



STATE BOARD OF EQUALIZATION

November 8, 1968

Gentlemen:

You will recall that the issue presented at the hearing was whether your operations should be characterized as a service or as a lease of equipment to your customers.

At the hearing you presented a number of factual points to support your argument that you are a service and not a lessor.

It is the staff's position that the term lease is not limited to a transaction which is chiefly a financing device, nor is it necessary that a lease be for a specified period. A temporary possession for so long as both parties agree still qualifies as a lease (CC 1925).

We recognize that a large number of leasing businesses extend expensive services to their lessees during the period of the lease. Therefore, we do not believe that it is solely determinative that your business has important service elements. We have focused our attention on the fact that the equipment is attached to the customer's plumbing system, and it operates in the house under his dominion and control and beyond the continuing dominion of the petitioner. It is significant that the customer never, or very seldom, manipulates the equipment while it is attached and operating, but neither does the petitioner.

Although the matter is not entirely free from doubt, it seems to us that this fact determines the question, and we have concluded that petitioner is leasing the water softening units. Our recommendation will be that the redetermination be made without adjustments.

We are aware, and so bring to your attention, how the tax law would apply to the opposite conclusion. It is your position that the customer does not obtain possession of the softener unit on his premises and that you are providing soft water which the customer then uses. In this instance the soft water "service" is the ion exchange or deionizing of water supplied by your client's water system. We note that the water has different qualities and properties after it has been softened. Petitioner has argued that the change in the water is what the customer is paying for, that the customer is completely unconcerned with the kind of tangible personal property which may be used by the petitioner to perform the service, and that the charge is due so long as petitioner provides soft water whether he uses any equipment or none. If the petitioner is right in that it does not lease, rent, hire or license equipment to customers for their water system, then the

petitioner is processing (softening) water for its customers with its own equipment. The processing of tangible personal property would constitute a sale (§ 6006(b)) whether or not the equipment of the processor is tax paid. All the Item A type of charges would be taxable, and not just the 13.84 percent of those charges which were set up in the determination as receipts attributable to units acquired ex tax.

If you desire an oral hearing before the Board, please let us know within 30 days.

Very truly yours

Philip R. Dougherty
Tax Counsel

PRD: smk [lb]

Note: This issue is now free from doubt. Culligan (1976) 17 C 3d 86