June 2, 2014

Tax Clarification resulting from HOUSE BILL 1050

In 2013 the General Assembly passed changes to tax law that became effective January 1, 2014. These changes created questions as to how some farms may become subject to an expanded sales tax base or not on products they sell, as well as, qualifying for sales tax exemption on farm inputs. House Bill 1050, passed by the General Assembly and signed by the Governor on May 29, 2014 provides clarification to some of these questions.

Sales and Use Tax: Collection and Remittance by Farmers on product sales

A farmer selling raised products (products the farmer grew or raised him/herself) from a farm road-side stand or at a farmer's market is NOT REQUIRED to collect and remit sales tax to the North Carolina Department of Revenue. The key is that the product is in the "original state" when sold.

Example

In most cases if there is any "value added" done to a product (e.g. selling cuts of meat) the seller must collect and remit sales tax. The example below uses the sweet potato:

a) If the sweet potato is sold by the farmer with the dirt still on the potato that is a sale of product in the original state and NO SALES TAX is charged, collected or remitted. This has been in place for years and still is in place.

b) If the sweet potato is purchased by another vendor and is resold by this second vendor, then 2% sales tax as a food item must be collected and remitted.

c) If the sweet potato is made into a pie and then sold at the farmer's market, the pie is subject to 2% sales tax as a food item and sales tax must be collected and remitted.

d) If the sweet potato pie is cut and a slice is placed on a plate with a fork and sold, the slice of pie is subject to 4.75% state sales tax PLUS local sales tax as a prepared food (think restaurant) item and sales tax must be collected and remitted.

As of January 1, 2014, there is a requirement that the farmer attests that the products sold by the farmer, at the farmer's market, are his/her own production. The North Carolina Department of Revenue (NCDOR) provided guidance through Directive on February 28, 2014 which requires that a statement of attestation is to be given to the manager/operator of the farmer's market. The NCDOR link is below.

http://www.dornc.com/press/2014/specialty.html

Sales and Use Tax: Sales tax exempt purchase of farming inputs

Clarification in HB 1050 provides that farmers, in order to purchase farm inputs exempt from sales tax, must have $10,000 of gross farm income from the <u>preceding tax year</u> in order to qualify for the exemption or $10,000 of gross farm income as an average of the preceding 3 taxable years. This may affect operators of small farms as gross farm income may be variable due to weather conditions.

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Further, HB 1050 allows for a **Conditional Exemption**. The conditional exemption is useful to beginning farmers who have no history of farm production. To receive a conditional exemption, the beginning farmer must certify they intend to engage in farming. The conditional exemption certificate is valid for the taxable year in which it is issued and the two subsequent years. The holder of the conditional certificate must provide the NCDOR copies of applicable State and Federal income tax returns within 90 days of the end of each tax year the certificate covers.

NCDOR is to issue guidance as to how to obtain a new exemption certificate.

Misuse of the Exemption Certificate is subject to a $250.00 fine.

THIS INCOME THRESHOLD IS NOT TO BE CONFUSED with the $1,000 of agricultural product produced as an average, over 3 years, for property tax purposes to qualify for Present Use Value program.

Sales and Use Tax: NEW agricultural exemption certificate to be required

HB 1050 provides that qualifying farmers who have an agricultural exemption certificate number issued prior to July 1, 2014 should apply for a new agricultural exemption certificate before July 1, 2014.

NCDOR is to issue guidance as to how to obtain a new exemption certificate.

Holders of agricultural exemption certificate numbers issued prior to July 1, 2014 may continue to use these certificate numbers on qualifying purchases made prior to October 1, 2014. If, however, the exemption certificate is not valid, the holder must notify vendors and pay sales tax on now none qualifying purchases.

Bottom line, farmers will need new agricultural exemption certificate numbers.

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