

## **Department of Revenue**

### **Revenue Notice # 16-03: Sales and Use Tax – Optional Warranty and Maintenance Contracts on Equipment – Revocation and Replacement of Revenue Notice # 12-12**

#### **Introduction**

This Revenue Notice explains the sales tax treatment of optional maintenance and warranty contracts on equipment. This Revenue Notice does not apply to optional maintenance contracts on computer software which are governed by *Minnesota Rules* part 8130.9910.

This Revenue Notice revokes and replaces Revenue Notice # 12-12. This notice in substance does not differ in result from the revoked notice but clarifies the information and adds additional information about unbundled maintenance contracts.

#### **Background**

In 2008, amendments were made to *Minnesota Statutes* to conform to the Streamlined Sales Tax Agreement bundled transaction provisions. *Minnesota Statutes* section 297A.61, subdivision 4(m), was added to provide that a retail sale includes a sale of a bundled transaction.

“Bundled transaction” is defined in *Minnesota Statutes* section 297A.61, subdivision 38, to mean the retail sale of two or more products sold for one nonitemized price. “Product” includes tangible personal property, services, intangibles, and digital goods, including specified digital products or other digital products, but does not include real property or services to real property.

A transaction that otherwise meets the definition of a bundled transaction is not a bundled transaction if the transaction includes taxable and nontaxable products (other than food and health care products) and the purchase price or sales price of the taxable products is de minimis.

For purposes of the bundled transaction definition, “purchase price” means the measure subject to use tax on purchases made by the seller, and “de minimis” means that the seller’s purchase price or sales price of the taxable products is ten percent or less of the total purchase price or sales price of the bundled products. Sellers must use either the purchase price or the sales price of the products to determine if the price of the taxable products is de minimis. Sellers may not use a combination of the purchase price and sales price of the products to determine if the price of the taxable products is de minimis. The seller must use the full term of a service contract to determine if the taxable products are de minimis.

#### **Types of optional contracts**

This Revenue Notice applies to three types of optional contracts: (1) bundled maintenance contracts, (2) unbundled maintenance contracts, and (3) warranty contracts. The determination as to whether a contract is a maintenance contract or a warranty contract is not necessarily based on the title of the contract. Instead, the determination is made based on the substantive

provisions of the contract.

### **1. *Bundled Maintenance Contracts***

A bundled maintenance contract is a contract for the service or repair of equipment sold for one nonitemized price. The single, nonitemized price includes both labor and the furnishing of tangible personal property. Tangible personal property includes repair parts, replacement parts, and consumable items. Consumable items are items that are depleted, disposable, get used up, or items that need to be replaced after they have been used for a period of time. Both the customer and the service provider are aware at the time the contract is entered into that tangible personal property will be replaced under the contract. The tangible personal property provided under the contract is more than ten percent of the total bundled price.

Example: An office supply company sells a photocopier machine to a customer. The customer also purchases an optional maintenance contract from the company for one nonitemized price. The maintenance contract entitles the customer to service and parts at no charge in the event of a breakdown of the photocopier machine. The contract also provides for quarterly inspections; replacement of the drum after 100,000 copies have been made; and toner to be provided on an as-needed basis. The price of the tangible personal property used under the contract is more than ten percent of the total bundled price.

### **2. *Unbundled Maintenance Contracts***

An unbundled maintenance contract is a contract for service or repair of equipment sold for separate, itemized prices. The separately itemized prices may be for labor or the furnishing of tangible personal property. Even if the invoice does not separately itemize prices, it will still be treated as an unbundled maintenance contract if the price is separately identified by product on sales-related documentation that is made available to the customer in paper or electronic form. Examples of sales-related documentation include an invoice, bill of sale, receipt, contract, service agreement, lease agreement, periodic notice of rates and services, rate card, or price list.

Example: A customer purchases a maintenance contract that provides for the labor to repair and service computer equipment as well as technology refresh services that provide for the periodic replacement of computers. The contract separately lists the price for the labor to repair and service the computer equipment and the price for the replacement computers used in the technology refresh program.

### **3. *Warranty Contract***

A warranty contract is a contract that acts like insurance against the future, unexpected costs to repair tangible personal property. Under this type of contract, neither the customer nor the seller knows at the time the contract is signed whether any tangible personal

property will be used under the contract. Warranty contracts may include repair parts and replacement parts, but do not include consumable items.

Example: An office supply company sells a computer to a customer. The customer also purchases an optional warranty contract on the computer. The warranty contract entitles the customer, at no additional charge, to telephone troubleshooting, and the labor and parts necessary to repair the computer in the event of a breakdown.

### **Department Position**

The total sales price of a bundled maintenance contract is subject to Minnesota sales and use tax if the price of the taxable products is more than de minimis. If the price of the taxable products is de minimis, then the bundled maintenance contract is not subject to Minnesota sales and use tax.

In the case of an unbundled maintenance contract, only the sales prices of separately stated taxable items are subject to Minnesota sales and use tax.

Optional warranty contracts are not subject to sales and use tax. The provider of the service must pay sales or use tax on the cost of all taxable items used under the contract. If the service provider charges the customer a separate amount for taxable items, the provider should buy the taxable items exempt for resale and charge sales tax to the customer.

Publication Date: 3/7/2016

  
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Ryan Church, Deputy Commissioner

