

Cite as Det. No. 99-056, 19 WTD 54 (2000)

BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

In the Matter of the Petition For Refund of)	<u>D E T E R M I N A T I O N</u>
)	
)	No. 99-056
)	
...)	Registration No. . . .
)	FY. . . /Audit No. . . .
)	

- [1] RULE 257: RETAILING B&O TAX – RETAIL SALES TAX – PERSONAL COMPUTERS – EXTENDED WARRANTY REPAIRS. When a person other than the warrantor makes a repair for the warrantor under an extended warranty not included in the retail selling price of the article, that person is making a retail sale of the repair service to the warrantor. The person making the repair must collect retail sales tax from the warrantor as measured by the labor and materials provided. That person must also report its gross income from making such repairs under the retailing B&O tax classification.

- [2] RCW 82.08.0273; ETA 316: RETAIL SALES TAX – EXEMPTION – SALES OF TANGIBLE PERSONAL PROPERTY TO NONRESIDENTS. Retail vendors of tangible personal property in Washington are permitted not to collect sales tax from certain nonresidents of Washington providing the vendors maintain proper records for each nontaxable sale that show the type of proof of identification the vendors accepted from their nonresident customers.

- [3] RETAIL SALES TAX – B&O TAX – ESTOPPEL – PRIOR AUDIT. The Department is not estopped from assessing taxes on warranty repair income because it did not assess such taxes in a prior audit due to oversight, inadvertence, neglect, etc.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

NATURE OF ACTION:

A corporation (the taxpayer) protests the assessment of business and occupation (B&O) tax and retail sales tax on sales of personal computers and warranty repairs it made on computers.¹

FACTS:

De Luca, A.L.J. – The taxpayer operates a retail store in Washington where it sells personal computers. The taxpayer has an agreement with [a computer manufacturer] to repair and service personal computers sold under the manufacturer's warranties and extended warranties. The Department of Revenue (the Department) reviewed the taxpayer's books and records for the period January 1, 1994 through June 30, 1997 and assessed \$. . . in taxes and interest. See Document No. FY. . . /Audit No. . . . The taxpayer and the Department's Audit Division agreed upon a test period of January 1, 1996 through December 31, 1996 to sample the warranty repair service income. The Audit Division noted that the taxpayer's records were not sufficient for the Audit Division to determine whether the warranty repairs were made under the manufacturer's warranties or extended warranties. Therefore, the Audit Division estimated that 90% of the repair services were made under the manufacturer's warranties and 10% were made under the extended warranties. Accordingly, the Audit Division determined that 90% of the warranty repair income was subject to wholesaling B&O tax and 10% of the warranty repair income was subject to retailing B&O tax and retail sales tax.

Additionally, the Audit Division assessed retail sales tax when it disallowed exemptions taken by the taxpayer for sales of tangible personal property to certain nonresidents of Washington. In some instances, the Audit Division found that the taxpayer did not have in its records the documents necessary to qualify the sales for the exemptions. In other cases, the taxpayer made sales to residents of non-qualifying states or provinces of Canada.

TAXPAYER'S EXCEPTIONS:

The taxpayer protests the entire assessment. It protests the B&O taxes and sales tax assessed on the warranty repair income because it claims to be a registered agent of [the computer manufacturer] and not just a third party making repairs. The taxpayer also objects to the disallowance of the nonresident exemption. Finally, the taxpayer states the Department audited it three years ago, and the Department did not question how the taxpayer treated the warranty repair income. Its business operations have not changed since then.

ISSUES:

1. Is the B&O tax and retail sales tax due on the warranty repair income?
2. Did the Department properly deny the retail sales tax exemptions taken by the taxpayer for sales of tangible personal property made to certain nonresidents?

¹ Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

3. Is the Department estopped from assessing the taxes on the warranty repair income because the taxpayer claims the Department did not assess taxes on such income in a prior audit?

DISCUSSION:

The taxpayer is registered to do business in this state. RCW 82.04.220 provides

Business and occupation tax imposed. There is levied and shall be collected from every person a tax for the act or privilege of engaging in business activities. Such tax shall be measured by the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be.

Consequently, the taxpayer owes B&O tax on its gross proceeds of sales because it is in business in this state. It does not matter if the taxpayer is operating as a registered agent of [the computer manufacturer] or as an unaffiliated repair shop. There is no tax exemption for “registered agents.”

The Audit Division determined that 90% of the taxpayer’s warranty repair income is subject to wholesaling B&O tax and 10% of that income was subject to retailing B&O tax and retail sales tax. The Audit Division made this decision based on a review of the taxpayer’s records in light of WAC 458-20-257 (Rule 257). Rule 257 is the Department’s rule that pertains to warranties and maintenance agreements. The rule is clear how the taxpayer should report its income from repairs to tangible personal property that is covered by manufacturer’s warranties and extended warranties.

For manufacturer’s warranties, Rule 257 provides:

(2) B&O TAX.

...

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

...

(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.

For extended warranties, Rule 257(2) provides:

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

...

(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.

Rule 257 also provides for the collection of retail sales tax for extended warranty repairs by third parties such as the taxpayer:

(3) RETAIL SALES TAX.

...

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

...

(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.

Thus, the Audit Division properly assessed the taxpayer's warranty repair income.

The next issue is the disallowance of the sales tax exemptions taken by the taxpayer for sales to certain nonresidents of Washington. RCW 82.08.0273 provides in pertinent part:

(1) The tax levied by RCW 82.08.020 shall not apply to sales to nonresidents of this state of tangible personal property for use outside this state when the purchaser (a) is a bona fide resident of a state or possession or Province of Canada other than the state of Washington and such state, possession, or Province of Canada does not impose a retail sales tax or use tax of three percent or more or, if imposing such a tax, permits Washington residents exemption from otherwise taxable sales by reason of their residence, and (b) agrees, when requested, to grant the department of revenue access to such records and other forms of verification at his or her place of residence to assure that such purchases are not first used substantially in the state of Washington.

(2)(a) Any person claiming exemption from retail sales tax under the provisions of this section must display proof of his or her current nonresident status as herein provided.

(b) Acceptable proof of a nonresident person's status shall include one piece of identification such as a valid driver's license from the jurisdiction in which the out-of-state residency is claimed or a valid identification card which has a photograph of the

holder and is issued by the out-of-state jurisdiction. Identification under this subsection (2)(b) must show the holder's residential address and have as one of its legal purposes the establishment of residency in that out-of-state jurisdiction.

(3) Nothing in this section requires the vendor to make tax exempt retail sales to nonresidents. A vendor may choose to make sales to nonresidents, collect the sales tax, and remit the amount of sales tax collected to the state as otherwise provided by law. If the vendor chooses to make a sale to a nonresident without collecting the sales tax, the vendor shall, in good faith, examine the proof of nonresidence, determine whether the proof is acceptable under subsection (2)(b) of this section, and maintain records for each nontaxable sale which shall show the type of proof accepted, including any identification numbers where appropriate, and the expiration date, if any.

...

(4) (b) Any vendor who makes sales without collecting the tax to a person who does not hold valid identification establishing out-of-state residency, and any vendor who fails to maintain records of sales to nonresidents as provided in this section, shall be personally liable for the amount of tax due.

The Audit Division denied the exemption in RCW 82.08.0273 for some of the taxpayer's sales to nonresidents because the taxpayer did not meet the requirements of subsection (3). The taxpayer failed to maintain records that showed either the type of proof the taxpayer accepted or the necessary information contained in the proof of nonresidence. For example, the statute suggests that the proof could include driver's licenses with identification numbers and expiration dates. In other instances, the taxpayer made sales to residents of states that do not qualify for the exemption under the statute, such as the sale to a Massachusetts resident. Excise Tax Advisory 316.08.193 lists the states, possessions, and Canadian provinces that qualify for the exemption. They are, as of July 1, 1993:

Alaska	Oregon	Montana
Delaware	New Hampshire	Virgin Islands
Guam	Yukon	Alberta
Puerto Rico	The Commonwealth of Northern Mariana Islands	

Unless the taxpayer can show it made sales only to bona fide residents of these states, possessions, and provinces and it maintained proper records identifying those sales and customers, the taxpayer is not entitled to the exemption. Thus far, the taxpayer has failed to provide such proof. If the taxpayer can provide the Audit Division such records before the time allotted in RCW 82.32.060 expires, it can seek a refund or credit for taxes paid.

Finally, the taxpayer states the Department did not assess tax on its warranty repair income in a prior audit three years ago. Even though the taxpayer has not changed its business practice since then, tax was assessed in the present audit. The Washington Supreme Court discussed a very

similar issue in Kitsap-Mason Dairymen's Ass'n. v. Washington State Tax Comm'n, 77 Wn.2d 812, 467 P.2d 312 (1970). In Kitsap-Mason, the taxpayer had made erroneous bookkeeping entries for fifteen years pertaining to sales tax collections and remittances. The state tax commission did not question that bookkeeping practice in audits prior to the one that raised it. Nonetheless, the Supreme Court ruled that the tax commission was not estopped (i.e. barred) from assessing and collecting the tax. The Supreme Court declared:

This is not a case in which auditors changed their interpretation of a statute or rule. It is one in which they overlooked through ignorance, neglect or inadvertence Kitsap's error in computing the tax. The fact that the oversight only recently has been discovered does not relieve Kitsap of its liability for the correct tax during the audit period now under consideration.

77 Wn.2d at 818. Likewise, in the present matter there was not a change in interpretation of a statute or rule. The fact that the Department previously overlooked the taxpayer's obligation to report the warranty repair income does not relieve the taxpayer of its liability for the correct tax during the audit period now under consideration.

DECISION AND DISPOSITION:

Taxpayer's petition is denied.

Dated this 8th day of March 1999