

WAC 458-20-257 Tangible personal property warranties and service contracts. (1) **Introduction.** This rule explains the business and occupation (B&O) tax, retail sales tax, and use tax reporting responsibilities of persons selling or performing services covered by warranties, service contracts, and mixed agreements for tangible personal property. For additional information on computer software maintenance agreements see WAC 458-20-15502, Taxation of computer software.

(2) **Examples.** This rule contains examples that identify a number of facts and then state a conclusion. The examples should be used only as a general guide. The tax results of other situations must be determined after a review of all of the facts and circumstances.

(3) **Definitions.** For the purpose of this rule, the following terms will apply:

(a) **Agreement.** Unless otherwise stated, "agreement" means "service contract," "warranty," or "mixed agreement" as those terms are defined.

(b) **Insurance rider.** An insurance rider is an attachment to an insurance policy that modifies the conditions of the policy by expanding or restricting its benefits or excluding certain conditions from the coverage.

(c) **Mixed agreement.** A mixed agreement is an agreement that contains provisions of both warranty and service contracts.

(d) **Seller.** "Seller" means every person making sales to a buyer, purchaser, or consumer, whether as agent, broker, or principal.

(e) **Service contract.** A service contract, sometimes referred to as a maintenance agreement or even an extended warranty, provides for the repairing, cleaning, altering, or improving of tangible personal property, generally for the purpose of continued satisfactory operation. These services may be performed on a regular or irregular basis. Even though a service contract may be referred to by some other name, it is the coverage that determines whether the contract is a service contract or extended warranty.

(f) **Warranty.** A warranty, sometimes referred to as a guarantee, is an agreement which provides for the replacement or repair of tangible personal property at no additional charge or at a reduced charge for tangible personal property, labor, or both, or to compensate for the replacement or repair of tangible personal property, based upon the happening of some unforeseen occurrence, e.g., a component part fails and the property needs repair. Unless otherwise stated, the term warranty includes both a warranty and an extended warranty.

(4) **Sales of agreements for tangible personal property.**

(a) **Retail sales.** Income from agreements sold with or without tangible personal property to consumers is subject to the retailing B&O tax and retail sales tax, unless a specific exemption applies. Income from the sales of insurance riders to consumers is also subject to retailing B&O tax and retail sales tax. See RCW 82.04.050. Sellers of agreements and insurance riders to consumers are responsible for collecting the retail sales tax from the consumers, and remitting it and retailing B&O tax to the department of revenue (department).

If a seller is acting as agent or broker for another party, such as the actual warrantor, the seller is still liable for collecting the retail sales tax from the buyer and remitting it to the department. In this case, the seller as an agent or broker of the warrantor normally receives a commission. Commission income is taxable under the service and other business activities B&O tax classification. See subsection (5) of this rule for "Sales by third parties." The warrantor's gross income on the sale is taxable under the retailing B&O tax classifica-

tion. There is no deduction allowed for the commission paid to the agent or broker.

(b) **Wholesale sales.** Sales of agreements can be made at wholesale when the buyer will be reselling the agreement without intervening use, or including the agreement in the sale of tangible personal property, and the seller takes from the buyer a copy of the buyer's reseller permit. The reseller permit documents the wholesale nature of any sale as provided in WAC 458-20-102, Reseller permits. (Reseller permits replaced resale certificates effective January 1, 2010.)

Example 1. An automobile dealer sells a vehicle to a customer for a selling price of \$20,000 that includes a manufacturer's limited five years or 50,000 miles warranty. The automobile dealer extends coverage for an additional two years, as a bonus to the customer. When the automobile dealer purchases the two-year agreement from a warranty provider, with the intent to sell the agreement along with the sale of the vehicle to the customer, the purchase of the extended warranty by the automobile dealer is for resale.

(i) **Example 2.** A home improvement store (store) sells a lawnmower to a customer. The store also makes available for purchase a manufacturer's agreement for extended coverage. The customer decides to purchase an agreement from the store for the lawnmower. As the store is reselling the agreement, the store may purchase it at wholesale from the manufacturer with the use of a reseller permit. Both the sales of the lawnmower and agreement to the customer are taxable retail sales. The store will collect the retail sales tax from the customer, and remit it along with retailing B&O tax to the department.

(ii) **Example 3.** For a special holiday sale, the home improvement store in Example 2 purchases the manufacturer's extended warranties to provide with the sales of lawnmowers. The store makes no intervening use of the extended warranties, and does not charge customers for the warranties. The warranty purchases by the store are wholesale purchases as long as the store provides a copy of its reseller permit to the manufacturer. The store is not the consumer of the warranties as the warranties are provided to customers as a condition of purchase of the lawnmowers. The store will collect retail sales tax, from the customers on the sales of the lawnmowers, and remit it along with retailing B&O tax to the department.

(c) **Agreement purchases from a third party.** When an agreement is purchased by a manufacturer, wholesaler, or retailer to be included in the sale of tangible personal property, the purchase of the agreement can be made at wholesale with the use of a reseller permit. In this instance, the manufacturer, wholesaler, or retailer is not the consumer of the warranty. When the retailer sells the tangible personal property including the agreement, it will collect the retail sales tax from the customer and remit it and the retailing B&O tax to the department.

Example 4. If a vehicle wholesaler sells a vehicle to a retailer and includes an agreement with the sale, the sale of the vehicle with agreement is a wholesale sale. RCW 82.04.050. The retailer must provide the wholesaler with a reseller permit.

(d) **Deferred sales or use tax due.** If a manufacturer, wholesaler, or retailer purchases an agreement, without knowing whether it will be sold or given as an incentive with the sale of tangible personal property, the agreement can be purchased at wholesale with the use of a reseller permit. If there is intervening use of the agreement by the manufacturer, wholesaler, or retailer, deferred sales or use tax will be due.

(e) **Additional charges for parts or repair services covered under an agreement.** In some cases, a customer is required to pay an amount for services or parts not fully covered under an agreement. This additional amount is subject to both the retailing B&O tax and retail sales tax, unless an exemption applies.

Example 5. The automobile dealer in Example 1 sells a vehicle to a customer for a selling price of \$20,000 that includes a manufacturer's limited five-year or 50,000 miles warranty. The dealer also sells its own extended warranty to the customer for \$200. The dealer insures itself with an insurance carrier, and under the policy claims are paid on the retail value of the repairs. The customer has the dealer complete \$500 of repairs under the warranty. The customer pays the dealer a reduced charge of \$100 for the warranty services and the dealer receives \$400 from its insurance carrier. In completing the repair, the dealer installed parts from its inventory which had a cost to the dealer of \$150 and subcontracted part of the repair to an electrical shop which charged the dealer \$200. The tax liability to the dealer and subcontractor is as follows:

(i) In addition to retail sales tax collected from the customer on the \$20,000 selling price, retail sales tax must be collected on the \$200 selling price for the dealer's own extended warranty.

(ii) The \$20,000 selling price for both the automobile and warranty is reported under the retailing B&O tax and retail sales tax classifications on the excise tax return. The \$20,000 paid for the automobile (but not the cost of the warranty) is also subject to the motor vehicle sales excise tax.

(iii) The \$100 charge paid by the customer for the warranty services performed is subject to the retailing B&O tax, and the dealer must collect retail sales tax from the customer.

(iv) The \$400 received by the dealer from the insurance company is a nontaxable insurance claim reimbursement.

(v) The \$150 cost of the parts taken from inventory is not subject to use tax.

(vi) The subcontractor is making a \$200 wholesale sale to the dealer, if the dealer provides the subcontractor with a copy of its reseller permit.

(f) **Exemptions.** The sale of an agreement by a retailer is not exempt simply because the sale of the tangible personal property to which it applies is exempt. Generally, for the sale of the agreement to be exempt, there must be a provision in statute exempting all services or products covered by the agreement. If all such obligations are not exempt, the sale of the agreement to the consumer is subject to retail sales tax. See RCW 82.08.190 and 82.08.195 for additional information regarding the taxation of bundled transactions.

(i) **Service contracts.** Since a service contract is a contract for the repairing, cleaning, altering, or improving of the tangible personal property covered by the contract, the sale of a service contract by the retailer may be exempt from retail sales tax if there is a statutory exemption for all activities covered by the contract.

(A) **Example 6.** RCW 82.08.955 provides a retail sales tax exemption for both the sales and repair of machinery and equipment used directly for retail sales of a biodiesel blend or E85 motor fuel. Company A sells machinery that qualifies for exemption under RCW 82.08.955 to Dealer BF. The purchase price of the machinery is \$10,000 and includes a ninety-day warranty against defects in material and workmanship. Dealer BF also purchases a service contract for an additional \$300 that covers the repairing and cleaning of qualified parts. If

Dealer BF provides Company A with an exemption certificate, the \$10,000 selling price and \$300 service contract price are exempt from retail sales tax. Company A reports the total \$10,300 under the retailing B&O tax and retail sales tax classifications, taking a deduction under retail sales tax for the exemption.

(B) **Example 7.** RCW 82.08.809 provides an exemption for the purchase of vehicles using clean alternative fuels provided the provisions of the exemption are followed. A dealer sells a new vehicle powered by natural gas for \$30,000 and a \$500 two-year service contract to a customer. The sale of the vehicle is exempt from retail sales tax, but the sale of the service contract is subject to retail sales tax as there is no statutory exemption for the repair activities covered by the service contract.

(ii) **Warranties.** The sale of a warranty by a retailer is exempt only if a specific statutory exemption is available. The place of sale for a warranty is the seller's business location if the buyer receives the warranty at that location. See RCW 82.32.730 and WAC 458-20-145, Local sales and use tax for additional sourcing information. See WAC 458-20-15502 for computer software warranties.

Warranties purchased and received outside of Washington are subject to use tax when put to use in Washington. See RCW 82.12.020.

Example 8. Assume that Dealer BF in Example 6 also purchases an extended warranty for an additional \$200. If Dealer BF provides Company A with a valid exemption certificate, the \$10,000 selling price and \$300 service contract are exempt from retail sales tax, but the \$200 for the extended warranty is subject to retail sales tax. RCW 82.08.955 does not provide for an exemption for a warranty for eligible equipment. As there is no corresponding tax exemption for B&O tax, Company A will pay retailing B&O tax to the department on the total amount of \$10,500 along with remitting the retail sales tax collected from Dealer BF.

(iii) **Mixed agreements.** The sale to a consumer of a mixed agreement for tangible personal property, which by definition contains provisions of both a warranty and a service contract, is a "bundled transaction." Retail sales tax must generally be collected from the consumer on the selling price of a mixed agreement, unless both the warranty provisions and service contract provisions each separately qualify for a retail sales tax exemption. Refer to RCW 82.08.190 and 82.08.195 for additional guidance on how retail sales tax applies to bundled transactions.

(5) **Sales by third parties.** Consideration received by a third party as a commission, for selling an agreement for the actual warrantor, is generally subject to tax under the service and other activities tax classification. In this situation, the third-party seller never takes possession of the agreement, and the warrantor maintains liability for the provisions of the agreement.

(a) **Responsibility for payment of retailing B&O tax.** The warrantor is subject to retailing B&O tax on the gross sales price received from the sales of agreements by third parties. No deduction is allowed for commissions paid to third parties.

(b) **Responsibility for collection of retail sales tax.** The third party is responsible for collecting the retail sales tax from the buyer and remitting it, along with service and other activities B&O tax on its commission income, to the department. If the seller of the agreement is licensed under chapter 48.17 RCW with respect to this selling activity, the seller owes tax on commissions under the insurance producers B&O tax classification.

(6) **Sales of repair services or parts to obligor.** A person obligated under an agreement, including any third-party obligor under an agreement sold to a retailer and provided at no additional charge to the end consumer, may purchase the following from a supplier or service provider at wholesale without incurring retail sales tax, provided the obligor provides the supplier or service provider with a reseller permit:

- Parts purchased to replace or become an ingredient or component of tangible personal property covered by the agreement, as long as there is no intervening use of the parts as a consumer; and
- Repair services purchased to satisfy the obligor's obligations under an agreement.

The supplier or service provider is taxable under the wholesaling B&O tax classification on the value of the parts and labor provided.

(7) **Warranties with insurance elements.** There are tangible personal property agreements that include elements of insurance (i.e., theft, loss) and elements of warranty (operational failure, damage). Income from sales to consumers of agreements defined as a warranty, service contract or maintenance agreement, that are not otherwise insurance contracts where tax has been paid under Title 48 RCW insurance premiums tax, is subject to retailing B&O tax and retail sales tax. See RCW 48.14.080. If a bundled transaction includes both taxable and nontaxable plans, retailing B&O and retail sales taxes are due on the income. For more information on bundled transactions see RCW 82.08.190 and 82.08.195.

(8) **Commonly asked questions.**

(a) **Is it a warranty or service contract when a credit card company replaces lost or damaged items purchased by one of their credit card holders?** The credit card company (company) covering the purchased items would be providing an insurance product, but the company may not be charging the card holders for the benefit of having lost or damaged items replaced at no charge and if not, the company would not owe premiums tax, but owe B&O tax on income. When the company replaces items, the company is responsible for paying sales tax on the items purchased and provided as replacements.

(b) **Is identity theft protection considered a warranty?** Identity theft protection is not tangible personal property. The protection plan may be a combination of products including monitoring a person's accounts. It depends on the coverage as to whether the protection plan is an insurance product that is subject to the premiums tax.

(c) **Are agreements that cover accidentally dropping a phone in water an insurance product?** Most agreements are service contracts and not insurance products, and are covered under chapter 48.110 RCW, Service contracts and protection product guarantees.

(d) **If a loaner piece of equipment is included in the cost of a warranty, does the customer using the loaner owe use tax on the loaned piece of equipment?** If the loan of the equipment is included in the warranty, the customer does not owe use tax on the use of the loaned equipment.

[Statutory Authority: RCW 82.32.300, 82.01.060(2), and chapters 82.08 and 82.12 RCW. WSR 15-09-005, § 458-20-257, filed 4/2/15, effective 5/3/15. Statutory Authority: RCW 82.32.300. WSR 90-10-081, § 458-20-257, filed 5/2/90, effective 6/2/90.]