 105-164.31 to determine the amount of sales and use tax for which he may be liable. Vendors having both cash and credit sales may elect to report their tax liability on either the cash or accrual basis of accounting provided their records are kept in such a manner that they can determine their tax liability correctly on the basis used. If a taxpayer wishes to change from one basis of reporting to another, he must apply to the Secretary of Revenue for permission to make such change.

History Note: Authority G.S. 105-164.22; 105-264;
Issued: June 1, 1996.

45-2 ACCRUAL BASIS

When a vendor elects to report and pay tax on the accrual basis, he must keep records which disclose a separate accounting of taxable and nontaxable sales. The vendor must pay tax on the total sales price of all taxable tangible personal property sold during the period covered by the return, whether or not such sales are cash, credit, installment or conditional sales and whether or not the vendor retains the installment and conditional sales contracts or sells or assigns them to others and without regard to any finance reserve withheld on finance paper sold or assigned to others. Finance charges, service charges or interest from credit extended under conditional sales contracts providing for deferred payment of the purchase price are not subject to tax if such charges are separately stated on the invoices given to the customers at the time of sale and in the vendor's records of sales. If, in reporting on the accrual basis, accounts of purchasers representing taxable sales on which the tax has been paid are found to be worthless and actually charged off for income tax purposes, the amount charged off representing taxable sales may at corresponding periods be deducted from gross sales provided the vendor maintains records disclosing separately that portion of bad accounts representing taxable sales and that portion representing nontaxable sales. Accounts charged off as bad debts must be added to gross sales if afterwards collected.

History Note: Authority G.S. 105-164.3; 105-164.22; 105-264;
Issued: June 1, 1996.

45-3 CASH BASIS

- A. When a vendor having both taxable and nontaxable sales elects to report and pay tax on the cash basis, the vendor must keep records which disclose a separate accounting of taxable and nontaxable sales and receipts on sales. Such vendor must pay tax on the total sales price of all taxable tangible personal property sold for cash during the period covered by the return and on that portion of the sales price collected or constructively received during such period on taxable tangible personal property sold on credit, installment or other deferred payment sales contracts without any arbitrary allocation for finance charges, service charges or interest charges. Finance charges, service charges and interest charges for credit extended under conditional sales contracts providing for deferred payment of the purchase price are not subject to the tax if such charges are separately stated on the invoices given to the customers at the time of sale and in the vendor's records of sales and collections. If, on conditional, installment or other deferred payment sales, the vendor sells or assigns the finance paper, he is deemed to have received the full balance of the consideration for the sale of tangible personal property and is liable for remitting tax on the total sales price of such property at the close of the period during which the paper was assigned or sold including any finance reserve withheld on the finance paper. If such vendor sells his accounts receivable he is liable for payment of tax on the outstanding taxable

balance of such accounts at the time they are sold notwithstanding that the accounts may be sold at a discount to the purchaser.

- B.** When persons filing their sales tax reports on the cash basis of accounting sell their accounts receivable, they are liable for payment of sales tax on their taxable accounts receivable balance outstanding at the time they sell such accounts. When a corporation is formed to succeed a proprietorship or partnership and the accounts receivable are sold to the corporation, the proprietorship or partnership is liable for remitting the sales tax due on its outstanding taxable accounts receivable balance at the time the accounts are sold.

History Note: Authority G.S. 105-164.3; 105-164.22; 105-264;
Issued: June 1, 1996.

45-4 WORTHLESS ACCOUNTS (BAD DEBTS)

- A.** In reporting sales and use taxes on an accrual basis, accounts of purchasers representing taxable sales on which the tax has been paid may be determined to be worthless and will actually be charged off for income tax purposes as "bad debts." The term "bad debts" has the same meaning as defined by 26 U.S.C. Sec.166, but does not include the following: finance charges or interest; sales and use taxes charged on the sales or purchase price; amounts that cannot be collected on property that remains in the possession of the seller until the purchase price is paid; expenses incurred in attempting to collect debt; and repossessed property. The amount charged off representing taxable retail sales may, during corresponding periods, be deducted from gross taxable sales provided the vendor maintains records disclosing separately the portion of bad debts representing taxable sales and the portions representing nontaxable sales. The amount of any deduction taken that is attributable to bad debts shall not include accrued interest.
- B.** In order for a worthless account to be "charged off for income tax purposes," the account must be written off as uncollectible on the claimant's books and records. If the charge-off is not made until the income tax return is filed, the bad debt should generally be deducted within one month of the date the income tax return reflecting the bad debt is filed. If the charge-off is made during the income tax year, the deduction of the bad debt should be taken for the period in which the charge-off occurs. A taxpayer is required to make the deduction for sales and use tax purposes within three years of charging off an account for income tax purposes. If a taxpayer fails to deduct a bad debt for sales and use tax purposes within three years of the date the bad debt is deducted for income tax purposes, the deduction from taxable gross receipts is not allowable.

A taxpayer who is not required to file income tax returns may deduct a bad debt on a return filed for the period in which the bad debt is charged off in its books and records as uncollectible and would otherwise be eligible for a bad debt deduction for income tax purposes if the taxpayer were required to file income tax returns. In this instance, the taxpayer is required to make the deduction for sales and use tax purposes within three years of the date the account is recognized and finally expensed as a bad debt in its books and records.

- C.** If the amount of the bad debt deduction exceeds the amount of taxable sales and the tax due is a credit (negative) balance on the sales and use tax return, a refund claim may be filed within the statute of limitations for filing refund claims. The claim must be filed within three years of the date the bad debt becomes eligible for deduction from gross retail sales on the sales and use tax return.
- D.** If a deduction is taken for a bad debt and the debt is subsequently collected in whole or in part, the tax on the amount collected must be paid and reported on the sales and use tax return filed for the period in which the collection occurs. For purposes of reporting collection of the bad debt subsequent to having charged off and deducted such bad debt, any payments on the debt shall

be applied first proportionally to the taxable price of the property or service and sales tax thereon, and secondly to interest, service charges, and any other charges.

- E.** Effective with the entry of North Carolina as a member state to the Streamlined Sales and Use Tax Agreement (Agreement), a Certified Service Provider (CSP) who enters into a contract with the Governing Board of the Agreement to offer services to collect and remit sales and use taxes on behalf of a seller/taxpayer may claim any bad debt deduction that would ordinarily be claimed by the seller/taxpayer. The terms of the contract between the Governing Board and a CSP will establish the procedures for credits by the CSP to a seller/taxpayer for allowable bad debt taken by the CSP.

History Note: Authority G.S. 105-164.3; 105-164.13; 105-164.22;
105-164.42C; 105-164.42I; 105-264;
Issued: October 11, 2010; July 1, 2005.