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**STATE BOARD OF EQUALIZATION**

December 6, 1967

Dear --- ---:

Following our discussions of the petition for redetermination filed by the above taxpayer, I have reached some conclusions which I propose to communicate to our Hollywood office with a recommendation that a reaudit be conducted. I agree with you that the facts and issues have been sufficiently developed at this point to permit this approach. Before the reaudit is begun, however, I would like to have some idea of what it may accomplish in the way of disposing of issues without further proceedings. With that objective in mind, I would like to hear from you after you have considered this letter.

1. From the standpoint of growth alone, a plant or tree should be regarded as remaining in substantially the same form unless by reason of its growth its value has increased by more than 20 percent.

The basis for this approach is as follows: Growing plants are constantly changing in form to some extent but it is particularly difficult to define a point at which the change is significant for purposes of Section 6006(g)(5) (formerly Section 6006(g)(4)). It appears reasonable to assume that one of the main purposes of taxing the rentals derived from property which is no longer in substantially the same form after tax has been paid on the cost of its acquisition is to capture tax on the increased value resulting from the change in form. I believe, therefore, that the criterion of value may appropriately be used as an indicator of the point at which a plant is no longer in substantially the same form. By drawing an analogy with our long-standing interpretation of the term "substantially" as used in Section 6006.5(b), it seems appropriate to consider a change of more than 20 percent in value as a substantial change.

2. A tree should be regarded as remaining in substantially the same form after a relatively simple base has been attached to it without extensive fabrication labor. An appropriate test is whether the value of the tree with the base is more than 20 percent of the value of the tree without the base.

3. Plants or trees should be regarded as remaining in substantially the same form even after they are arranged into a particular pattern when the arrangement is made under the direction and control of the lessee, on his premises, after the lease is entered into, and where the arrangement does not last beyond the term of the lease. The fact that a person who is normally employed by the lessor assists in making the arrangement under the direction of the lessee does not change this

result if his assistance is optional with the lessee and if the arrangement does not result in an increase in the rental rate over the usual rate for the plants and trees as separate items.

4. For the period from August 1, 1965 to April 26, 1966, rentals of plants and trees are taxable if the taxpayer has not paid tax on their cost regardless of the fact that the taxpayer acquired them in a transfer constituting an occasional sale under Section 6006.5(b) from a transferor who did pay tax on their cost.

I have thoroughly considered your arguments to the contrary. The issue is admittedly arguable and you have argued it well. The rule that I have stated is supportable, however, and it is a rule that we have applied consistently to all taxpayers in the same class. It has been announced in several rulings by the legal staff and has been published in Business Taxes General Bulletin 66-15, a copy of which is enclosed. Since the rule is supportable and has become so well established, I believe that we should adhere to it.

5. All rentals of plants or trees acquired without tax are taxable on and after August 1, 1965. (See California Tax Service, annotations 1535.25, 1536.29, and 1536.36.)

6. The taxpayer may not elect to pay tax on the cost of property acquired in an exempt transaction and thus avoid tax on rentals of the property. (See California Tax Service, annotations 1535.25, 1536.29, and 1536.36.)

For current law see Sec. 6094.1 DJH 10/20/87.
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You have stated that no allowance has been made for the period from August 1, 1965 to April 26, 1966, with respect to rentals of plants and trees acquired tax paid by the taxpayer after January 1, 1965. I will recommend that an appropriate allowance be made on reaudit, based on a reasonable allocation if necessary.

I believe that I have covered all of the issues that were raised. I am looking forward to hearing from you.

Very truly yours,

T. P. Putnam  
Tax Counsel

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