

SC PRIVATE LETTER RULING #09-1

SUBJECT: Residential Water Heater Repair Program
(Sales and Use Tax)

REFERENCES: S. C. Code Ann. Section 12-36-910 (2000, Supp. 2007)
S. C. Code Ann. Section 12-36-1310 (2000, Supp. 2007)

AUTHORITY: S. C. Code Ann. Section 12-4-320 (2000)
S. C. Code Ann. Section 1-23-10(4) (2005)
SC Revenue Procedure #05-2

SCOPE: A Private Letter Ruling is an advisory opinion issued to a specific taxpayer by the Department to apply principles of law to a specific set of facts or a particular tax situation. It is the Department's opinion limited to the specific facts set forth, and is binding on agency personnel only with respect to the person to whom it was issued and only until superseded or modified by a change in statute, regulation, court decision, or another Departmental advisory opinion, providing the representations made in the request reflect an accurate statement of the material facts and the transaction was carried out as proposed.

Question:

Are the monthly charges by XYZ Company (d/b/a ABC) to residential customers for its repair program for existing, connected water heaters subject to the sales and use tax?

Conclusion:

The monthly charges by XYZ Company (d/b/a ABC) to residential customers for its repair program for existing, connected water heaters are not subject to the sales and use tax since the sales tax is only imposed on sales or renewals of warranty, maintenance, or similar service contracts for tangible personal property and the water heaters in question are real property at the time of the sales or renewals of the warranty contracts.

Facts:

XYZ Company, d/b/a/ ABC, ("ABC") is a public utility corporation that will be offering its residential customers in South Carolina the opportunity to participate in a Water Heater Repair Program ("the program").

The program will cover the repair and replacement of a customer's existing, connected electric or gas water heater due to normal wear and tear, up to an annual maximum of \$750.00. The retail cost of the program to customers will be \$4.99 per month per water heater. There will be no deductibles for repairs or service calls; however, the cost of any repairs completed that exceed the annual maximum of \$750.00 will be the responsibility of the customer and will be due at the time the service is rendered.

There is a 30-day waiting period from the day a customer enrolls in the program before a customer is eligible for repair services. Once a customer makes the first monthly payment, the customer is enrolled and the 30-day waiting period begins. The term of the program begins at the end of the 30-day waiting period when the customer is eligible for covered repairs and remains in effect provided there is not a failure of the customer to make a monthly payment. A term is defined as a month in length. If a customer moves, the program is not transferable to the customer's new residence and the customer must enroll in the program at the new residence.

ABC has contracted with a third party to administer the program ("Administrator"). The contract with the Administrator also gives the Administrator the right to market and sell agreements under the program to ABC's customers, and customer agreements under the program will be the exclusive property of the Administrator. The customer agreements will be written between the customers and a subcontractor of the Administrator. Customers will call a toll-free number owned by the Administrator to request service. Service will be performed by a subcontractor of the Administrator; however, ABC's vans (with ABC's logo) will be used and technicians will carry identification badges with ABC's name.

Under the terms of ABC's contract with the Administrator, ABC will bill customers for the monthly fees on their electric bills and remit the monthly fees, less an administrative fee or commission, to the Administrator. All work completed will be covered from the Administrator's portion of the monthly fee. ABC will not be billed by the Administrator for labor or the purchase of parts used in the performance of the warranty work.

Discussion:

Effective for sales or renewals on or after October 1, 2005, Code Sections 12-36-910(B) and 12-36-1310(B) impose the sales and use tax on the:

gross proceeds accruing or proceeding from the sale or renewal of warranty, maintenance, or similar service contracts for tangible personal property, whether or not such contracts are purchased in conjunction with the sale of tangible personal property.

Code Section 12-36-60 defines the term “tangible personal property” to mean:

personal property which may be seen, weighed, measured, felt, touched, or which is in any other manner perceptible to the senses. It also includes services and intangibles, including communications, laundry and related services, furnishing of accommodations and sales of electricity, the sale or use of which is subject to tax under this chapter and does not include stocks, notes, bonds, mortgages, or other evidences of debt. Tangible personal property does not include the transmission of computer database information by a cooperative service when the database information has been assembled by and for the exclusive use of the members of the cooperative service. (Emphasis added.)

As such, a charge for the sale or renewal of a warranty, maintenance, or similar service contract for tangible personal property is subject to the sales and use tax, whether or not such contract was purchased in conjunction with the sale of the tangible personal property. In addition, since warranty, maintenance and similar service contracts are subject to the sales and use tax, sales or renewals of warranty, maintenance and similar service contracts are considered sales of tangible personal property for purposes of the sales and use tax.

Based on the above, if the water heaters are tangible personal property, then the charges for the warranty contracts are subject to the tax (unless otherwise exempt under the law). If the water heaters are real property, then the charges for the warranty contracts are not subject to the tax.

For additional guidance in this matter, we refer to *City of North Charleston v. Claxton*, 431 S.E.2d 610 (S.C. 1993). While that case dealt with the value of property in a condemnation proceeding, it also addressed the issue of real (fixtures) versus personal property.

Quoting from that case:

Criteria for determining whether an item remains personalty or becomes a fixture when affixed to realty includes: (1) the mode of attachment; (2) the character of the structure of the article; (3) the intent of the parties making the annexation; and, (4) the relationship of the parties. Creative Displays, 272 S.C. at 72, 248 S.E.2d at 918.

The Court, in *Claxton*, referenced *Rebel Manufacturing and Marketing Corporation* 54 B.R. 674 (Bkrcty. D.S.C. 1985). In that case, a bank argued that the sale of a mobile home was subject to a mortgage on the realty because it was a fixture [real property]. The mobile home was underpinned, anchored, and connected to sewerage, water and electric lines. Also, the home had a screened porch attached and was adjacent to several large trees.

In ruling for the bank, the Court reasoned:

The various substantial structures and trees surrounding the mobile home would be severely damaged, if not destroyed, should the mobile home be removed.

* * * *

It seems clear that the debtor's positioning the mobile home among the trees, and adding the construction [the porch] warrants the inference that the intent of the debtor was for the mobile home to become a part of the realty.

Paris Mountain Water Company v. Woodside _133 S.C. 383, 131 S.E. 37 (1925), a South Carolina State Supreme Court case, was concerned with whether water pipes placed in lands belonging to others were to be taxed as realty or personalty. The Court, in holding that the pipe was to be taxed as realty, stated:

In the requirement of an intention to make the article annexed a permanent accession to the land, the expression of permanent does not, it seems, imply that the annexation must be intended to be perpetual, but rather that the article shall appear to be intended to remain where fastened until worn out, until the purpose to which the realty is devoted has been accomplished, or until the article is superseded by another article more suitable for the purpose.

Based on the above, water heaters that become a part of a home are real property. As such, the monthly charges by XYZ Company (d/b/a ABC) to residential customers for its repair program for existing, connected water heaters are not subject to the sales and use tax since the sales tax is only imposed on sales or renewals of warranty, maintenance, or similar service contracts for tangible personal property and the water heaters in question are real property at the time of the sales or renewals of the warranty contracts.

SOUTH CAROLINA DEPARTMENT OF REVENUE

s/Ray N. Stevens
Ray N. Stevens, Director

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Columbia, South Carolina