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No. 2007/019

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TO COUNTY ASSESSORS:

APPLICABILITY OF THE BUSINESS INVENTORY EXEMPTION TO  
TOMATO PASTE BINS OR DRUMS

Business inventories exempt from property taxation include "goods intended for sale or lease in the ordinary course of business."<sup>1</sup> Property Tax Rule 133 specifies that business inventories eligible for exemption from taxation include "[c]ontainers or container material such as kegs, bottles, cases, twine and wrapping paper, whether returnable or not, if title thereto will pass to the purchaser or lessee of the product to be sold or leased therein." Thus, to qualify as exempt business inventory, packaging material must be considered a container and title to the container must pass to the purchaser or lessee of the product.

Further guidance is provided in Letter To Assessors 83/59, *Applicability of the Business Inventory Exemption to Returnable Containers, and Definition of Containers and Container Materials*, May 10, 1983, which provides that:

Rule 133 does not offer any examples of items which are not to be classified as containers. However, the limited description of containers and container materials offered in the rule – kegs, bottles, cases, twine, and wrapping paper – should be considered indicative as to the types of containers that are eligible for the inventory exemption, namely, packaging materials that hold, enclose, or include products.

Most pallets and rigid delivery cases are portable platforms that are used to transport products from one location to another. A carton (container) of products may be loaded onto a pallet at the time of manufacture, but the carton is likely to be removed from the original pallet and loaded onto other pallets during the various phases of manufacture, storage, transportation, and distribution. Since the primary use of pallets and rigid delivery cases is to facilitate transportation and handling of groups of products rather than containment of products as Rule 133 contemplates, such items are not normally containers within the meaning of the rule.

<sup>1</sup> Revenue and Taxation Code section 129.

Pallets and rigid delivery cases can be containers, however. Bricks, concrete blocks, and other masonry items are commonly placed on pallets (are not otherwise contained by packaging materials) at the time of manufacture and stay on those pallets until they are "consumed" by the bricklayer. When used in this manner, the pallet or delivery case is the primary container of the products and therefore is eligible for the inventory exemption if title to the container passes to the purchaser of the product.

Thus, pallets and rigid delivery cases are not generally considered containers when their primary purpose is to transport groups of already contained products, or when products are likely to be moved from pallet to pallet (or case to case) between the time the manufacturing process is finished and the time that product is used or consumed by the purchaser of the product. However, pallets and rigid delivery cases can be considered "containers" eligible for exemption when the products that they hold, enclose, or contain are placed on or in the pallets or rigid delivery cases at the time of manufacture and are not removed until the products are ready to be used or consumed by the purchaser.

As to tomato paste bins or drums, it appears that:

- 300-gallon foil bags, weighing about 2,800 pounds when full, are attached to or placed in a wooden bin; or
- Smaller foil bags are placed in 55-gallon drums prior to being filled with tomato paste; and
- The foil bags are not removed from the bin or drum until the tomato paste is ready to be used by the purchaser of the paste; and
- Moving the foil bags without the support and protection provided by the bins or drums would subject the foil bags to a significant risk of puncture or damage.

Under these circumstances, we consider that a bin or drum is part of the container of the tomato paste, and is eligible for exemption from taxation if title to the bins passes to the purchaser.

Bins and drums that qualify as containers of tomato paste are nevertheless subject to taxation unless they are held for sale or lease in the ordinary course of business; that is, unless title to the bins passes to the purchaser of the tomato paste.<sup>2</sup> Letter To Assessors 83/59 provides additional guidance regarding the determination of whether title to a returnable or reusable container passes to the purchaser or lessee. The factors to be considered include:

- Title transfer provisions contained in a written contract;
- Deposit amount compared to the cost or value of the containers;
- Inclusion of sales tax reimbursement, where applicable;
- Distinctive markings on or construction of the container;

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<sup>2</sup> Property Tax Rule 133.

- Seller's method of accounting for the containers; and
- Conditions imposed on the return of the container.
- Actual business practice regarding return and re-use of containers.

The determination of title transfer will require a fact-specific analysis on a case-by-case basis. Thus, whether any particular tomato paste bins or drums, even if they are considered containers, would qualify for the business inventory exemption would depend on the analysis of the transfer of title, in conjunction with actual business practice consistent with transfer of title language.

Please contact our Technical Services Unit at 916-445-4982 if you have questions regarding this letter.

Sincerely,

/s/David J. Gau

David J. Gau  
Deputy Director  
Property and Special Taxes Department

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