

OHIO BOARD OF TAX APPEALS

Home Depot USA, Inc.,)	CASE NOS. 2006-M-206, 207
)	
Appellant,)	(SALES TAX)
)	
vs.)	DECISION AND ORDER
)	
William W. Wilkins,)	Affirmed on Appeal April 2, 2009
Tax Commissioner of Ohio,)	Ohio Supreme Court No. 2008-1182
)	
Appellee.)	2009-Ohio-1431

APPEARANCES:

For the Appellant -	Thompson Hine LLP Jeffrey J. Erney Gregory J. Gawlik 3900 Key Center 127 Public Square Cleveland, Ohio 44114
For the Appellee -	Thomas R. Winters First Assistant Attorney General of Ohio Damion M. Clifford Assistant Attorney General State Office Tower 30 East Broad Street, 25 th Floor Columbus, Ohio 43215

Entered May 20, 2008

Ms. Margulies, Mr. Eberhart, and Mr. Dunlap concur

This cause and matter comes to be considered by the Board of Tax Appeals upon notices of appeal filed on February 6, 2006. Appellant challenges two final determinations of the Tax Commissioner, appellee, wherein the commissioner denied refund claims for the periods January 1, 1998 through December 31, 2000 and January 1, 2001 through July 31, 2003.

The two notices of appeal are identical except for the tax periods involved, and seek refunds of sales taxes originally paid by Home Depot USA, Inc. (“Home Depot”) on sales of consumer goods within the state of Ohio. Home Depot specifies the following as error:

“A. The Tax Commissioner erred in denying the Appellant’s bad debt deduction as provided pursuant to Ohio Revised Code (‘R.C.’) 5739.121.

“B. The Tax Commissioner erred in concluding that the Appellant did not satisfy the requirements for claiming a bad debt deduction as set forth in R.C. 5739.121 and Ohio Administrative Code Rule 5703-9-44.

“C. The Tax Commissioner erred in concluding that the appellant did not satisfy the requirement for claiming a bad debt deduction where the record shows that the appellant remitted sales tax to the Department on credit sales, the underlying debt became worthless or uncollectible and the appellant properly deducted the expense on its Federal income tax return.

“D. The Tax Commissioner erred in denying the Appellant’s bad debt deduction where the Appellant, alone, bears the economic risk for the bad debt loss deducted for sales tax purposes.

“E. The Tax Commissioner erred in denying the Appellant’s bad debt deduction resulting in the appellant remitting more Ohio sales tax than it actually collects which discriminates against the Appellant in favor of other vendors in the state.

“F. The Tax Commissioner erred by denying the Petitioner the right to due process of law and equal protection under the Fifth and Fourteenth Amendments of the Constitution of the United States of America, and Article I, Section 2 of the Ohio Constitution, and denying Petitioner the right to due course of law under Article I, §16 of the Constitution of the State of Ohio, by, among other things, improperly denying the Appellant’s bad debt deduction based on the appellant’s method of financing and accounting for credit sales.

“G. The Appellant hereby renews its arguments previously presented to the Tax Commissioner before the Tax Appeals Division to the extent not accepted by the Tax Commissioner in the Final Determination.”

The matter is considered by the Board of Tax Appeals upon the notices of appeal, the statutory transcripts certified to this board by the Tax Commissioner, and the testimony and other evidence adduced at the hearing. The parties have also provided written argument by way of brief.

As a preliminary matter, we consider the admission of appellant’s exhibits 7 and 8. The presiding attorney examiner reserved ruling at hearing. Counsel for the Tax Commissioner objected to the exhibits on the ground that the exhibits were in summary form without supporting documentation. Counsel claimed that they had not received the underlying information. However, a review of the statutory transcript indicates that the underlying information was presented to the Tax Commissioner’s agent during the refund review process. S.T. at 20. Therefore, the Tax Commissioner’s objection is overruled and Appellant’s Exhibits 7 and 8 are received into the evidence to be considered in this matter.

At issue in this appeal are sales made by Home Depot and financed by General Electric Capital Corporation (“General Electric Capital”) and its subsidiaries through use of a “private-label credit card.” A private-label credit card is a card identified as a particular retail store’s credit card and used in a limited number of stores, usually those under a corporate umbrella. In this instance, Home Depot’s

private-label credit card can be used at its retail locations and the locations of its sister company, EXPO Design Center. H.R. at 19.

Testimony at hearing indicated that the private-label credit card business grew out of the difficulty of companies with national presences to comply with state-by-state consumer credit regulations. Federal regulations have also tightened, making the administration of credit-lending programs outside the core competency of retailers like Home Depot. H.R. at 28. However, studies have shown that credit cards identified with a single retailer bring about customer loyalty. A private-label credit card can also be cheaper for the identified retail establishment than general credit cards, such as VISA or MasterCard. H.R. at 20.

Because of the benefits, Home Depot entered into private-label credit card agreements with General Electric Capital. The two corporations actually had three programs operating during the refund periods, the consumer revolving program, the commercial PROX agreement, and the business revolving agreement. H.R. at 23-24, appellant's Exs. 1-3. Each program had a different target customer. However, as is relevant to our determination herein, the programs would operate in similar manners. In return for General Electric Capital presenting credit customers with a credit card with Home Depot's name on it, Home Depot would advertise the program in its stores, solicit customers either through the mail or in-store, and obtain credit applications using General Electric Capital forms. H.R. at 26.

The decision whether or not to provide credit was General Electric Capital's alone. Upon receipt of a credit application (usually transmitted

electronically at the store), General Electric Capital would determine creditworthiness of a particular customer and set a credit limit. H.R. at 26. If the customer then purchased the item with credit established by General Electric Capital, Home Depot would accept the cardholder's number, close the transaction, and then transmit the information to General Electric Capital, which would then transfer funds to Home Depot. The funds transferred on a daily basis, but would be less than the full transaction price, as a "merchant discount" would be deducted. H.R. at 29.

A merchant discount is not unique to private-label credit cards, but is charged by all credit card providers. As Michael J. Mitchell, director of credit-legal for Home Depot explained during his testimony before the board, the merchant discounts of a private-label credit card issuer were usually less than those of a general-purpose credit card issuer. H.R. at 21. Home Depot brought forth testimony at hearing indicating that, with private-label credit card issuers, the merchant discount can be targeted to the customer base. Mr. Mitchell testified that both General Electric Capital and Home Depot do studies to determine the type of customer that will seek credit for Home Depot purchases. That customer profile is taken into account when setting merchant discount fees, as, with sophisticated modeling, the companies are able to predict with some accuracy the cost of running of the programs. H.R. at 36-37.

Mr. Mitchell testified that, in setting merchant fees, bad debts are taken into account:

"Bad debt is part of the cost that GE incurs. And that we –
And our position, of course, is that we prepay all that. GE is

in the business to make money. They did make money during the period that this operated. We're sure of that. And all their costs had to be covered and were covered. And bad debt, expected loss and actual loss was one of their costs." H.R. at 38.

This statement is the crux of the claim made by Home Depot. It is Home Depot's position that General Electric Capital's bad debts were paid by Home Depot through its merchant fees. Home Depot further argues that, as anticipated, General Electric Capital did have accounts that remained unpaid after attempts to collect. Home Depot provides evidence of defaulted accounts for the refund periods. Appellant's Ex. 7, 8. Home Depot claims that it remitted sales tax upon each sale made. The state provides a retailer with a method for reimbursement of sales taxes when certain sales are consummated, but the consumer does not meet financing obligations. Home Depot argues that as the state provides a vendor with a method of reimbursement for sales tax paid on bad debts, and as it prepaid actual bad debts, Home Depot asserts that its refund claims should not have been rejected.

In any appeal from a decision of the Tax Commissioner, the standard by which review takes place begins with the acknowledgement that the Tax Commissioner's findings are entitled to a presumption of correctness and it is incumbent upon a taxpayer challenging a finding of the Tax Commissioner to rebut the presumption and establish a right to the relief requested. *Alcan Aluminum Corp. v. Limbach* (1989), 42 Ohio St.3d 121; *Belgrade Gardens v. Kosydar* (1974), 38 Ohio St.2d 135; *Midwest Transfer Co. v. Porterfield* (1968), 13 Ohio St.2d 138. Moreover, the taxpayer is assigned the burden of showing in what manner and to what

extent the Tax Commissioner's determination is in error. *Federated Dept. Stores, Inc. v. Lindley* (1983), 5 Ohio St.3d 213.

As a general rule, statutory provisions for the refund of taxes illegally or erroneously paid or paid on an illegal or erroneous assessment should be liberally construed in favor of the taxpayer. *Columbus Southern Lumber Co. v. Peck* (1953), 159 Ohio St. 564; *Phoenix Amusement Co. v. Glander* (1947), 148 Ohio St. 592. However, in *Chrysler Financial Co., L.L.C. v. Wilkins*, 102 Ohio St.3d 443, 2004-Ohio-3922, the court considered the Tax Commissioner's denial of a refund under R.C. 5739.121 and concluded that when, as here, the refund does not stem from an illegal or erroneous payment, the refund is more analogous to an exemption or exception from tax and should be strictly construed.

R.C. 5739.121,¹ entitled "Bad debt deduction," provided in pertinent part the following during the major portion of the refund period:

"As used in this section, 'bad debt' means any debt that has become worthless or uncollectible in the time period between a vendor's preceding return and the present return, has been uncollected for at least six months, and that may be claimed as a deduction pursuant to the 'Internal Revenue Code of 1954' 68A Stat. 50, 26 U.S.C. 166, as amended, and regulations adopted pursuant thereto, or that could be claimed as such a deduction if the vendor kept accounts on an accrual basis. 'Bad debt' does not include any interest or sales tax on the purchase price, uncollectible amounts on property that remains in the possession of the vendor until the full purchase price is paid, expenses incurred in attempting to collect any account receivable or for any portion of the debt recovered,

¹ The statute was amended twice during the refund period. The first amendment merely redirected remittances from the treasurer to the Tax Commissioner. Am. Sub. H.B. 94, Eff. Jan. 1, 2002. The second amendment divided the statute into subsections and established a refund procedure when the amount of bad debts to be deducted was greater than the amount of tax due during a reporting period. The substance of the statute remained unchanged. H.B. 95, Eff. Sep. 26, 2003.

any accounts receivable that have been sold to a third party for collection, and repossessed property.

“In computing taxable receipts for purposes of this chapter, a vendor may deduct the amount of bad debts as defined in this section. The amount deducted must be charged off as uncollectible on the books of the vendor. A deduction may be claimed only with respect to bad debts on which the taxes pursuant to sections 5739.10 and 5739.12 of the Revised Code were paid in a preceding tax period. If the vendor’s business consists of taxable and nontaxable transactions, the deduction shall equal the full amount of the debt if the debt is documented as a taxable transaction in the vendor’s records. If no such documentation is available, the maximum deduction on any bad debt shall equal the amount of the bad debt multiplied by the quotient obtained by dividing the sales taxed pursuant to this chapter during the preceding calendar years by all sales during the preceding calendar year, whether taxed or not. If a consumer or other person pays all or part of a bad debt with respect to which a vendor claimed a deduction under this section, the vendor shall be liable for the amount of taxes deducted in connection with that portion of the debt for which payment is received and shall remit such taxes in his next payment to the treasurer of state.

Each party to this appeal accuses the other of seeking (or keeping) sales taxes not rightfully due that entity. Home Depot argues that the Tax Commissioner has received sales tax upon items for which the General Assembly has granted the vendor reimbursement. The Tax Commissioner claims that Home Depot does not fall within the class of persons which may avail themselves of R.C. 5739.121. The Tax Commissioner focuses on the language in the second paragraph² of R.C. 5739.121 – that a bad debt must be “charged off as uncollectible on the books of the vendor.” The Tax Commissioner points out that Home Depot is the vendor, but any bad debt is

² In the current version of R.C. 5739.121, the paragraph is now subsection (B).

charged off General Electric Capital's books. That statement is supported by testimony at hearing. At hearing, Mr. Andrew Donnelly, the tax director for GE Money-Americas, presented tax returns for 1998 through 2003 exhibiting a bad debt deduction taken. H.R. at 93-96, Appellant's Ex. 4. Thus, the Tax Commissioner argues, the vendor, Home Depot, does not charge off the bad debt, as required by statute, but deducts a merchant discount (identified on its tax return as a "credit card discount") as an expense of doing business from gross income.

In *Chrysler Financial Co., L.L.C. v. Wilkins*, 102 Ohio St.3d 443, 2004-Ohio-3922, the Ohio Supreme Court considered a refund claim for sales taxes paid the state on automobiles after the loans securing those automobiles were reduced to bad debts. The refund claims were filed by the lending institution, as the bad debt deductions had been taken by it. The court, however, strictly construed R.C. 5739.121 and concluded that the lending institution was not the vendor of the sale, and, therefore, could not avail itself of the bad debt deduction.

We now have before us facts similar to those found in *Chrysler Financial* – a refund claim for sales taxes paid the state on consumer goods after the loans securing those consumer goods were reduced to bad debts – but a different claimant. The applicant is not the lending institution holding the debt, but the vendor originally making the sale. However, a strict construction of R.C. 5739.121 leads to the same result. Whereas *Chrysler Financial* was not the vendor in the earlier matter, in the present appeal, Home Depot is not the entity reporting the bad debts on its books.

Home Depot argues that it is responsible for the bad debt deduction and does take that deduction on its books each time it deducts a merchant fee, as the fee itself includes a bad debt component. Home Depot brought forth evidence that a consideration of potential losses for non-payment is made in setting merchant fees for private-label credit cards. H.R. at 38. However, a statute that is specific in its requirements must be applied as written. *Columbia Gas Transmission Corp. v. Levin*, 117 Ohio St.3d 122, 2008-Ohio-511. R.C. 5739.121 requires that bad debts *must* be charged off as uncollectible on the vendor's books. The fact that bad debts were *taken into consideration* in deductions on the vendor's books does not meet statutory requirements.

Home Depot argues that the Tax Commissioner's position in this appeal defies the legislative purpose and intent behind R.C. 5739.121 and allows the state to retain taxes that were never collected from the ultimate consumer. The board would agree that the statute as written has limited application under current business practices. When originally passed in Am. Sub. S.B. 16, eff. Oct. 29, 1979, retailers were more likely to provide credit directly to customers. Therefore, the entity making the sale was likely to be the same entity extending the credit. R.C. 5739.121 reflects the unity between retailer and lender, as the statute is written to allow a vendor to remit taxes due after deducting for bad debts. See Ohio Adm. Code 5703-9-44 (which provides "In reporting gross sales and net taxable sales a vendor may exclude an amount equal to the sum of the vendor's bad debts arising from sales occurring on or

after July 1, 1980 and charged off as uncollectible on his books during the sales tax reporting period.”).

In the present appeal, Home Depot is paid the full purchase price (less merchant discount), plus sales tax, which tax it then remits to the state of Ohio. General Electric Capital purchases the right to collect payment from the ultimate consumer. *Chrysler Financial* instructs that the “bad debt” was never Home Depot’s, as when the transaction occurred, the vendor was paid in full. Thus, even if a consumer ultimately defaults, the default occurs after the transaction leaves Home Depot. Thus, the board cannot find that the statute permits reimbursement to Home Depot.

The Tax Commissioner³ argues in the alternative that Home Depot’s proof of claim was not sufficient. However, as this board has concluded Home Depot is not entitled to a refund, we find no reason to consider this claim.

Through its notice of appeal, Home Depot makes a number of constitutional claims, and argues its position through its briefs. The Board of Tax Appeals is without authority to rule on claims of a constitutional nature. Instead, such determination is properly reserved for courts created by Section 1, Article IV, of the Ohio Constitution. *Dublin City School Dist. Bd. of Edn. v. Tracy* (Feb. 14, 1996), BTA No. 1995-K-692, unreported, affirmed on other grounds (1998), 126 Ohio

³ Home Depot argues that the Tax Commissioner cannot claim it did not present sufficient evidence to support its refund claim, as it did not raise that as an issue in his final determination and cites this board’s holding in *Key Services Corp. v. Tracy* (Oct. 15, 1999), BTA No. 1998-K-553, unreported. However, the Supreme Court reversed the board’s holding in *Key Servs. Corp. v. Zaino*, (2002) 95 Ohio St.3d. 11, where the court held that in a proceeding before the Board of Tax Appeals, there is no statutory limit on what the Tax Commissioner may contest.

App.3d 603. See, also, *NACCO Industries v. Tracy* (June 7, 1996), BTA No. 1995-K-1210, unreported, affirmed on other grounds (1997), 79 Ohio St.3d 314. In *MCI Telecommunications Corp. v. Limbach* (1994), 68 Ohio St.3d 195, the court explained this board's role as being limited to a "receiver of evidence" when constitutional issues are raised at this level. Home Depot has availed itself of the hearing process; the board has fulfilled its duty.

Considering the record, the statutes and case law, this board concludes that Home Depot has failed to prove error on the part of the commissioner. Therefore, the Tax Commissioner's final determinations must be, and hereby are, affirmed.

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