



# PROPOSED RULE MAKING

## CR-102 (June 2004)

(Implements RCW 34.05.320)

Do NOT use for expedited rule making

**Agency:** Department of Revenue

- Preproposal Statement of Inquiry was filed as WSR 12-06-072 ; or
- Expedited Rule Making--Proposed notice was filed as WSR ; or
- Proposal is exempt under RCW 34.05.310(4).

- Original Notice
- Supplemental Notice to WSR
- Continuance of WSR

**Title of rule and other identifying information:** WAC 458-20-257 (Rule 257) *Warranties and maintenance agreements service contracts.*

**Hearing location(s):**

Capitol Plaza Building  
4<sup>th</sup> Floor L&P Conference Room  
1025 Union Avenue SE  
Olympia, Washington 98504

Copies of draft rules are available for viewing and printing on our website at [Rules Agenda](#)

**Date:** January 3, 2013 **Time:** 10 a.m.

**Date of intended adoption:** January 10, 2013

**Submit written comments to:**

Name: Gayle Carlson  
E-mail: GayleC@dor.wa.gov  
Address: Post Office Box 47453  
Olympia, Washington 98504-7453

By: January 3, 2013

**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 hearing date. For Hearing impaired please contact us via the Washington Relay Operator at (800) 833-6384.

**Purpose of the proposal and its anticipated effects, including any changes in existing rules:**

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 proposing an amendment to Rule 257 to:

- Update the rule to recognize that the sale of an extended warranty is a retail sale;
- Explain that the sale of a mixed agreement (an agreement containing provisions of both a warranty and service contract), is a bundled transaction; and
- Reformat the rule to provide the information in a more useful manner.

**Reasons supporting proposal:** To update the rule to recognize current law.

**Statutory authority for adoption:**

RCW 82.32.300 and 82.01.060(2)

**Statute being implemented:**

RCW 82.04.050 and 82.08.010

**Is rule necessary because of a:**

- Federal Law?  Yes  No
- Federal Court Decision?  Yes  No
- State Court Decision?  Yes  No

If yes, CITATION:

**CODE REVISER USE ONLY**

OFFICE OF THE CODE REVISER  
STATE OF WASHINGTON  
FILED

**DATE: November 16, 2012**

**TIME: 1:52 PM**

**WSR 12-23-051**

**Date**  
November 16, 2012

**Name** Alan R. Lynn

**Signature**

**Title** Rules Coordinator

**Agency comments or recommendations, if any, as to statutory language, implementation, enforcement, and fiscal matters:**

None.

**Name of proponent:** Department of Revenue

- Private
- Public
- Governmental

**Name of agency personnel responsible for:**

Name	Office Location	Phone
Drafting..... Gayle Carlson	1025 Union Ave. SE. Ste #544, Olympia ,WA	(360) 534-1576
Implementation.... Alan R. Lynn	1025 Union Ave. SE. Ste #544, Olympia ,WA	(360) 534-1599
Enforcement..... Russ Brubaker	1025 Union Ave. SE. Ste #544, Olympia ,WA	(360) 534-1505

**Has a small business economic impact statement been prepared under chapter 19.85 RCW?**

Yes. Attach copy of small business economic impact statement.

A copy of the statement may be obtained by contacting:

Name:  
Address:

Phone:  
E-mail:

No. Explain why no statement was prepared.

This rule does not impose any new performance requirement or administrative burden on any small business not already required by statute.

**Is a cost-benefit analysis required under RCW 34.05.328?**

Yes A preliminary cost-benefit analysis may be obtained by contacting:

Name:  
Address:

Phone:  
E-mail:

No: Please explain:

This is not a significant legislative rule as defined in RCW 34.05.328.

THIS PROPOSED RULE IS SUBMITTED FOR PUBLIC COMMENTS AFTER INPUT FROM INTERESTED PARTIES AND IS TO BE USED SOLELY FOR DISCUSSION PURPOSES AT THE PUBLIC HEARING ON THE PROPOSED RULE. UNDER NO CIRCUMSTANCES IS THIS PROPOSED RULE TO BE USED TO DETERMINE TAX LIABILITY AND OR EXEMPTIONS.

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

**WAC 458-20-257 Warranties and ((maintenance agreements)) service contracts.** ((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.~~

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~~(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~~

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~~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.~~

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~~(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.~~

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~~(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 does not pertain to similar types of agreements for real 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" as those terms are defined in this rule.

(b) Warranty. A warranty, sometimes referred to as a guarantee, means an agreement for a specified duration to perform the replacement or repair of tangible personal property at no additional charge or a reduced charge for tangible personal property, labor, or both 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 is an agreement that contains provisions of both warranty and service contracts.

(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. Persons making sales of agreements to persons who will be reselling the agreements, without intervening use, are subject to the wholesaling B&O tax

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classification. Sellers must obtain reseller permits from their customers to document the wholesale nature of any sale as provided in WAC 458-20-102 (Reseller permits).

**(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 from the customer, and report \$20,000 in sales under the retailing B&O tax and retail sales tax classifications on the excise tax return.

**(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 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 excise tax.

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(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. 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 is subject to retail sales tax. See also 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 may be exempt from retail sales tax if there is a statutory exemption for all activities covered by the contract.

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 that covers only exempt parts and repairs. If Manufacturer B provides Company A with a valid M&E exemption certificate, the \$10,000 selling price and \$300 service contract price are exempt from retail sales tax. The service contract is exempt as RCW 82.08.02565 includes an exemption for the sales of or charges made for labor and services rendered in respect to installing, repairing, cleaning, altering, or improving the machinery and equipment. 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 and retail sales tax classifications, taking a deduction under retail sales tax for the M&E exemption.

Example 4. 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 and a two-year service contract

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to a customer. The sale of the vehicle is exempt from retail sales tax, but the sale of the service contract is not as there is no statutory exemption for the activities covered by the service contract.

(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 5. 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.

(iii) **Mixed agreements.** The sale of a mixed agreement, which by definition contains provisions of both a warranty and a service contract, is a "bundled transaction." Retail sales tax must generally be collected 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.

(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.

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