



# TAX FACTS 2017-1

## AGRICULTURAL COOPERATIVES

This publication provides general information about the application of the general excise, use, and income taxes on agricultural cooperatives organized under Chapter 421, Hawaii Revised Statutes (HRS), and farmer's cooperatives organized under Internal Revenue Code (IRC) section 521.

### 1 What is an agricultural cooperative?

An agricultural cooperative is a nonprofit corporation organized under Chapter 421, HRS, for the mutual benefit of its members, as agricultural producers, including fish and aquacultural producers, which renders service and provides a means and facilities by and through which agricultural producers receive a reasonable and fair return for their products.

### 2 What is a farmer's cooperative organized under IRC section 521?

A farmer's cooperative is defined as farmers', fruit growers', or like associations organized and operated on a cooperative basis for the purpose of marketing the products of members and other producers or for the purpose of purchasing of supplies and equipments for the use of its members.

### 3 What is the purpose of an agricultural cooperative?

The purpose of an agricultural cooperative is to engage in cooperative activity for its members in connection with the producing, assembling, marketing, buying or selling of agricultural products or harvesting, preserving, drying, processing, blending, canning, packing, ginning, grading, storing, warehousing, handling, shipping, or utilizing the products, or marketing the byproducts. However, 75% of such agricultural products shall be of Hawaiian origin.

A cooperative also buys or supplies machinery, equipment, feed, fertilizer, fuel, seeds, and other

agricultural supplies to its members, and performs or furnishes business or educational services on a cooperative basis or to its members.

### 4 What are the economic benefits for being a member of an agricultural cooperative?

Members are able to save on their purchases of supplies since the cooperative can purchase farm supplies in bulk. Additionally, the members are able to combine their products for marketing and shipping; thus, resulting in a lower pro-rata share of marketing and shipping cost for the individual members.

### 5 Can an exempt agricultural cooperative provide services to a nonmember?

Yes, section 421-9(b)(8), HRS, provides that the cooperative may provide nonmembers the same services, sale of products, handle equipment, machinery, and supplies, as long as the annual value provided to nonmembers is less than or equal to the same goods and services provided to members.

Note: Section 421-9(b)(14), HRS, further states that if the cooperative charges different rates on the sale of its goods and services to members and nonmembers, it must be stated in the bylaws of the cooperative association.

### 6 How do I form an agricultural cooperative?

An agricultural cooperative is a nonprofit corporation that can be made up of three or more persons engaged in the business of producing agricultural products or two or more associations of such producers.

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An Articles of Incorporation must be prepared and filed with the Department of Commerce and Consumer Affairs (DCCA) and bylaws must be adopted within 30 days after incorporation.

There are certain other requirements that must be met in forming an agricultural cooperative. Interested persons should contact the United States Department of Agriculture/Rural Development/Rural Business Cooperative Service for more information.

## **7 How can I become a member of an agricultural cooperative?**

You must be an agricultural or aquacultural producer, a tenant/landlord receiving a share of the crop, or a cooperative association of the producers. Contact the cooperative association to see if you qualify for membership.

## **8 Are agricultural cooperatives subject to Hawaii's general excise and income taxes?**

Cooperative associations organized under Chapter 421, HRS, and farmers' cooperatives organized under IRC section 521 are exempt from Hawaii's general excise and income tax, provided they meet the requirements of section 421-23, HRS. (Farmers' cooperatives organized under IRC section 521, need not be organized in Hawaii.)

## **9 What is section 421-23, HRS, and what are the requirements that must be met?**

Section 421-23, HRS, exempts domestic associations organized under Chapter 421, HRS, from "all corporation, franchise, and income taxes, and taxes and charges upon reserves held by the association for distribution to members."

To obtain the exemption from taxation, the agricultural cooperative must file within 90 days after the close of its fiscal year:

- 1) A copy of its annual report\* with the Director of Taxation; and
- 2) A report with the tax assessor of each district in which there are persons doing business to whom the

agricultural cooperative has paid any proceeds of goods marketed during the preceding fiscal year, showing the name of each person who received proceeds from the cooperative, the total proceeds for which the person is taxable under Chapter 237, HRS, for the fiscal year, and the applicable activity (e.g., wholesaling or retailing) tax rate.

\*The cooperative must file an annual report with the DCCA and the Department of Agriculture within 90 days after the close of its fiscal year containing the information specified in section 421-22, HRS.

## **10 To which gross proceeds does this exemption apply?**

The exemption applies only to the gross income derived from the activities of the cooperative which are done pursuant to the purposes and powers authorized by Chapter 421, HRS. Note that the provisions requiring corporate organization in Hawaii do not apply to IRC section 521 cooperatives.

## **11 How do the members know what the cooperative sold for them?**

The cooperative is responsible for providing its members with their respective share of the gross proceeds of the cooperative.

## **12 As a member of a qualified agricultural cooperative, am I also exempt from the general excise tax (GET) for the products sold by the cooperative on my behalf?**

No, the exemption does not relieve you or any person who receives proceeds from the cooperative of the duty to report and pay the GET at the same tax rate that would apply had the sale been made directly by that person.

## **13 Are sales of agricultural supplies to an agricultural cooperative exempt from the GET?**

No. Sales of agricultural supplies to cooperatives are taxed similar to sales made directly to agricultural or aquacultural producers. Sections 237-4(a)(3), (5), (6), and (7), HRS, describe wholesale transactions where

cooperatives are involved. Supplies that are sold to the cooperative associations for their own consumption are taxed at the retail tax rate.

## **14 Are the agricultural cooperatives subject to use tax for importation of tangible personal property?**

Because the use tax is a complementary tax to the GET, the application of the tax would be the same as the GET. If the cooperative imports any product that is incorporated into the members' products as provided under sections 237-4(a)(3), (5), (6), and (7), HRS, and sold at retail or in any manner other than at wholesale, the use tax rate for the members is 0.5%. If sold at wholesale, no use tax would apply. All other importations for consumption by the members or cooperative association shall be taxed at the rate of 4% (4.5% if subject to the county surcharge.)

## **15 If agricultural cooperatives organized under Hawaii laws receive "unrelated business taxable income" as defined under IRC section 512, do they have to file a Hawaii income tax return?**

Yes, the cooperative must file Form N 30, Hawaii Corporation Income Tax Return reporting the "unrelated business taxable income."

## **16 Are agricultural cooperatives organized under Hawaii laws subject to Federal income taxes?**

These cooperatives should obtain a determination from the Internal Revenue Service on the status. Contact the Internal Revenue Service for more information.

## **17 Are consumer cooperatives organized under Chapter 421C, HRS, also exempt from the GET?**

No. The exemption under section 237-23(a)(8), HRS, does not apply.

### **Where to Get Forms and Information**

Website: [tax.hawaii.gov](http://tax.hawaii.gov)

Telephone: 808-587-4242

Toll-Free: 1-800-222-3229

Telephone for the hearing impaired: 808-587-1418

Toll-Free for the hearing impaired: 1-800-887-8974

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