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No. 91/68

September 27, 1991

TO COUNTY ASSESSORS:

INVENTORY EXEMPTION FOR LINEN RENTALS

In our letter to assessors 80/69, on page 14, section F, question 2, we provided the following advice:

"Are linen supplies that are leased to customers eligible for the business inventory exemption?"

"Answer: Yes, if not out on lease on the lien date."

This answer is based on California Revenue and Taxation Code Section 129 which states in part:

"'Business inventories' shall include goods intended for sale or lease in the ordinary course of business"

"'Business inventories' shall not include any goods actually leased or rented on the lien date"

In separate letters to the Monterey County Assessor (May 1990) and the Sacramento County Assessor (June 1990), we advised that if a supply of linen stock is "committed" to service a lease, the linens would be "out on lease" and none of the committed stock would be eligible for the business inventory exemption. This would apply regardless of whether the lessee or lessor has possession of the linens. Although these letters were written to individual assessors, they have apparently been given wide distribution.

After further consultation with our legal staff, we have reviewed the position we took in the letters to Monterey and Sacramento Counties and believe it should be clarified.

A typical contract for linen service specifies an initial quantity of linens to be delivered to the customer (lessee). Depending on actual usage and seasonal demands, the quantity of linens held by the customer may be adjusted up or down from the original contract amount.

Pursuant to the contract, the lessor periodically, as often as daily, exchanges clean linens for soiled linens. The customer always has possession of a specific supply of linens, which consists of clean linens, soiled linens, and linens in use. The lessor has an obligation to replace soiled linens with clean linens on a periodic basis.

The typical contract does not require the lessor to maintain any supply of linens beyond the linens actually in the customer's possession, so the number of linens kept by the lessor is entirely at the discretion of the lessor.

It is Board staff's opinion that:

1. Linens in the possession of the lessee or renter are not eligible for the inventory exemption, regardless of the quantity of linens specified by the contract.
2. If the lessee has a contractual right to a specific quantity of linens, and under the contract has a right to control the use of the linens, the specified quantity of linens is not eligible for the inventory exemption. The quantity of linens specified would be committed to lease.
3. If the lessee has a contractual right to specific linens, and under the contract has a right to control the use of the linens, the specified linens are not eligible for the inventory exemption. The specified linens would be committed to lease.

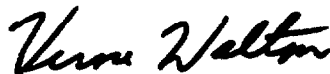
Except for the circumstances described above, linens held for sale or lease in the ordinary course of business would normally include linens held by the lessor which are intended to be exchanged for linens held by the lessee on the lien date.

The example given in the Sacramento letter involved a restaurant with one tablecloth on the table, two other tablecloths on the restaurant premises, and the linen supply company has three other tablecloths either en route or at the linen plant. The letter to Monterey County covered a similar circumstance.

The conclusion in the letters to Sacramento and Monterey Counties did not consider the contract terms between lessor and lessee. It would be inappropriate to rely on these letters to Sacramento and Monterey Counties since the conclusions reached in those letters were not based on all relevant facts.

If you have any questions or comments on this matter, please contact our Business Property Technical Services Unit at (916) 445-4982.

Sincerely,



Verne Walton, Chief
Assessment Standards Division

VW:sk