



PREPROPOSAL STATEMENT OF INQUIRY

CR-101 (June 2004)
(Implements RCW 34.05.310)
Do NOT use for expedited rule making

Agency: Department of Revenue

Subject of possible rule making: WAC 458-20-257 (Rule 257) *Warranties and maintenance agreements.*

Statutes authorizing the agency to adopt rules on this subject:
RCW 82.32.300 and 82.01.060(2)

Reasons why rules on this subject may be needed and what they might accomplish:
Rule 257 explains the business and occupation (B&O), retail sales, and use tax reporting responsibilities of persons:

- Selling warranties and maintenance agreements for tangible personal property; and
- Performing services covered by such a warranty or maintenance agreement.

The Department is considering an amendment to Rule 257 to:

- Update the rule to recognize that the sale of an extended warranty is a retail sale;
- Reformat the rule to provide the information in a more useful manner.

Identify other federal and state agencies that regulate this subject and the process coordinating the rule with these agencies: None

Process for developing new rule (check all that apply):

- Negotiated rule making
- Pilot rule making
- Agency study
- Other (describe) Parties interested in this rule making may contact the individual listed below. The public may also participate by providing written comments throughout this rule making or giving oral testimony at the public meeting or public hearing.

How interested parties can participate in the decision to adopt the new rule and formulation of the proposed rule before publication:
A preliminary draft of possible rule changes is available via the Department's online [Rules Agenda](#).
Written comments may be submitted by mail and should be directed to Gayle Carlson at either of the following addresses:
email: GayleC@dor.wa.gov, or mailing address: Gayle Carlson, ITA Division, PO Box 47453, Olympia, WA 98504-7453.
Written and oral comments will be accepted at the public meeting.

Public meeting location:
Capitol Plaza Building
4th Floor Conference Rm Lg
1025 Union Avenue SE
Olympia, Washington

Assistance for persons with disabilities:
Contact Mary Carol LaPalm (360) 725-7499 or Renee Cosare (360) 725-7514 no later than 10 days before the meeting date.
For Hearing Impaired please contact us via the Washington Relay Operator at (800) 833-6384.

Date: April 17, 2012 **Time:** 10:00 A.M.

Date March 6, 2012
Name Alan R. Lynn
Signature
Title Rules Coordinator

CODE REVISER USE ONLY
OFFICE OF THE CODE REVISER STATE OF WASHINGTON FILED
DATE: March 06, 2012
TIME: 2:10 PM
WSR 12-06-072

This draft is provided for discussion purposes only to determine what topics a possible proposed rule might address. This discussion draft is under no circumstances to be used to determine a tax liability and/or eligibility for tax exemptions.

AMENDATORY SECTION (Amending WSR 90-10-081, filed 5/2/90, effective 6/2/90)

WAC 458-20-257 Warranties and maintenance agreements.

~~((1) **Definitions.** For the purposes of this section, the following terms will apply:~~

~~(a) **Warranties.** Warranties, sometimes referred to as guarantees, are agreements which call for the replacement or repair of tangible personal property with no additional charge for parts or labor, or both, based upon the happening of some unforeseen occurrence, e.g., the property needs repair within the warranty period.~~

~~(b) **Warrantor.** The warrantor is the person obligated, as specified in the warranty agreement, to perform labor and/or provide materials to the owner of the personal property to which the warranty agreement relates.~~

~~(c) **Maintenance agreements.** Maintenance agreements sometimes referred to as service contracts, are agreements which require the specific performance of repairing, cleaning, altering, or improving of tangible personal property on a regular or irregular basis to ensure its continued satisfactory operation.~~

~~(2) **B&O tax.**~~

~~(a) Manufacturer's warranties included in the retail selling price of the article being sold.~~

~~(i) When a manufacturer's warranty is included in the retail selling price of the property sold and no additional charge is made, the value of the warranty is a part of the selling price. The value of the warranty is included in the "gross proceeds of sale" of the article sold and reported under the appropriate classification, e.g. retailing, wholesaling, etc.~~

~~(ii) When a repair is made by the manufacturer-warrantor under the warranty, the value of the labor and or parts provided are not subject to B&O tax.~~

~~(iii) When a person other than the manufacturer-warrantor makes a repair for the manufacturer-warrantor, the person making the repair is making a wholesale sale of the repair service to the manufacturer-warrantor. The person doing the repair is B&O taxable under the wholesaling classification on the value of the parts and labor provided.~~

~~(b) Nonmanufacturer's warranties and manufacturer's warranties not included in the retail selling price of the article being sold.~~

~~(i) When a warranty is sold for a charge separate from the charge of the product, e.g., a warranty extending the manufacturer's warranty, the charge is reported in the service and other activities classification of the B&O tax.~~

~~(ii) When a repair is made by the warrantor under a separately stated warranty, the value of the labor and or parts~~

~~provided are not subject to B&O tax.~~

~~(iii) When a person other than the warrantor makes a repair for the warrantor, the person making the repair is making a retail sale of the repair service to the warrantor. The person making the repair is B&O taxable under the retailing classification.~~

~~(c) Maintenance agreements.~~

~~(i) Maintenance agreements (service contracts) require the periodic specific performance of inspecting, cleaning, physical servicing, altering, and/or improving of tangible personal property. Charges for maintenance agreements are retail sales, subject to retailing B&O tax and retail sales tax under all circumstances.~~

~~(d) Amounts received as a commission or other consideration for selling a warranty or maintenance agreement of a third party warrantor or provider are generally subject to B&O tax under the service and other activities classification. However, if the seller of the warranty is licensed under chapter 48.17 RCW with respect to this selling activity, the commission is subject to B&O tax under the insurance agent classification.~~

~~(e) In the event a warrantor purchases an insurance policy to cover the warranty, amounts received by the warrantor under the insurance policy are insurance claim reimbursements not subject to B&O tax.~~

~~(3) **Retail sales tax.**~~

~~(a) Manufacturer's warranties included in the retail selling price of the article being sold.~~

~~(i) When a manufacturer's warranty is included in the retail selling price of the property sold and no additional or separate charge is made, the value of the warranty is a part of the selling price and retail sales tax applies to the entire selling price of the article being sold.~~

~~(ii) When a repair is made by the manufacturer-warrantor under the warranty, the repair performed is not a retail sale and no retail sales tax is collected.~~

~~(iii) When a person other than the manufacturer-warrantor makes a repair for the manufacturer-warrantor, the person making the repair is making a wholesale sale of the repair service to the manufacturer-warrantor. No retail sales tax is collected from the manufacturer-warrantor.~~

~~(b) Nonmanufacturer's warranties and manufacturer's warranties not included in the retail selling price of the article being sold.~~

~~(i) When a warranty is sold for a charge separate from the charge of the product, e.g., a warranty extending the manufacturer's warranty, the sale is not a retail sale and no retail sales tax is collected on the amount charged.~~

~~(ii) When a repair is made by the warrantor under its own separately stated warranty, the value of the labor and/or parts provided is not a retail sale and no retail sales tax is collected.~~

~~(iii) When a person other than the warrantor makes a repair for the warrantor, the person making the repair is making a retail sale of the repair service to the warrantor. Retail~~

~~sales tax is collected from the warrantor measured by the labor and materials provided.~~

~~(c) Maintenance agreements are sales at retail and subject to retail sales tax under all circumstances.~~

~~(i) Parties subcontracting to the party selling the maintenance agreement are making sales at wholesale, and are required to take from their customer (maintenance seller) a resale certificate as provided in WAC 458-20-102.~~

~~(4) USE TAX.~~

~~(a) Manufacturer's warranties included in the retail selling price of the article being sold.~~

~~(i) When a manufacturer warrantor makes repairs required under its warranty, the value of the parts used in making the repairs is not subject to use tax.~~

~~(ii) Where a third party makes repairs for a manufacturer-warrantor, the transaction is a wholesale sale and the parts used in the repair are not subject to use tax.~~

~~(b) Nonmanufacturer's warranties and manufacturer's warranties not included in the retail selling price of the article being sold.~~

~~(i) When a repair is made by the warrantor under a separately stated warranty, the warrantor is the consumer of the parts and the parts are subject to use tax measured by the warrantor's cost.~~

~~(ii) When a person other than the warrantor makes a repair for the warrantor, the person making the repair is making a retail sale to the warrantor. Retail sales tax, not use tax, is~~

collected.

~~(c) Maintenance agreements.~~

~~(i) Persons performing services under the requirements of maintenance agreements sold by them, are not subject to use tax or retail sales tax on materials which become a part of the required repairs or services.~~

~~(5) **Additional service — deductible.** In the event services are provided in addition to any warranty or maintenance agreement, such services are separately taxable as retail sales, subject to retail sales tax and retailing B&O tax. This includes so-called "deductible" amounts not covered by a warranty or maintenance agreement.~~

~~(6) **Mixed agreements.** If an agreement contains warranty provisions but also requires the actual specific performance of inspection, cleaning, servicing, altering, or improving the property on a regular or irregular basis, without regard to the operating condition of the property, such agreements are fully taxable as maintenance agreements, not warranties.~~

~~(7) **Examples:**~~

~~(a) An automobile dealer sells a vehicle to a customer for selling price of \$15,000 cash and the selling price includes a manufacturer's limited warranty for 5 years or 50,000 miles. The owner of the vehicle has \$600 (\$200 parts and \$400 labor) warranty work, paying no deductible, performed by the dealer who is not the manufacturer-warrantor. The tax liability of the dealer is as follows:~~

~~(i) Retail sales tax is collected on the \$15,000 selling~~

price.

~~(ii) The \$15,000 selling price is reported under the retailing B&O tax classification. The \$600 repair is reported under the wholesaling B&O tax classification.~~

~~(iii) The \$200 of parts used in the repair are not subject to use tax.~~

~~(b) The automobile dealer in example (a) 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. In addition to the repairs in example (a), the customer has the dealer complete \$500 of repairs under the dealer's extended warranty. The customer paid the \$100 deductible and the dealer received \$400 from his 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 the subcontractor are as follows:~~

~~(i) The dealer reports the \$200 sale of the warranty under the service and other activities classification of B&O tax. No retail sales tax is collected on the sale.~~

~~(ii) The \$100 deductible received by the dealer is a retail sale subject to retail sales tax and retailing B&O tax.~~

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

~~(iv) The dealer is the consumer of the parts removed from its inventory and used in the repair. The \$150 dealer cost of~~

~~the parts taken from inventory is subject to use tax.~~

~~(v) The subcontractor is making a retail sale to the dealer subject to retail sales tax and retailing B&O.)) (1)~~

Introduction. This rule explains the business and occupation (B&O), retail sales, and use tax reporting responsibilities of persons selling or performing services covered by warranties, service contracts, and mixed agreements that cover tangible personal property.

This rule contains examples which 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.

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

(a) **Agreement.** Unless otherwise stated, "agreement" means "service contract," "warranty," or "mixed agreement."

(b) **Warranty.** A warranty, sometimes referred to as a guarantee, provides for the replacement or repair of tangible personal property with no additional charge for parts or repair services, 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.

(c) **Service contract.** A service contract, sometimes referred to as a maintenance agreement, 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.

(d) **Mixed agreement.** A mixed agreement contains properties of both a warranty and a service contract.

(3) **Sales of agreements.** Sales of agreements to consumers are subject to the retailing B&O and retail sales taxes, unless a specific exemption applies. Sales of extended warranties, when not to end-consumers, can be wholesale sales under RCW 82.04.060 (1)(f).

(a) **Sale of a product, which includes an agreement at no separate charge.** The sales price of a product often includes, for no extra charge, warranty coverage for a specific period of time. This type of warranty is commonly referred to as a "manufacturer's warranty." Some sellers may extend the warranty period for no extra charge. Where there is no separate charge for the sale of an agreement, the sale is considered a sale of the product only, and the entire sales price is taxed accordingly (e.g., retail, wholesale, or tax-exempt).

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 warranty coverage for an additional two years, with no separate charge to the customer. The dealer must collect retail sales tax on the \$20,000 selling price and must report \$20,000 under the retailing B&O tax classification.

(b) **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.

Example 2. The automobile dealer in Example 1 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 a reduced charge of \$100 for the warranty services and the dealer received \$400 from his 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 on the \$20,000 selling price, retail sales tax is collected on the \$200 paid for the dealer's own extended warranty.

(ii) The \$20,200 selling price for both the automobile and warranty is reported under the retailing B&O tax classification.

(iii) The \$100 reduced charge paid 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 wholesale sale to the dealer.

(c) Exemptions. The sale of an agreement is not exempt simply because the sale of the property to which it applies is exempt.

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

Example 3. RCW 82.08.02565, known as the "M&E exemption," provides a retail sales tax exemption for both the sale and repair of eligible manufacturing machinery and equipment. Company A sells equipment that qualifies for the M&E exemption to Manufacturer B. The purchase price of the equipment is \$10,000 and includes a 90-day warranty against defects in materials and workmanship. Manufacturer B also purchases a service contract for an additional \$300. If Manufacturer B provides Company A with a valid M&E exemption certificate, the \$10,000 selling price and \$300 service contract are exempt from retail sales tax. The 90-day warranty included in the selling price is not subject to additional tax. Company A reports the total \$10,300 under the retailing B&O tax classification.

(ii) Warranties. The sale of a warranty 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 for additional sourcing information.

Example 4. Assume that Manufacturer B in Example 3 also purchases an extended warranty for an additional \$200. If Manufacturer B provides Company A with a valid M&E 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 82.08.02565 exempts sales tax on repairs of eligible equipment, but does not provide for an exemption for a warranty for eligible equipment. As there is no corresponding tax exemption for B&O tax, the total amount of \$10,500 is subject to the retailing B&O tax.

(4) **Sales of agreements by third parties.** Consideration received by a third party as a commission, for selling an agreement for the actual warrantor, is subject to B&O tax under the service and other activities B&O tax classification.

(5) **Sales of repair services or parts to obligor.** A person obligated under an agreement may purchase the following from a supplier or service provider at wholesale, provided that the obligor provides the supplier or service provider with a reseller permit (reseller permits replaced resale certificates effective January 1, 2010):

 Parts purchased to replace or become an ingredient or component of 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.

Sales of the above are subject to wholesaling B&O tax, provided the obligor provides the supplier or service provider with a reseller permit.

[Statutory Authority: RCW 82.32.300. 90-10-081, § 458-20-257, filed 5/2/90, effective 6/2/90.]