



STATE BOARD OF EQUALIZATION  
PROPERTY AND SPECIAL TAXES DEPARTMENT  
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No. 2014/004

January 8, 2014

TO COUNTY ASSESSORS AND INTERESTED PARTIES:

**PROPERTY TAX RULE 133,  
BUSINESS INVENTORY EXEMPTION**

A project has been initiated to discuss proposed revisions to Property Tax Rule 133, *Business Inventory Exemption*. This project has been prompted by inquiries as to whether the business inventory exemption applies to certain space flight property regulated under the Arms Export Control Act (AECA)<sup>1</sup> and the International Traffic in Arms Regulations (ITAR).<sup>2</sup>

The State Board of Equalization's legal staff has recently opined that within the context of that federal statutory and regulatory scheme, contracts and business practices that demonstrate that space flight property to which control is relinquished at launch qualifies for the business inventory exemption. The opinion may be viewed at [www.boe.ca.gov/proptaxes/ptr133.htm](http://www.boe.ca.gov/proptaxes/ptr133.htm).

Enclosed is a draft of Rule 133 with proposed revisions. Interested parties are encouraged to review the suggested revisions and submit any comments/suggestions regarding the draft to Ms. Sherrie Kinkle at [sherrie.kinkle@boe.ca.gov](mailto:sherrie.kinkle@boe.ca.gov), or mailed to the above address, by January 31, 2014. Upon reviewing comments submitted, it is anticipated that this project will proceed as follows:

- If necessary, staff will meet with interested parties on February 6, 2014 to discuss any comments received. The meeting is scheduled to start at 10 a.m. in Room 122, Board of Equalization Headquarters, 450 N Street, Sacramento.
- If necessary, staff will further revise the rule to address relevant comments.
- Staff will then bring the revised rule before the Board to request approval to publish amendments to Rule 133 and begin the formal rulemaking process to adopt the proposed revisions.

All documents regarding this project will be posted on the BOE website at [www.boe.ca.gov/proptaxes/ptr133.htm](http://www.boe.ca.gov/proptaxes/ptr133.htm). If you have questions regarding this project, you may contact Ms. Kinkle at 1-916-274-3363.

Sincerely,

/s/ John K. Thompson for

David J. Gau  
Deputy Director  
Property and Special Taxes Department

DJG:sk

Enclosure

<sup>1</sup> 22 U.S.C., section 2778.

<sup>2</sup> 22 C.F.R., sections 120-130.

**RULE 133. BUSINESS INVENTORY EXEMPTION.**

*Authority Cited:* Section 15606, Government Code.  
*Reference:* Sections 129 and 219, Revenue and Taxation Code.

**(a) SCOPE OF EXEMPTION.**

(1) "Business inventories" that are eligible for exemption from taxation under Section 129 of the Revenue and Taxation Code include all tangible personal property, whether raw materials, work in process or finished goods, which will become a part of or are themselves items of personalty held for sale or lease in the ordinary course of business.

(A) The phrase "ordinary course of business" does not constitute a limitation on the type of property which may be held for sale or lease, but it does require that the property be intended for sale or lease in accordance with the regular and usual practice and method of the business of the vendor or lessor.

(B) The phrase "goods intended for sale or lease" means property acquired, manufactured, produced, processed, raised or grown which is already the subject of a contract of sale or which is held and openly offered for sale or lease or will be so held and offered for sale or lease at the time it becomes a marketable product. Property which is ready for sale or lease must be displayed, advertised or otherwise brought to the attention of the potential purchasers or lessees by means normally employed by vendors or lessors of the product.

(2) "Business inventories" includes:

(A) Containers 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.

(B) New and used oak barrels used in the manufacturing process that physically incorporate the flavor- and aroma-enhancing chemical compounds of the oak into wine or brandy to be sold, when used for this purpose. However, an oak barrel is no longer business inventory once it loses the ability to impart the chemical compounds that enhance the flavor and aroma of the wine or brandy. An "oak barrel" used in the manufacturing process is defined as having a capacity of 212 gallons or less. Oak barrels not used in the manufacturing process but held for sale in the ordinary course of business are also considered business inventory.

(C) Materials such as lumber, cement, nails, steel beams, columns, girders, etc., held by a licensed contractor for incorporation into real property, providing the real property will not be retained for the licensed contractor's use.

(D) Crops and animals held primarily for sale or lease and animals used in the production of food or fiber and feed for animals in either category.

(E) Space flight property listed in the International Traffic in Arms Regulations (22 CFR section 121.1) as a defense article on the United States Munitions List, the control over which is relinquished by the owner upon launch. "Space flight" means any flight designed for suborbital, orbital, or interplanetary travel by a space vehicle, satellite, space facility, or space station of any kind.

**(b) EXCLUSIONS.** Property eligible for the "business inventories" exemption does not include:

(1) Property of any description in the hands of a vendee, lessee or other recipient on the lien date which has been purchased, leased, rented, or borrowed primarily for use by the vendee,

lessee or other recipient of the property rather than for sale or lease or for physical incorporation into a product which is to be sold or leased. Examples of property excluded from business inventories are office supplies, furniture, machines and equipment and manufacturing machinery, equipment and supplies such as dies, patterns, jigs, tooling or chemicals used to produce a chemical or physical reaction, and contractors' supplies, tools, concrete forms, and other items that will not be incorporated into and become a part of the property. Also ineligible are materials that a contractor is holding to incorporate into real property that will be retained for his own use.

(2) Property being used by its owner for any purpose not directly associated with the prospective sale or lease of that property.

(3) Property actually leased or rented on the lien date.

(4) Property which has been used by the holder prior to the lien date, even though held for lease on the lien date.

(5) Property intended to be used by the lessor after being leased or during intervals between leases even though held for lease on the lien date.

(6) Property in the hands of a lessor who, with intent to enjoy the benefits of the inventory exemption, had leased the property for a period that expired shortly before the lien date but who renewed, extended or renegotiated the lease shortly thereafter.

**(c) SERVICE ENTERPRISES.** Property held by a person in connection with a profession which is primarily a service activity such as medicine, law, architecture or accountancy is not "business inventories" held for sale or lease even though such property may be transferred to a patient or client incidental to the rendition of the professional service. Property held by enterprises rendering services of a nonprofessional type such as dry cleaners, beauty shop operators and swimming pool service companies is to be regarded as "business inventories" held for sale if such property is delivered as an item regularly included in the service.

**(d) REPAIRERS AND RECONDITIONERS.** Persons engaged in repairing or reconditioning tangible personal property with the intent of transferring parts and materials shall be regarded as holding said parts and materials as "business inventories."

**(e) AGRICULTURAL ENTERPRISES.** Animals, crops and feed held primarily for sale or lease in the ordinary course of business are included in the term "business inventories," as are animals used in the production of food or fiber and feed for such animals.

(1) "Animals used in the production of food and fiber" includes all animals customarily employed in the raising of crops or for the feeding, breeding and management of livestock, or for dairying, or any other confined animals whose products are normally used as food for human consumption or for the production of fiber useful to man. Excluded are animals held by an owner or lessee principally for sport, recreation or pleasure such as show animals, horses kept for racing or horses and other animals kept as pets.

(2) The term "crops" means all products grown, harvested, and held primarily for sale, including seeds held for sale or seeds to be used in the production of a crop which is to be held primarily for sale. It does not include growing crops exempted pursuant to Article XIII, section 3 (h), of the California Constitution or fruit trees, nut trees, and grapevines exempted by section 223 of the Revenue and Taxation Code.

(3) The term "food" means property normally considered as food for human consumption.

(4) Feed for animals held primarily for sale or lease or for animals used in the production of food or fiber constitutes "business inventories" subject to exemption. It includes every type of

natural-grown or commercial product fed to animals except medicinal commodities intended to prevent or cure disease unless the medicinal commodities are purchased as a component part of feed for such animals.

*History:* Adopted November 20, 1968, effective December 21, 1968.

Amended January 7, 1970, effective February 8, 1970.

Amended January 6, 1971, effective February 18, 1971.

Amended February 5, 1975, effective March 20, 1975.

Amended August 20, 1980, effective November 14, 1980.

Amended October 10, 1984, effective February 21, 1985.

Amended January 5, 2000, effective July 26, 2000.

Amended and effective April 6, 2001.