



HB 4009: Commercial Activities Tax Technical Fixes for Oregon Agriculture

Since passage of HB 3427 and HB 2164 in the 2019 session, agricultural stakeholders have engaged with the Oregon Department of Revenue to address issues with implementation of the commercial activities tax for the agricultural sector. While temporary rules are expected to clarify some of our key concerns, we believe the following require statutory clarification to ensure permanent rules work for Oregon agriculture. Our coalition of agricultural stakeholders respectfully requests adoption of the below two technical fixes to HB 4009:

- An ag-specific definition for ‘cost inputs’; and
- An apportionment certificate for comingled bulk commodities.

Cost Inputs and the Cost of Goods Sold

In the 2019 legislative session, agricultural stakeholders raised concerns about the calculation of ‘cost inputs’ for the purposes of qualifying for the 35% subtraction from tax liability under Oregon’s commercial activity tax (CAT). “Cost inputs” are defined in HB 2164 (2019), the CAT technical fix, as the “cost of goods sold as calculated in arriving at federal taxable income under the Internal Revenue Code.” Unfortunately for farmers and ranchers, ‘cost of goods sold’ is a term frequently used in accrual accounting but not for agricultural businesses that typically operate on a cash basis.

The determination of ‘cost of goods sold’ is complicated for family farms. For tax purposes, most farmers are allowed to report income and expenses on a cash basis for their business and individual tax returns. This means that farmers are only required to report cash received offset by cash paid before year-end, typically December 31. In some cases, farmers wait to sell grain and cattle until after the first of the year. Meanwhile, they can prepay certain expenses such as chemical, fertilizer, and seed that won’t be used until the next growing season.

Problem: The definition of ‘cost inputs’ as ‘cost of goods sold’ under the Internal Revenue Code doesn’t fit the cash accounting model that most farmers use and doesn’t account for costs incurred to plant and grow a crop in one calendar year, when the sale of that crop or commodity is in a different calendar year.

Proposed solution: Create a ‘cost inputs’ definition that relies on existing statutory, rule and tax forms that farmers and ranchers can use instead of ‘cost of goods sold.’

- a. **RECOMMENDED LANGUAGE: ‘Cost inputs’ for agricultural businesses who are not filing a form 1125-A under section 471 of the IRC includes 35% of their expenses reported on the Schedule F, Section 179 expenses on the Schedule K, or Form 4835.**

Agricultural Resale Certificate

The comingling of commodities presents challenges when calculating tax liability for farmers and ranchers whose commodities are sold outside of Oregon. For example, three hazelnut farmers may each deliver 15 tons of hazelnuts to a marketer who subsequently ships 95% of all Willamette Valley hazelnuts out of the country. Currently, the rules provide no way of determining which nuts were exported and which nuts were sold in Oregon. As a result, farmers have no certainty with regard to their tax liability.

Problem: In order to qualify for the out-of-state sales exemption provided in HB 3427 and HB 2164 (2019), the farmer must obtain certification from the wholesaler or broker at the time of sale to show that the product is leaving the state. However, in many instances, the ultimate destination of the product at the time of sale is unknown. For growers, this presents many questions:

- How will the co-mingled commodities be taxed?
- How will this co-mingling be reflected on the certificate at time of sale?
- How can the distributor or marketer forecast where the future buyer is located?
- Can a distributor use averages as the basis of the certificate (e.g. 80% of volume went to the export market for the previous year)?
- What if the distributor or broker is unable to provide documentation as to the destination of sale at the time of the sale?

Proposed solution: Provide farmers and wholesalers with a clear and simple process to certify out-of-state sales of bulk commodities, providing clarity when a certificate is unavailable from a wholesaler, distributor or broker.

a. RECOMMENDED LANGUAGE: Provide farmers and ranchers with a two-tiered approach to determining their tax liability and apportionment for commodities. Taxpayers may choose one of two options to apportion income to determine CAT liability:

- 1. For the purposes of ORS 317A.100 (20), wholesaler includes taxpayers which process and resell agricultural commodities.**
 - i. A wholesaler purchasing bulk commodities for the purpose of resale may, at the time the purchase is made, provide the seller of the property with an out-of-state resale certificate, declaring the percent of the bulk commodity sold out of state v. in state (current year or for previous year if bulk commodities have not been sold); or**
 - ii. The seller may elect to use an “industry average” to apportion in-state versus out-of-state tax liability for bulk commodities delivered to wholesalers. DOR shall publish existing data from the Oregon Department of Agriculture and USDA agricultural census to estimate the average percent of the commodity sold outside the state in the previous tax year. (‘alternative method’ identified by DOR rules)**
 - iii. The election shall be considered timely made whether on an original return or an amended return, provided it is made within the statute of limitations within the period specified in ORS 314.415.**