

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING #97-07**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

Taxability of warranty contracts sold to out of state consumers.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the department by the taxpayer. The rulings herein are binding upon the Department and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time.

Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and

(E) The taxpayer directly involved must have acted in good faith in relying upon the ruling; and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[THE TAXPAYER] is a Tennessee corporation whose principal offices are in [CITY], Tennessee. [THE TAXPAYER] designs, produces, and markets computer software and hardware used in the [INDUSTRY]. The hardware and software, along with maintenance contracts, are sold to customers throughout the United States and around the world. Product sales are invoiced for the amount of the product plus the appropriate sales tax. The state sales tax rates used are those applicable to the state where the goods are shipped.

The maintenance agreement provides that [THE TAXPAYER] warrants "all hardware repairs and standard updates, calibrations, software updates, mass product releases (including manual revisions) and telephone assistance." Repairs for hardware, telephone assistance, and other warranty services are performed in Tennessee. Upon the purchase of [THE TAXPAYER'S] warranty or maintenance agreement, [THE TAXPAYER] obligates itself to provide the warranty services. The agreement to provide such services is made by [THE TAXPAYER] in Tennessee. [THE TAXPAYER] collects Tennessee sales tax on hardware maintenance agreements sold to out of state customers. Out of state customers who do not have a Tennessee sales tax exemption certificate are billed for Tennessee sales tax on repair work contracts and hardware maintenance contracts.

ISSUE

Whether [THE TAXPAYER] must collect Tennessee sales tax on the sale of repair work and maintenance contracts to out of state customers.

RULING

[THE TAXPAYER] must collect Tennessee sales tax on the sale of repair work and maintenance contracts sold to out of state customers.

ANALYSIS

Tenn. Code Ann. § 67-6-205 imposes "a tax at the rate of six percent (6%) of the gross charge for all services taxable under this chapter." Tenn. Code Ann. § 67-6-102(23)(F)(ix) includes as a taxable service "[c]harges for warranty or service contracts warranting the repair or maintenance of tangible personal property; provided, that any

repairs to the extent covered by the contract shall not also be subject to tax.” The sale of a warranty or service contract is defined in the statute as a taxable service.

The Tennessee Supreme Court addressed a situation where equipment was leased in Tennessee for use out of state in *Williams Rentals, Inc. v. Tidwell*, 516 S.W. 2d 614 (Tenn. 1974). The Court held that the transaction was not exempt as interstate commerce and the lessor was responsible for collecting sales tax on the lease. The Court held that the test of whether the lease was an interstate transaction, and exempt from tax, was the location where the lease was made. Since the lease was made in Tennessee, the lease was subject to tax, although the equipment involved was immediately taken and used out of state. *Williams Rentals, Inc. v. Tidwell*, 516 S.W. 2d 614 (Tenn. 1974).

[THE TAXPAYER]’s repair work contracts and hardware maintenance contracts are contractual obligations. [THE TAXPAYER] obligates itself to provide the warranty service in Tennessee. [THE TAXPAYER] both enters into and performs the taxable service, the contractual obligation under the warranty contracts, in Tennessee.

Accordingly, [THE TAXPAYER] must collect Tennessee sales tax on the amount charged for a work repair or maintenance agreement.

Caroline R. Krivacka
Tax Counsel

APPROVED: Ruth E. Johnson
Commissioner

DATE: 4/18/97