
State of South Carolina
Department of Revenue
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SC REVENUE RULING #06-9

SUBJECT: Warranty, Maintenance and Similar Service Contracts
(Sales and Use Tax)

EFFECTIVE DATE: October 1, 2005

SUPERSEDES: SC Revenue Ruling #93-6 for transactions on or after
10/1/05, SC Revenue Ruling #05-12, and all previous
advisory opinions and any oral directives in conflict
herewith.

REFERENCE: S. C. Code Ann. Section 12-36-910(B)(6) (Supp. 2005)
S. C. Code Ann. Section 12-36-1310(B)(6) (Supp. 2005)
Senate Bill 1245, Sections 20, 21, and 23 (Act No. 386) of
2006 (Effective October 1, 2005)

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

SCOPE: The purpose of a Revenue Ruling is to provide guidance to
the public and to Department personnel. It is an advisory
opinion issued to apply principles of tax law to a specific
set of facts or general category of taxpayers. It is the
Department's position and is binding on agency personnel
until superseded or modified by a change in statute,
regulations, court decision, or another Departmental
advisory opinion.

EFFECTIVE DATE NOTICE:

This advisory opinion is effective for transactions occurring on or after October 1, 2005. SC Revenue Ruling #93-6 is still valid with respect to transactions occurring prior to October 1, 2005. (See House Bill 3767, Section 19 (Act No, 161) of 2005 and Senate Bill 1245, Sections 20, 21 and 23 (Act No. 386) of 2006.)

INTRODUCTION:

Frequently, when tangible personal property is purchased, the manufacturer warrants that the property will be free of defects for a specified period of time. The cost of this warranty is not separately stated, but is a part of the sales price of the property.

The retailer, usually in conjunction with the manufacturer, will often offer the customer the opportunity to purchase an extended warranty or other maintenance or similar service contract at the time the tangible personal property is purchased. For example, a copier manufacturer may warrant that the copier it manufactures will be free from defects for twelve months. For an additional fee, that will be separately stated on the invoice to the customer, the customer can buy an extended warranty. The extended warranty will guarantee that the copier will be free from defects for an additional twelve months, for a total warranty period of twenty-four months. If the copier does breakdown, the manufacturer (or an authorized service center) will repair the copier, usually, free of charge.

If the customer decides not to purchase the extended warranty or other maintenance or similar service contract at the time the tangible personal property is purchased, some retailers will allow the customer to purchase such a contract after the sale. In the above example, if the customer had not purchased the extended warranty at the time of the sale, the retailer may contact the customer at any time within a specified period of time after the sale and offer the customer a second opportunity to buy the extended warranty.

In addition, other companies may also sell warranty or other maintenance or similar service contracts for tangible personal property that was sold by another person.

Questions have arisen as to the application of the sales and use tax to the sale or renewal of warranty, maintenance, or similar service contracts for tangible personal property and to the sale or use of tangible personal property used in replacing a defective part under the warranty contract.

LAW AND DISCUSSION:

Effective for sales or renewals on or after October 1, 2005, Code Sections 12-36-910(B)(6) and 12-36-1310(B)(6) 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.

Code Section 12-36-2120 exempts from the tax:

* * * *

(53) motor vehicle extended service contracts and motor vehicle extended warranty contracts.

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(69) the sale or renewal of a warranty, maintenance, or similar service contract for tangible personal property if the sale or purchase of the tangible personal property covered by the contract is exempt or excluded from the tax imposed by this chapter.

In addition, it is important to be aware of an additional statutory provision as it relates to warranties. The sales tax, in addition to sales of tangible personal property, also applies to the “fair market value of tangible personal property previously purchased at wholesale which is withdrawn from the business or stock and used or consumed in connection with the business.” See Code Section 12-36-90.

As such, the sales tax is due on the withdrawal from inventory of the tangible personal property for use in replacing a defective part under the warranty contract; however, Code Section 12-36-90(1)(c)(iii) excludes from the tax:

tangible personal property replacing defective parts under written warranty contracts if:

(A) the warranty, maintenance, service, or similar contract is given without charge, at the time of original purchase of the defective property, or the tax was paid on the sale or renewal of warranty, maintenance, or similar service contract for tangible personal property of which the defective part was a component, whether or not such contract was purchased in conjunction with the sale of tangible personal property,

(B) in the case of a warranty, maintenance, service, or similar contract that is given without charge at the time of original purchase of the defective property, the tax was paid on the sale of the defective part or on the sale of the property of which the defective part was a component, and

(C) the warrantee is not charged for any labor or materials.

Therefore, the tax does not apply to the withdrawal from inventory of tangible personal property for use in replacing defective part under a warranty contract if:

1. tax was paid on the sale or the renewal of the warranty contract and the customer is not charged for any labor or material when the part is replaced; or,
2. the warranty contract is given without charge at the time of the original purchase of the defective property, and the tax was paid on the sale of the defective part or on the sale of the property of which the defective part was a component, and the customer is not charged for any labor or material when the part is replaced.

Note, if both conditions set forth in Item 1 are not met, or if all three conditions set forth in Item 2 are not met, then tax is due on the withdrawal from inventory of the tangible personal property for use in replacing a defective part under the warranty contract. The tax would be based on the fair market value of the property withdrawn from inventory.

Code Section 12-36-90(2) states that “gross proceeds of sales,” the basis for the sales tax, does not include:

- (1) tangible personal property purchased by a person engaged in the business of servicing a warranty, maintenance, or similar service contract for use in replacing a defective part under the contract if tax was paid on the sale or the renewal of the contract and the customer is not charged for labor or material when the part is replaced.

Therefore, the sale at retail of tangible personal property to a person engaged in the business of servicing a warranty, maintenance, or similar service contract for use in replacing a defective part under the contract is not subject to the tax if tax was paid on the sale or the renewal of the contract covering the tangible personal property being repaired and if the customer is not charged for labor or material when the part is replaced.

QUESTIONS AND ANSWERS:

Sales and Renewals of Contracts

1. Are sales of warranty, maintenance or similar service contracts for tangible personal property subject to the sales and use tax?

Sales at retail of warranty, maintenance or similar service contracts for tangible personal property are subject to the sales and use tax, unless otherwise exempt under the law.

2. Are charges for renewals of warranty, maintenance or similar service contracts for tangible personal property subject to the sales and use tax?

Charges for renewals of warranty, maintenance or similar service contracts for tangible personal property are subject to the sales and use tax, unless otherwise exempt under the law.

3. Must a warranty, maintenance or similar service contract for tangible personal property be sold in conjunction with the tangible personal property covered by the contract in order for the sale or renewal of the contract to be subject to the sales and use tax?

No. Sales and renewals of warranty, maintenance or similar service contracts for tangible personal property are subject to the sales and use tax, unless otherwise exempt under the law, when sold in conjunction with the tangible personal property covered by the contract and when not sold in conjunction with the tangible personal property covered by the contract.

4. Must a warranty, maintenance or similar service contract for tangible personal property be sold by the same person selling the tangible personal property covered by the contract in order for the sale or renewal of the contract to be subject to the sales and use tax?

No. Sales and renewals of warranty, maintenance or similar service contracts for tangible personal property are subject to the sales and use tax, unless otherwise exempt under the law, when sold by the person selling the tangible personal property covered by the contract and when sold by any other person (i.e., a third party who did not sell the tangible personal property covered by the contract).

Exemptions for Contracts:

5. Does the sales and use tax law exempt any retail sales or renewals of warranty, maintenance or similar service contracts for tangible personal property?

Yes. Code Section 12-36-2120 exempts from the sales and use tax the sale or renewal of “motor vehicle extended service contracts and motor vehicle extended warranty contracts” and the sale or renewal of a “warranty, maintenance, or similar service contract for tangible personal property if the sale or purchase of the tangible personal property covered by the contract is exempt or excluded from the [sales and use] tax.”

6. If a warranty or extended service contract only covers a particular part or component of a motor vehicle, is the sale or renewal of a motor vehicle extended service contract or a motor vehicle extended warranty contract exempt from the sales and use tax?

The sale or renewal of a warranty or extended service contract that only covers a particular part or component of a motor vehicle is exempt from the sales and use tax, provided the part or component is a major part or component that is integral and necessary to the functioning of the motor vehicle as a motor vehicle and the contract was originally sold in conjunction with the sale of the motor vehicle or the contract is a renewal of a contract that was originally sold in conjunction with the sale of the motor vehicle.

The following two examples are provided as guidance:

(a) The engine of a motor vehicle is a major part or component integral and necessary to the functioning of the motor vehicle as a motor vehicle; therefore, the sale or renewal of a warranty or extended service contract that only covers the engine of the motor vehicle is exempt from the sales and use tax if the contract was originally sold in conjunction with the sale of the motor vehicle or the contract is a renewal of a contract that was originally sold in conjunction with the sale of the motor vehicle. If the warranty or extended service contract that covers the engine was not sold in conjunction with the sale of the motor vehicle (e.g., the owner of the motor vehicle purchases a replacement engine for the motor vehicle), then contract is not a motor vehicle warranty or motor vehicle extended service contract and is not exempt from the tax.

(b) The radio in a motor vehicle is not a major part or component integral and necessary to the functioning of the motor vehicle as a motor vehicle; therefore, the sale or renewal of a warranty or extended service contract that only covers the radio in the motor vehicle is not exempt from the sales and use tax.

7. What are some examples of an exempt sale or renewal of a warranty, maintenance, or similar service contract for tangible personal property when the sale or purchase of the tangible personal property covered by the contract is exempt or excluded from the [sales and use] tax?

Each of the following is an example of a sale or renewal of a warranty, maintenance, or similar service contract for tangible personal property that is exempt from the tax because the sale or purchase of the tangible personal property covered by the contract is exempt or excluded from the [sales and use] tax:

(a) the sale or renewal of a warranty, maintenance, or similar service contract for a manufacturing machine, or a part of a manufacturing machine, that is exempt from the sales and use tax under Code Section 12-36-2120(17);

(b) the sale or renewal of a warranty, maintenance, or similar service contract for farm machinery, or a part of the farm machinery, used in planting, cultivating or harvesting farm crops that is exempt from the sales and use tax under Code Section 12-36-2120(16);

(c) the sale or renewal of a warranty, maintenance, or similar service contract for railroad cars, locomotives, monorail cars and the engines or motors that propel them, and their parts that are exempt from the sales and use tax under Code Section 12-36-2120(20); and,

(d) the sale or renewal of a warranty, maintenance, or similar service contract for technical equipment and machinery sold to radio and television stations and cable television systems used in producing, broadcasting or distributing programs that are exempt from the sales and use tax under Code Section 12-36-2120(26).

Contracts for Maximum Tax Items

8. Is the sale or renewal of a warranty, maintenance or similar service contract for tangible personal property that is subject to the maximum tax provisions under Code Section 12-36-2110 subject to the sales and use tax?

Yes, the sale or renewal of a warranty, maintenance or similar service contract for tangible personal property that is subject to the maximum tax provisions under Code Section 12-36-2110 is subject to the sales and use tax, unless otherwise exempt under the law. In addition, the maximum tax provisions do not apply to sales and renewals of warranty, maintenance or similar service contracts.

Each of the following is an example of a sale or renewal of a warranty, maintenance, or similar service contract for tangible personal property that is subject to the maximum tax provisions under Code Section 12-36-2110:

(a) The sale of a boat for \$20,000.00 is subject to the tax; however, the tax due is limited to \$300.00 under the maximum tax provisions under Code Section 12-36-2110. If the retailer sold the purchaser an extended warranty contract for the boat for an additional \$1,000.00, the sales price (\$1,000.00) of the extended service

contract is subject to the tax at the rate of 5% (6% beginning June 1, 2007¹), plus any additional local sales and use tax. Based on a 5% state tax rate in a non-local tax county, the total tax due on the boat and the extended service contract would be \$350.00 (\$300.00 tax on the boat and \$50.00 on the extended service contract).

Note: See SC Revenue Ruling #92-12 for information as to the calculation of the tax when a boat is sold in conjunction with a motor and/or a trailer.

(b) The sale of an airplane for \$2,000,000.00 is subject to the tax; however, the tax due is limited to \$300.00 under the maximum tax provisions under Code Section 12-36-2110. If the retailer sold the purchaser an extended warranty contract for the airplane for an additional \$10,000.00, the sales price (\$10,000.00) of the extended service contract is subject to the tax at the rate of 5% (6% beginning June 1, 2007²), plus any additional local sales and use tax. Based on a 5% state tax rate in a non-local tax county, the total tax due on the airplane and the extended service contract would be \$800.00 (\$300.00 tax on the airplane and \$500.00 on the extended service contract).

(c) The sale of a motor vehicle for \$20,000.00 is subject to the tax; however, the tax due is limited to \$300.00 under the maximum tax provisions under Code Section 12-36-2110. If the retailer sold the purchaser an extended warranty contract for the motor vehicle for an additional \$1,000.00, the sales price (\$1,000.00) of the extended service contract is exempt from the tax under Code Section 12-36-2120(53). The total tax due on the motor vehicle and the extended service contract would therefore be \$300.00 (\$300.00 tax on the motor vehicle and \$0.00 on the extended service contract since it is exempt under Code Section 12-36-2120(53)).

Note: See Questions #5 and #6 for additional information concerning motor vehicle warranty contracts and motor vehicle extended service contracts.

¹ At the time this document was issued, the total state sales and use tax rate was 5%. Beginning June 1, 2007, the total state sales and use tax rate will be 6%. Code Section 12-36-1110, which increases the sales and use tax rate by 1% beginning June 1, 2007, states:

Beginning June 1, 2007, an additional sales, use, and casual excise tax equal to one percent is imposed on amounts taxable pursuant to this chapter, except that this additional one percent tax does not apply to amounts taxed pursuant to Section 12-36-920(A), the tax on accommodations for transients, nor does this additional tax apply to items subject to a maximum sales and use tax pursuant to Section 12-36-2110 nor to the sale of unprepared food which may be lawfully purchased with United States Department of Agriculture food coupons.

² See footnote #1.

Repairs

9. If a retailer withdraws a part from his inventory to replace a defective part under a warranty contract, is the withdrawal of the part from inventory subject to the sales tax?

When a retailer withdraws an item from inventory for use instead of for sale to a customer, the withdrawal is considered a retail sale subject to the sales tax based on the fair market value of the item withdrawn from inventory.

However, with respect to repairs made under a warranty contract, the sales tax does not apply to the withdrawal from inventory of tangible personal property for use in replacing defective part under the warranty contract if:

(a) tax was paid on the sale or the renewal of the warranty contract and the customer is not charged for any labor or material when the part is replaced; or,

(b) the warranty contract is given without charge at the time of the original purchase of the defective property, and the tax was paid on the sale of the defective part or on the sale of the property of which the defective part was a component, and the customer is not charged for any labor or material when the part is replaced.

Note, if both conditions set forth in Item (a) are not met, or if all three conditions set forth in Item (b) are not met, then the tax is due on the withdrawal from inventory of the tangible personal property for use in replacing a defective part under the warranty contract. The tax would be based on the fair market value of the property withdrawn from inventory.

10. If a person who is engaged in the business of servicing a warranty, maintenance, or similar service contract on behalf of another person who sold or issued the contract purchases a replacement part at retail to repair the tangible personal property covered by the warranty, maintenance, or similar service contract, is the purchase at retail of the replacement part subject to the tax?

No, provided the tax was paid on the sale or the renewal of the contract covering the tangible personal property being repaired and the customer is not charged for labor or material when the part is replaced. See Code Section 12-36-90(2)(1).

However, if the tax was not paid on the sale or the renewal of the contract covering tangible personal property being repaired, or the customer is charged for labor or material when the part is replaced, then the tax is due on the purchase of the replacement part.

Note: If the warranty contract is given without charge at the time of the original purchase of the defective property, and the tax was paid on the sale of the defective part or on the sale of the property of which the defective part was a component, and the customer is not

charged for any labor or material when the part is replaced, the sales tax does not apply to the withdrawal from inventory of tangible personal property for use in replacing defective part under the warranty contract.

Wholesale Sales of Contracts;

11. If a manufacturer of a product also makes available an extended warranty contract or extended service contract with respect to the manufactured product, can the manufacturer accept a valid resale certificate from, and sell an extended service contract at wholesale to, an unrelated retail dealer of its product who will in turn resell the extended service contract at retail to the end user?

Yes, since warranty, maintenance or similar service contracts for tangible personal property are considered tangible personal property for sales and use tax purposes under Code Section 12-36-60, a manufacturer of a product that also makes available an extended warranty contract or extended service contract with respect to the manufactured product can accept a valid resale certificate from, and sell an extended service contract at wholesale to, an unrelated retail dealer of its product who will in turn resell the extended service contract at retail to the end user.

Remittance of the Tax:

12. If a manufacturer of a product also makes available an extended warranty contract or extended service contract with respect to the manufactured product, but the extended service contract is sold at retail to the end user by an unrelated retail dealer, who must remit the tax to the Department of Revenue on the sale of the contract – the manufacturer or the retail dealer?

The retail dealer is responsible for remitting the tax due on the retail sale of the extended service contract – whether such contract was purchased at wholesale and sold at retail by the retail dealer, or sold at retail on consignment by the retail dealer, or sold at retail by the retail dealer as the agent of the manufacturer.

However, if the manufacturer establishes a bona fide agent principal relationship with the retail dealer with respect to the sale or renewal of extended service contract, then the manufacturer can be held responsible for remitting the tax to the Department of Revenue on the sale or renewal of extended service contracts by the retailer if the retailer fails to remit the tax to the Department.

13. If a customer who purchased an extended warranty contract or extended service contract from the retail dealer described above in Question #12, renews the contract, who must remit the tax to the Department of Revenue on the sale of the renewal of the contract – the manufacturer or the retail dealer?

If the customer renews the extended warranty contract or extended service contract, then:

(a) the retail dealer must remit the tax to the Department of Revenue on the renewal of the contract if the customer renews the contract with the retail dealer (whether such renewal was sold at retail by the retail dealer, or sold at retail on consignment by the retail dealer, or sold at retail by the retail dealer as the agent of the manufacturer); or

(b) the manufacturer must remit the tax to the Department of Revenue on the renewal of the contract if the customer renews the contract directly with the manufacturer. In addition, if the manufacturer establishes a bona fide agent principal relationship with the retail dealer with respect to the sale or renewal of extended service contract, then the manufacturer can be held responsible for remitting the tax to the Department of Revenue on the sale or renewal of extended service contracts by the retailer if the retailer fails to remit the tax to the Department.

14. Since the sale or renewal at retail of a warranty, maintenance or similar service contract for tangible personal property is subject to the use tax, can a South Carolina purchaser of a warranty, maintenance or similar service contract for tangible personal property located in the State be held liable for the use tax on the purchase of the contract from an out-of-state retailer of the contract (including retail dealers, manufacturers selling or renewing contracts at retail, third-party retail sellers of contracts, etc)?

Yes. If the purchaser buys or renews the contract with an out-of-state retailer (including retail dealers, manufacturers selling or renewing contracts at retail, third-party retail sellers of contracts, etc) that has not obtained a retail license from the Department, or that does not otherwise collect the tax from the purchaser, then the purchaser is liable for the use tax on its purchase or renewal of the contract.

SOUTH CAROLINA DEPARTMENT OF REVENUE

s/Ray N. Stevens

Ray N. Stevens, Director

November 16, 2006
Columbia, South Carolina