

April 28, 2023

The Honorable Morgan Meyer
Chair, House Ways & Means Committee
P.O. Box 2910
Austin, TX 78768

Re: HB 3389 – Tax Paid on Bad Debt

Mr. Chairman and Members of the Committee:

I write on behalf of the American Financial Services Association (“AFSA”)¹ in support of House Bill 3389, which would allow a lender or other financial institution to claim a refund of motor vehicle sales taxes paid on uncollectable and charged off accounts. Bad debt statutes, which allow merchants to claim refunds for sales tax paid in advance for financed retail transactions that are not repaid in full, are critical in preventing an additional, unfair and unwarranted tax burden on businesses. Preventing this burden benefits consumers and businesses alike by decreasing the risk of providing credit and lowering the cost of credit for borrowers.

Consumers often finance larger, more expensive retail purchases, like vehicles and other items, with retail installment loan contracts that allow them to pay off the purchase over time with monthly payments. When financing the purchase of a vehicle, the consumer is able to finance the purchases and sales taxes (due at the of purchase) by borrowing the full amount of the sales tax and paying that amount over the life of the loan. Sometimes, a customer is no longer able or willing to continue paying off their purchase. Typically, the vehicle will be returned to the finance company and sold at auction and the proceeds will be used to satisfy the unpaid debt, including any previously paid taxes. If the proceeds do not cover the remaining debt, and the finance company determines the unpaid loan amount is otherwise uncollectable, it is considered “bad debt.” When a debt becomes uncollectable, many states have statutes that provide for a refund of a pro rata share of the prepaid sales tax because the customer failed to eventually pay off the product in full. These statutes are intended to ensure that sales tax is only paid on the actual purchase price paid by the customer as opposed to the amount expected to be paid.

By allowing for the refund of uncollected sales tax paid on bad debt, HB 3389 would prevent financial institutions from facing significant losses that can be passed along to consumers. Depending on the price of the vehicle and the length of time remaining on the loan term when it becomes uncollectable, the added exposure could total thousands of dollars for a single vehicle. Vehicle finance companies lose money whenever an account become uncollectable, even in instances when the vehicle is repossessed, due to the costly act of physical repossession and the replacement of loan contracts with

¹ Founded in 1916, the American Financial Services Association (AFSA), based in Washington, D.C., is the primary trade association for the consumer credit industry, protecting access to credit and consumer choice. AFSA members provide consumers with many kinds of credit, including direct and indirect vehicle financing, traditional installment loans, mortgages, payment cards, and retail sales finance. AFSA members do not provide payday or vehicle title loans.

depreciating assets in the form of vehicles. HB 3389 would help limit these losses by providing a method for recovering the uncollected portion of the sales taxes.

Consumers are affected by the current absence of a bad debt statute Texas, as the risk borne by the lender is increased, which forces lenders to price in the additional risk in the form of higher interest rates for certain loans. The interest rate charged, by necessity, takes into account many factors, including the consumer's financing needs and the risk of default and resulting costs. Financial institutions rely on bad debt statutes to offset the risk of purchasing retail installment contracts from dealers and to mitigate losses associated with uncollectable accounts. If the state enacts a provision allowing lenders and other financial institutions to take a refund on associated sales taxes, the lower costs and risks associated with consumer default can be priced into the sales contract, potentially resulting in lower interest rates and decreased costs for Texas consumers looking to purchase a vehicle. Consumers also directly benefit from retail bad debt laws because the amount recovered by the financial institution is then credited to offset any loss. Conversely, when there is no retail bad debt law in place, consumers are liable for the entire amount of the financed sales tax paid. If HB 3389 is enacted, Texas residents—for whom ownership of a reliable vehicle is essential—will have an easier time securing credit and affording the vehicles they rely on in their daily lives and may not otherwise have been able to afford.

For these reasons, we respectfully urge you to support HB 3389. Thank you for your consideration of our comments. If you have any questions or would like to discuss this further, please do not hesitate to contact me at (202) 469-3181 or mkownacki@afsamail.org.

Sincerely,



Matthew Kownacki
Director, State Research and Policy
American Financial Services Association
919 Eighteenth Street, NW, Suite 300
Washington, DC 20006-5517

cc:
House Ways & Means Committee Members