

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)	
)	DOCKET NO. 22600
[Redacted])	
Petitioner.)	
)	DECISION
_____)	

On October 30, 2009, the staff of the Sales and Use Tax Audit Bureau (Bureau) of the Idaho State Tax Commission (Commission) issued a Notice of Deficiency Determination (Notice) to [Redacted](taxpayer) proposing sales tax and interest for the audit period April 1, 2006, through March 31, 2009, in the total amount of \$7,436.

In correspondence dated October 21, 2009, the taxpayer filed a timely appeal and petition for redetermination. At the taxpayer’s request, the Commission held an informal hearing on March 9, 2010. For the reasons that follow, the Commission upholds the audit findings.

BACKGROUND

The taxpayer, an incorporated entity owned by a family, operates an [Redacted] business in Idaho. In a sales and use tax audit of the business, the Bureau asserted that the taxpayer made untaxed sales for which there were no tax exemptions.

The taxpayer made repairs of [Redacted] in fulfillment of buyers’ claims against their optional warranties purchased concurrently with the [Redacted]. The taxpayer billed the repairs to the retailers who sold both the [Redacted]. The Bureau’s review of the record determined that the taxpayer failed to collect tax from the retailers/warrantors on the sale [Redacted].

According to the auditor, one particular [Redacted] incorrectly collected a sales tax on the optional [Redacted] when it sold [Redacted]. According to the taxpayer, the [Redacted] buyers who purchased [Redacted], erroneous as it may be in the estimation of the Bureau, should free

the taxpayer of any obligation to collect tax from the retailer/warrantor. This supposition is central to the disagreement that is the subject of this decision.

APPLICABLE TAX LAW

In Idaho, the sale of tangible personal property is taxable (Idaho Code §§ 63-3612(1) and 63-3619). The term “sales price,” for determining the amount subject to tax in a transaction, includes both the amount for which tangible personal property is sold plus the amount charged for services agreed to be rendered as a part of the sale (Idaho Code § 63-3613(a)).

Warranties on goods sold are of two general types. One type is a warranty which comes with the purchase of goods and over which the customer has no control. Often, these warranty charges are not separately stated from the price of the goods themselves, and the warranty is always a condition of the sale itself. Such warranties are called mandatory.

There are optional warranties as well. As the name implies, the customer has discretion with an optional warranty when he or she buys goods. A buyer can accept the offer of warranty terms and pay for it or decline the purchase.

Applying the definition of “sales price,” discussed above, when warranties are sold as a condition of a sale of tangible personal property (i.e. mandatory) they are to be taxed as part of the sale. When parts are replaced under a mandatory warranty claim, the parts are considered to have been taxed at the time the warranty or service agreement was sold.

Optional warranties are treated differently than mandatory warranties. Since an optional warranty is not taxed at the time tangible personal property is sold, because it is not a condition of the sale of goods, when a third-party repair facility performs a warranty repair and bills the warranty seller, the repair facility should separately state and charge tax on the sale of parts to the warranty seller.

As it applies to the facts in this case, the repair facility, in this instance the taxpayer in the audit protest, should have collected tax on the sale of parts used in fulfillment of the retailer/warrantor's obligations to the customers who purchased the [Redacted] goods.

Idaho Sales Tax Administrative Rule 049 provides a summary of the foregoing mandatory and optional warranty definitions and the tax consequences. The text regarding optional warranties is cited here in relevant part:

05. Optional Warranty or Service Agreement. If the warranty or service agreement is optional to the purchaser, no sales tax shall be charged on the sale of the warranty or service agreement. A taxable transaction does occur with regard to the seller of the warranty or service agreement upon performance of the repair....

b. When a third-party dealer or repair facility performs the repair and bills the seller of the warranty or service agreement, the third-party dealer or repair facility will separately state and charge sales tax on the parts to the seller of the warranty or service agreement.... (IDAPA 35.01.02.049.)

PROTEST SUMMARY

The audit approach involved the sampling of transactions from the taxpayer's universe of available data. The errors found in the sample were translated into an error rate which was then applied to the total value of the relevant accounts to determine a liability.

The protest letter states that there are "factual differences" in some sample transactions that the auditor tested for sales tax compliance. While this likely meant that the taxpayer had some documents that, once examined by the auditor, would lower the number of errors and, ultimately, the error rates which contributed to the liability, this issue was not pursued at the hearing, nor was it mentioned in any further discussion between the Commission and the taxpayer.

The only legal issue discussed was the tax liability imposed by the auditor on the sale of repair parts the taxpayer provided in fulfillment of the retailer/warrantor's guarantees to its

customers. The taxpayer noted that one retailer was the primary seller of the optional warranties and that it charged tax on the warranties at the time it sold the [Redacted] goods. Since the retailer charged tax on the warranties, the taxpayer believes it has no tax liability because the retailer remitted tax to the state.

ANALYSIS

The taxpayer's protest implies that, regardless of underlying circumstances, tax was owed and collected. It should make no difference as to how this came about. It is unclear from the protest letter and the hearing if the taxpayer disagrees with the administrative rule regarding optional warranties, cited previously, or whether the taxpayer merely believes that the payment of tax has been fulfilled.

Alternatively, the Commission argues that the tax at issue was not owed by the optional warranty purchasers. If a purchaser wants a refund for tax paid erroneously to a retailer, it would qualify for a refund if properly applied for, documented, and was within the statute of limitations for a refund.

The legal incidence of the tax aside, the Commission is unable to determine if the taxpayer's approach is to the detriment of the state. That is, does the tax erroneously collected by the [Redacted] retailer from its customers completely offset the tax due on the sale of parts in fulfillment of the terms of the optional warranties? It depends upon the failure rates of a multitude of products over various warranty periods, and it is not relevant to this decision to determine the answer. Regardless of the conclusion that research may have brought to bear on the question, the Commission must abide by the applicable statutes and the associated administrative rule. The Commission, therefore, issues a decision consistent with them.

In order to further consider its options with respect to the Notice of Deficiency Determination, on August 11, 2010, the taxpayer signed a waiver to extend the time within which the Commission was obligated by statute to issue a decision (Idaho Code § 63-3045B(3) – (5)).

The Bureau added interest to the sales tax deficiency per Idaho Code §§ 63-3045(6). Interest is accrued through November 30, 2010, and continues to accrue until the tax liability is paid.

WHEREFORE, the Notice of Deficiency Determination dated October 30, 2009, is hereby APPROVED, and as APPROVED, is AFFIRMED and MADE FINAL, in accordance with the provisions of this decision.

IT IS ORDERED and THIS DOES ORDER that the taxpayer pay the following tax and interest:

<u>TAX</u>	<u>INTEREST</u>	<u>TOTAL</u>
\$6,673	\$1,459	\$8,132

DEMAND for immediate payment of the foregoing amount is hereby made and given.

An explanation of the taxpayer's right to appeal this decision is enclosed.

DATED this _____ day of _____ 2010.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this _____ day of _____ 2010, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to:

[Redacted]
