

**CALIFORNIA STATE BOARD OF EQUALIZATION**  
**APPEALS DIVISION SUMMARY FOR BOARD HEARING**

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3 In the Matter of the Petition for Redetermination )  
4 Under the Sales and Use Tax Law of: )  
5 LIVING SPACES FURNITURE LLC, dba ) Account Number: SR Y AA 100-202947  
6 Living Spaces Furniture ) Case ID 425660  
7 Petitioner )  
\_\_\_\_\_ ) Rancho Cucamonga, San Bernardino County

8 Type of Business: Furniture retailer

9 Audit period: 1/1/04 – 12/31/06

<u>Item</u>	<u>Disputed Amount</u>
11 Additional taxable sales	\$6,170,485
12 As determined:	\$ 701,153.84
13 Adjustment - Sales and Use Tax Department	+ 218,162.69
14 - Appeals Division	+ 193,922.49 <sup>1</sup>
Proposed redetermination	<u>\$1,113,239.02</u>
15 Less concurred	<u>628,432.90</u>
Balance, protested	<u>\$ 484,806.12</u>
16 Proposed tax redetermination	\$1,113,239.02
17 Interest through 4/30/11	<u>308,994.47</u>
Total tax and interest	\$1,422,233.49
18 Payments received	<u>628,951.17</u>
Balance Due	<u>\$ 793,282.32</u>
19	
20 Monthly interest beginning 5/1/11	<u>\$2,825.01</u>

**UNRESOLVED ISSUE**

22 **Issue:** Whether petitioner’s sales of Guardian Protection Plan Kits are sales of tangible  
23 personal property, the gross receipts of which are subject to sales tax. We conclude that they are.

24 Petitioner sells furniture, mattresses, and home entertainment units. Petitioner gives purchasers  
25 of new furniture the option of also purchasing a “Guardian 1 Plan Kit” (kit) issued by Guardian  
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27 <sup>1</sup> The Sales and Use Tax Department notified petitioner of both of these increases, pursuant to Revenue and Taxation Code  
28 section 6563, by letters dated July 18, 2008, and October 4, 2010.

1 Protection Products, Inc. (Guardian), which includes Guardian cleaners, shampoos, conditioners,  
2 polishes, and other furniture maintenance products for application to the new furniture. The kits are  
3 not offered for sale without a purchase of qualifying furniture. The kits also include a warranty plan  
4 where, subject to certain conditions and exclusions, Guardian agrees to repair or replace Plan-covered  
5 furniture when damaged by a covered occurrence. When purchasers purchase kits for fabric-  
6 upholstered furniture, petitioner applies a Guardian-supplied protectant to the new fabric-upholstered  
7 furniture prior to its delivery to the purchaser, while for leather, vinyl, and wood furniture, purchasers  
8 themselves must initially apply the products included in the kits. After the initial treatment (whether  
9 performed by petitioner or the purchaser), purchasers must thereafter re-apply the Guardian  
10 maintenance products to the furniture every 90 days to ensure warranty coverage. Petitioner is  
11 obligated to assist Guardian in obtaining replacement furniture and parts, and provide such furniture  
12 and parts to Guardian at petitioner's wholesale cost. Petitioner sells the kits for ten percent of the sales  
13 price of the furniture item(s) to be covered, subject to a \$70 minimum charge and limited to furniture  
14 sales invoices up to \$15,000 (equal to a \$1,500 maximum charge). Guardian charges petitioner \$36 for  
15 each kit, provides fabric protectant to petitioner at no charge, and does not collect sales tax  
16 reimbursement or use tax from petitioner. During the audit period, petitioner received \$6,170,485 for  
17 its sales of the kits, none of which petitioner reported on its sales and use tax returns because it  
18 concluded that such receipts were for optional warranties.

19 The Sales and Use Tax Department (Department) determined that 60 percent of the kit sales  
20 receipts, or \$3,702,291, was for petitioner's sales of kits for new fabric-upholstered furniture and  
21 40 percent, or \$2,468,194, was for petitioner's sales of kits for new furniture constructed of non-fabric  
22 materials (i.e., leather, vinyl, or wood). In the audit, the Department estimated that 25 percent of the  
23 \$3,702,291 kit sales receipts for fabric-upholstered furniture, or \$925,573, represented taxable  
24 fabrication labor for applying protectant to new fabric-upholstered furniture. Later, the Department  
25 concluded that the entire \$3,702,291 kit sales receipts for fabric-upholstered furniture was includable  
26 in the measure of tax, and it prepared a reaudit that increased the measure of tax by \$2,776,717, to  
27 \$3,702,290, for this audit item. Based on our conclusion in the D&R upholding the Department's  
28 determination because all petitioner's sales receipts for the kits were subject to sales tax regardless of

1 the type of furniture, the Department prepared a second reaudit increasing the measure of tax by  
2 \$2,468,195, to \$6,170,485, which increase it asserted by letter pursuant Revenue and Taxation Code  
3 section 6563.

4 On appeal, petitioner contends that the kits are optional warranties which represent intangible  
5 personal property; that the true object of the kit transactions is Guardian's promise to repair or replace  
6 furniture and not the application of the protectant to the furniture, the protectant's special properties, or  
7 the products in the kits; and that any tangible personal property transferred to the purchasers in  
8 connection with its sales of the kits is merely incidental to the performance of a warranty contract.  
9 Petitioner has cited the Board's pamphlet 119 (*Sales Tax and Warranties*), which provides that  
10 separate charges for optional warranties are generally not taxable. Petitioner contends that it did not  
11 fabricate or finish new furniture when it applied the protectant because the furniture was previously  
12 fully functional, and that the purchasers received no added benefits from petitioner's application of the  
13 protectant because the furniture would nevertheless be covered by the warranty.

14 In its Request for Reconsideration (RFR), petitioner objects to the finding in the D&R that the  
15 entire warranty charge subject to tax whether it is the minimum \$70 or the maximum \$1,500 charge,  
16 even though the kits provided for those widely varying charges are identical. Petitioner also contends  
17 that the D&R's comparison of its warranty with those provided by The Club and Kryptonite bicycle  
18 locks is misplaced because those warranties are "fundamentally different" from the Guardian Kit  
19 warranty. In addition, petitioner asserts that any tax due on the transactions at issue should be a sales  
20 tax owed by the vendor because petitioner did not provide a resale certificate to the vendor.

21 There is no dispute that a purchaser could purchase the furniture without also purchasing the  
22 Guardian kit. Thus, the charge for the kits was not taxable as part of the sale of the furniture, and must  
23 instead be examined separately to determine if the charge was for the sale of tangible personal property  
24 or merely for service.<sup>2</sup> However, contrary to petitioner's argument, the warranty at issue here was

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26 <sup>2</sup> For example, where a seller of a product offers a pure warranty involving no fabrication or tangible personal property, the  
27 charge is part of the sale of the warranted property if the purchaser cannot purchase that property without also purchasing  
28 the warranty. If so and if the sale of the property is taxable, the measure of tax includes the charge for the warranty.  
However, if the purchaser can purchase the tangible personal property without also purchasing the warranty, then that  
warranty is optional and the charge for it is not taxable.

1 mandatory. That is, petitioner purchased the products in the kits (i.e., tangible personal property) from  
2 Guardian for resale and then sold those kits at retail. The subject warranty was included with, and  
3 could not be obtained without, purchase of the kit. Furthermore, that warranty was conditioned on the  
4 purchasers' regular application of the products purchased in the kits. That is, to obtain and maintain  
5 the Guardian coverage, a purchaser not only had to purchase the kit, but also had to use that tangible  
6 personal property on a regular basis to protect the covered furniture. In other words, the purchasers  
7 purchased tangible personal property that was warranted to work as promised (to protect furniture from  
8 damage).

9 We reject petitioner's contention that the warranties with The Club and Kryptonite locks are  
10 somehow fundamentally different than the warranty with the Guardian kit. These products are devices  
11 to deter theft of something other than the warranted device (i.e., the warranty is that they will work as  
12 advertised to protect the locked vehicle or bicycle from theft), and each warranty provides for  
13 reimbursement to the purchaser for certain amounts of loss in the event of a theft when the device is  
14 used as directed. That is virtually identical to the situation here. The kit contains products intended to  
15 protect other property, furniture, and is accompanied by a warranty that the products will protect the  
16 furniture when applied as directed, and if not, the furniture will be repaired or replaced. When retail  
17 sales of The Club or Kryptonite locks are made in California, sales tax applies, with no deduction for  
18 the warranty that is included as part of the purchase price. The same result is applicable here.

19 We note that the fact petitioner sold the identical kit for prices ranging from \$70 to \$1,500 is  
20 wholly irrelevant. It does not appear that, except for marketing, petitioner added any significant value  
21 to the products it purchased from Guardian for resale to explain why petitioner could charge a price  
22 ranging from \$70 to \$1,500 when it paid the same amount to Guardian for each such kit, nor does  
23 petitioner bear the risk of loss for claims. As noted, Guardian, who created and produced the kit and  
24 who bore the risk of loss for claims (whether for a piece of furniture sold for \$500 or for \$15,000),  
25 charged petitioner the same price for each kit regardless of how much petitioner charged for the  
26 furniture sold with the kit. That is, Guardian determined that its \$36 per unit charge to petitioner  
27 adequately covered its cost of the product, warranty, and profit. While petitioner has every right to set  
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1 its prices in any fashion it wishes, the fact that petitioner was able to sell the kits it purchased for \$36  
2 for up to \$1,500 does not provide any basis for a deduction from the taxable measure.

3 Finally, we reject petitioner’s argument that Guardian is liable for sales tax because petitioner  
4 did not issue a resale certificate to Guardian. Whether or not petitioner had issued a resale certificate  
5 to Guardian, we conclude that petitioner made retail sales of tangible personal property, and petitioner  
6 is thus the person liable for the sales tax on those sales.

7 **OTHER DEVELOPMENTS**

8 None.

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10 Summary prepared by Pete Lee, Business Taxes Specialist II