

**STATE BOARD OF EQUALIZATION**

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July 19, 1995

BURTON W. OLIVER
Executive Director

Mr. K--- H---
R. L. H--- Co.
P.O. Box XXX
---, ID XXXXX

Re: Taxability of Sprout Inhibitors
Account No. SS -- XX-XXXXXX

Dear Mr. H---:

This is in response to your letter dated May 9, 1995, in which you inquired about a product sold by your company, which is used to inhibit the growth of sprouts on harvested potatoes.

This product, Isopropyl-M-Chlorocabanilate, also known as chloroprotham or CIPC, is applied to potatoes after they have been harvested to prohibit sprouting while in storage. Your inquiry is whether sales tax is due on sales of this chemical to growers.

Sales tax is imposed on all retailers measured by their gross receipts from retail sales of tangible personal property occurring in this state. (Rev. & Tax. Code § 6051.) When sales tax does not apply, use tax applies to the use of property purchased from a retailer for use in California. (Rev. & Tax. Code §§ 6201, 6401.) A retail sale is a sale for any purpose other than resale in the regular course of business. (Rev. & Tax. Code § 6007.) Your sales are presumed to be taxable retail sales unless you take in good faith from the purchaser a timely and valid resale certificate. (Rev. & Tax. Code § 6091, Regulation 1668.)

The sale of tangible property is regarded as a non-taxable sale for resale when the purchased tangible property will be incorporated into the manufactured or processed article to become an ingredient or a component part of the manufactured article. The physical presence of the tangible property in the final product must produce some beneficial effect on that final product, as opposed to merely remaining in the final product after accomplishing its purpose in the manufacturing process. (Regulation 1525(b).) Tax applies to the sale of tangible personal

property purchased for use in manufacturing or processing tangible personal property and not for the purpose of physically incorporating it into the manufactured article. (Regulation 1525(a).)

One possibility here is that the chemicals are used during the storage to prevent the potatoes from sprouting, with the inhibition of sprouting to continue after the treatment even if the CIPC is physically removed after the treatment. If such is the case, I assume that the only reason that the CIPC is not removed after the treatment is that it does not present any danger to the consumer if eaten and washing off this chemical would mean an unnecessary and costly step. The opinion of the Court in Kaiser Steel Corp. v. State Board of Equalization (1979) 24 Cal.3d 188 is helpful in this respect. In Kaiser Steel, the Court held that “chemicals used as catalyst or otherwise to produce a chemical or physical reaction such as the production of heat or the removal of impurities” are examples of property not purchased for the purposes of physically incorporating it into the manufactured article and, therefore, not for resale. The Court also stated that “if property is purchased as an aid in the manufacturing process, it is taxable despite the fact that some portion remains in the finished product” (Id. at 192-193.) This analysis also applies here. If the sprouting would continue to be inhibited at the time of the sale to the consumer, even if the CIPC were removed from the potatoes prior to the sale, the CIPC cannot be purchased for resale and sales tax would apply.

A second possibility is that if the CIPC were removed, the sprouting would not be inhibited. That is, the CIPC must be physically present on the potatoes at the time of the sale in order to continue inhibiting the growth of sprouts and that this is the grower's reason for applying the chemical. If this is the case, the growers are regarded as reselling the CIPC and they may purchase the CIPC extax for resale by issuing timely resale certificates. A copy of Regulation 1668, entitled “Resale Certificates,” (copy enclosed) explains your obligations when accepting a resale certificate.

I have also enclosed a copy of Regulation 1525 for your review. If you have any further questions please feel free to contact this office again.

Sincerely,

Patricia Hart Jorgensen
Senior Staff Counsel

PHJ/cmm
Enclosures

cc: Mr. Dennis Fox (MIC:40)
District Administrator (OH)