

OSU EXTENSION

THE LEGAL AND PRACTICAL ASPECTS OF THE AGRICULTURAL SALES TAX EXEMPTION

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INTRODUCTION

Farmers have enjoyed an exemption from the Ohio and county sales tax for many years. Historically, obtaining the exemption from the sales tax was relatively simple. The farmer merely filled out a post card sized exemption form at his local agricultural retailer, checked the box that he was involved in “agriculture,” and most of his subsequent purchases from that agricultural retailer were exempt.

More recent, agricultural retailers seem increasingly reluctant to give farmers the agricultural exemption. Numerous questions have arisen regarding why sales tax is being charged on certain items of tangible personal property that the farmer feels should be exempt.

Much has already been written on the subject of the agricultural exemption from sales tax. For a good overview of the agricultural sales tax exemption, see OCES Bulletin 761, written by Paul L. Wright, Douglas E. Sassen, and Nan M. Still, (November 1987), and Fact Sheet OAM-2-12, written by Chris Bruynis, PhD (2012). Both of these documents remain good resources.

However, to fully understand why sales tax is now being charged on items that once appeared to be exempt, one must delve deeper into the Ohio law and its practical application to purchases. The Ohio Revised Code, the Ohio Administrative Code, legal cases that further interpret those codes, the Ohio Department of Taxation, and the sales tax collection process all have a bearing on the agricultural exemption from sales tax.

ALL SALES BEGIN AS TAXABLE

Initially, all sales are taxable. Ohio Revised Code section 5739.02 states: “. . . an excise tax is hereby levied on each retail sale made in this state.” ORC sec. 5739.02(C) expands this requirement by stating: “(C) For the purpose of the proper administration of this chapter, and to prevent the evasion of the tax, it is presumed that all sales made in this state are subject to the tax until the contrary is established.” The effect of this statement is to place the burden of proving that a sale is exempt on the purchaser. As a general legal principle, exemptions from tax are narrowly construed.

HOW DO SALES BECOME NON-TAXABLE?

There are two ways that sales become non-taxable. One way is for a sale to be “excepted” from the definition of a sale by statute. The other way is for a sale to be “exempted” from the sales tax requirement.

A sale is non-taxable if it is specifically excepted from the definition of a “sale.” Ohio Revised Code section 5739.01(B) provides the definition of “sale” and the act of “selling.” One can find an extensive list of transactions that are considered to be a “sale” or the act of “selling” in this section. Also contained in this list are specific exceptions for transactions that are not considered to be sales or the act of selling within the legal definition.

However, more important for our discussion, the agricultural sales tax exemption is an “exemption” from sales tax, not an “exception.” Therefore, this paper focuses on Ohio Revised Code section 5739.02 which provides a list of goods and services that are specifically exempted from the Ohio sales tax.

AGRICULTURAL SALES TAX EXEMPTIONS IN THE OHIO REVISED CODE

ORC section 5739.02(B) provides a list of 53 items that are specifically exempted from the Ohio sales tax. Several items apply to agriculture:

(B)(13) building and construction materials sold to construction contractors for incorporation into a horticulture structure or livestock structure for a person engaged in the business of horticulture or producing livestock. This exemption was later expanded by section (B)(36) to include sales to “persons” in addition to contractors.

(B)(30) land tile

(B)(31) portable grain bins

The subsection that applies most often to agriculture is (B)(17). This subsection states:

(B)(17) Sales to persons engaged in farming, agriculture, horticulture, or floriculture, of tangible personal property for use or consumption primarily in the production by farming, agriculture, horticulture, or floriculture of other tangible personal property for use or consumption for sale by farming, agriculture, horticulture, or floriculture; or material and parts for incorporation into any such tangible personal property for use or consumption in production; and of tangible personal property for such use or consumption in the conditioning or holding of products produced by and for such use, consumption, or sale by persons engaged in farming, agriculture, horticulture, or floriculture, except where such property is incorporated into real property.

In an attempt to better understand this subsection, let’s break it down into its requirements.

1. The sale must be made to a person engaged in farming, agriculture, horticulture, or floriculture;
2. It must be an item of tangible personal property;
3. The item of tangible personal property must be used or consumed primarily (more than 50%) in the production of another item of tangible personal property that will eventually be sold;
4. The item can be material or parts incorporated into tangible personal property for use or consumption in farming;

5. The item can be for use or consumption in the conditioning or holding of products produced by a person involved in farming, agriculture, horticulture, or floriculture, for further use, consumption, or sale, EXCEPT where such item is incorporated into real property.

THE OHIO ADMINISTRATIVE CODE PROVIDES FURTHER CLARIFICATION

The Ohio Revised Code contains the laws passed by the Ohio General Assembly. In contrast, the Ohio Administrative Code contains the rules that agencies use to implement those laws. The rules in the Ohio Administrative Code are promulgated by the agency that is responsible to administer the program and those rules are then reviewed and approved by another agency called the Joint Committee on Agency Rule Review.

Ohio Administrative Code (OAC) rules have a more direct impact on the agricultural sales tax exemption because they are promulgated by the Ohio Department of Taxation and serve as the guidelines for collecting the sales tax.

OAC section 5703-9-23 expands the agricultural sales tax exemption provided in the Ohio Revised Code. This section first provides the definitions for “farming”, “agriculture”, “horticulture”, and “floriculture.” “Farming” is defined as the occupation of tilling the soil for the production of crops as a business and shall include the raising of farm livestock, bees, or poultry, where the purpose is to sell such livestock, bees, or poultry, or the products thereof as a business. “Agriculture” is defined as the cultivation of the soil for the purpose of producing vegetables and fruits and includes gardening and horticulture, together with the feeding and raising of cattle or stock for sale as a business.

Note that the definitions of “farming” and “agriculture” include tilling the soil and cultivation of the soil. Therefore, taking all of the requirements together, the agricultural sales tax exemption has been allowed only for those items that are used directly and primarily in the tilling or cultivation of the soil, used in the propagation of plants, or the care and raising of livestock. Timber is not included, nor is a utility vehicle or a chain saw if the technical definition is strictly followed.

OAC section 5703-9-23 further expands what “sales” are tax-exempt. Most of those sales are items that are incorporated into, or used or consumed, producing other tangible personal property for sale.

OAC section 5703-9-23 concludes with three very important statements:

1. Exemptions do not apply to any article which is incorporated into real property
2. The tax or non-tax of a sale is determined by the use of the item sold. An article of tangible personal property that appears to be agricultural in nature must also be used for a non-taxable purpose. For example, a pitch fork used in my barn may be tax-exempt, but taxable if primarily used in my garden.

3. Sales of materials such as lumber, nails, glass and similar items to be used in the construction or repair of buildings shall be subject to the tax.

CASE LAW PROVIDES THE FINAL DETERMINATION

Even with the foregoing analysis of the laws and rules, it is impossible to list every item of tangible personal property that is exempt from sales tax. Certain items are clearly used in agriculture and are exempt. On the other hand, some items are clearly not exempt. Some items fall somewhere in the middle and are difficult to tell whether they are tax-exempt, either because the item is used for a personal use a majority of the time or the items could be used for a taxable purpose.

Occasionally, courts are asked to determine the taxability of a particular item. This is most often seen where the resulting sales tax is large enough to warrant spending the money to go to court, such as a manufacturer that is going to produce or purchase mass quantities of that item. Individuals rarely can warrant going to court over a sales tax dispute.

THE PRACTICAL ASPECTS OF THE AGRICULTURAL SALES TAX EXEMPTION

Armed with the best legal information, a farmer may firmly believe that the item he is purchasing should be tax-exempt. However, the cash register rings up that the sale as taxable. Does he have to pay the sales tax? Yes, from a practical standpoint. There are two ways to look at each situation – the legal way and the practical way. From a practical point of view, the farmer may still have to pay the sales tax at the cash register even though he feels that the item is tax-exempt. However, if the farmer is erroneously required to pay the sales tax, he/she must file an application for a refund (ST-AR form) with the Ohio Department of Taxation.

Let's take a closer look at the collection process. Both ORC section 5739.02(C) and OAC section 5703-9-03 state that all sales are presumed to be taxable until the contrary is established. Each vendor is required to collect from the consumer, as a trustee of the State, the full and exact amount of the tax payable on each taxable sale. To be tax-exempt, the farmer must provide to the vendor a fully completed exemption certificate. The vendor is required to keep this exemption certificate on file.

In discussions with some local retailers, I discovered that one large agricultural retailer receives a list of taxable and non-taxable items from its corporate office and the local store is required to collect the sales tax according to the list, notwithstanding the identity of the purchaser. Conversely, the local tractor store determines in-house which items are taxable or non-taxable and for items that may go either way, the store gives the exemption if the purchaser has a tax-exempt form on file. For other large retailers without an agricultural base, they do not recognize the agricultural sales tax exemption.

Exemption forms are available on the Ohio Department of Taxation’s website and may be reproduced. The farmer should use form STEC-U for a unit exemption or STEC-B for a blanket exemption if he is going to purchase numerous items from that vendor. If the farmer wants a refund of sales tax that he feels is erroneously paid, he should file form STAR with the Ohio Department of Taxation. Rather than receiving a cash refund of the sales tax erroneously paid, the farmer may apply the refund to any indebtedness that he owes the State, for example, income tax.

EXEMPTION CERTIFICATES

As previously mentioned, exemption forms may be obtained from the Ohio Department of Taxation website. OAC section 5703-9-03(D) states that: “An exemption certificate is fully completed if it contains the following data elements:

- (1) The purchaser’s name and business address,
- (2) A tax identification (e.g. vendor’s license or consumer’s use tax account) for the purchaser issued by this state, if any,
- (3) The purchaser’s type of business or organization,
- (4) The reason for the claimed exemption, and
- (5) If the certificate is in hard copy, the signature of the purchaser.

If any of these elements is missing the exemption certificate is invalid.”

There has been some confusion recently caused by some agriculture retailers advising farmers that if they want the sales tax exemption, the farmer needs to go to the county courthouse and obtain a vendor’s license. This is not correct. The retailer is trying to comply with the requirement found in subsection (D)(2) above where it states that the exemption certificate requires a tax identification number. However, the retailer’s advice ignores the last two words of that section – “if any.” Farmers are not required to obtain a vendor’s license because they do not sell at retail. I recommend that the farmer write “none required” or “not applicable” on the exemption form where it requests a tax identification number. Of course, then the farmer is burdened with explaining to the cash register attendee that a vendor’s license number is not required. Good luck with that.

ULTIMATE LIABILITY FOR SALES TAX

Many farmers believe that if they give a tax exemption form to the retailer, the farmer should not be ultimately responsible for the sales tax. However, both the purchaser and the vendor may ultimately be liable for the tax. Initially, the purchaser is responsible to pay the sales tax to the vendor. If the purchaser claims that the sale is non-taxable, he/she must provide an exemption certificate to the vendor specifying the reason that the sale is non-taxable (ORC 5739.03(A)).

A vendor that obtains a fully completed exemption certificate from a purchaser is initially relieved of liability for collecting and remitting tax on any sale covered by that certificate. If it is later determined that the exemption was improperly claimed, ORC section 5739.03(B)(1)(b) makes the purchaser liable for any tax due on that sale.

If a vendor improperly fails to collect the sales tax, another section of the ORC makes either the purchaser OR the vendor personally liable for the sales tax. ORC section 5739.13 says that the tax commissioner may make an assessment against either the vendor or the purchaser as the facts require. An assessment against a vendor when the tax has not been collected shall not discharge the purchaser's liability to reimburse the vendor for the tax. From a practical standpoint, the vendor would have to take steps to collect the unpaid tax from the purchaser.

To put additional pressure on a vendor to collect and remit the sales tax, ORC section 5739.33 states that if any vendor required to file (sales tax) returns for any reason fails to file the return or remit payment, any employee having control or supervision over the filing of returns and making payments, or any officer, member, manager, or trustee who is responsible for the vendor's fiscal responsibilities shall be personally responsible. The amount due may be assessed against that person.

Because of this liability exposure, from both a corporate and personal standpoint, it is my opinion that the vendor is going to err on the side of collecting the sales tax if it is not clear that the item is non-taxable.

CONCLUSION

Even though it may appear from a legal standpoint that the purchase of an item should be tax-exempt, without a complete list of what items are taxable and non-taxable from the Ohio Department of Taxation, there is still room for confusion. The vendor initially determines whether the item is non-taxable at the cash register. The purchaser needs to provide a tax-exemption certificate to the vendor to receive the sales tax exemption. If the vendor collects sales tax on an item that the farmer feels is tax-exempt, the farmer should file a request for a refund with the Ohio Department of Taxation.