OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeals of: **J.R. SIMPLOT COMPANY and BRITZ-SIMPLOT GROWER SOLUTIONS, LLC**	OTA Case Nos. 19075067, 19075068 CDTFA Account Nos. 28-099638, 101-146920 CDTFA Case IDs: 912895, 1015352

OPINION

Representing the Parties:

For Appellant: Timothy Mashburn, Representative
Eleanor H. Kim, Tax Counsel

For Respondent: Chad T. Bacchus, Tax Counsel III

A. KWEE, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 6561, J.R. Simplot Company and Britz-Simplot Grower Solutions, LLC (collectively, appellants) appeal decisions issued by respondent California Department of Tax and Fee Administration (CDTFA)[1] denying appellant J.R. Simplot Company's (JRS) timely claim for refund of $171,436.29, filed in connection with a March 9, 2015 Notice of Determination (NOD), and appellant Britz-Simplot Grower Solutions, LLC's (BSG) timely claim for refund of $414,291.58, filed in connection with a March 20, 2015 NOD. The NOD issued to appellant JRS is for $146,559.41 in tax, plus $24,876.88 in interest, for the period April 1, 2010, through March 31, 2013. The NOD issued to appellant BSG is for $340,950.67 in tax, plus $73,340.91 in interest, for the period July 1, 2010, through July 26, 2012. Appellants timely paid the liabilities as determined in the NOD.

Upon motion by appellants, and without objection by CDTFA, these matters were consolidated because they involve substantially the same issue and facts. These matters are being decided based on the written record because appellants waived the right to an oral hearing.

[1] Sales taxes were formerly administered by the Board of Equalization (board). Effective July 1, 2017, functions of the board relevant to this case were transferred to CDTFA. (Gov. Code, § 15570.22.) When referring to acts or events that occurred before July 1, 2017, CDTFA shall refer to its predecessor; the board.

ISSUE

Whether sales of Grow-Plex and Menefee Humate qualify as exempt sales of fertilizer.

FACTUAL FINDINGS

1. Earthgreen Products, Inc. (manufacturer) manufactures and wholesales Grow-Plex and Menefee Humate.
2. Appellants sold Grow-Plex and Menefee Humate to consumers. Appellants' customers applied these products to land used for agricultural purposes. Food products for human consumption are grown on the area to which these products are applied.
3. The manufacturer of Grow-Plex and Menefee Humate registered both of these products as auxiliary soil and plant substances with the California Department of Food and Agriculture (DFA). The manufacturer did not register either of these products as a commercial fertilizer with DFA.
4. Food and Agricultural Code section 14522 defines a "commercial fertilizer" as any substance which contains 5 percent or more of nitrogen (N), available phosphoric acid (P2O5), or soluble potash (K2O), singly or collectively, which is distributed in this state for promoting or stimulating plant growth.
5. The packaging for Menefee Humate describes the product as an "all natural organic soil conditioner." The packaging does not describe the product as a fertilizer, or state that the product contains any N, P2O5, or K2O.
6. The packaging for Grow-Plex describes the product as "[a]n all-purpose water-soluble powder." The packaging does not describe the product as a fertilizer, or state that the product contains any N, P2O5, or K2O. It does, however, specify that the product contains 10 percent Humic Acid.
7. Appellants claimed their retail sales of Menefee Humate and Grow-Plex as exempt sales of fertilizer.
8. During an audit of appellants, CDTFA disallowed all of the claimed exempt fertilizer sales of Menefee Humate and Grow-Plex on the basis that the products did not qualify for the exemption. CDTFA's audit methodology and the calculation of the liability are not at issue in this appeal. CDTFA issued an NOD for the understatement.

9. Appellants paid the liability in full and timely filed claims for refund.
10. In a decision dated January 24, 2019, CDTFA granted appellants' claims for refund in their entirety on the basis that appellants established that the products meet the definition of a commercial fertilizer set forth in the Food and Agricultural Code.
11. In a supplemental decision dated June 20, 2019, CDTFA reversed its original decision to grant the refunds, on the basis that the products constitute auxiliary soil and plant substances, the sale of which are taxable in this state.
12. These timely appeals followed.
13. On appeal, appellants submitted an independent expert's analysis of the products, prepared by Midwest Laboratories. The expert's soil analysis indicates that these products both contain more than 5 percent, by volume, of the following products: N, P2O5, and K20.
14. Appellants also submitted, as evidence, pictures of the manufacturer's website to indicate that the products are intended for use in the promotion or stimulation of plant growth.
15. Appellants' documentation tends to suggest that the products meet the definition of a "commercial fertilizer" as set forth in Food and Agricultural Code section 14522. CDTFA has not specifically disputed that these products meet the definition of a commercial fertilizer.
16. Appellants contend that sales of products meeting the definition of a commercial fertilizer under the Food and Agricultural Code qualify as exempt fertilizer sales, based on the board's precedential memorandum opinion that it issued on May 13, 1999, in *In The Matter of the Petition for Redetermination under the Sales and Use Tax Law of Leonard Eugen Perry* (*Perry*), 1999 WL 636447. In that appeal, an expert witness with a Ph.D. in Plant Pathology provided testimony that the products at issue had 5.5 percent, by volume, of the following chemicals: N, P2O5, and K2O, and that the products promoted or stimulated plant growth and, on that basis, the board concluded the taxpayer's sales of those products qualified as exempt fertilizers.
17. CDTFA contends that *Perry* is inapplicable because there is no discussion in the board's opinion on whether the products at issue were registered with DFA as auxiliary soil and plant substances.

DISCUSSION

California imposes sales tax measured by a retailer's gross receipts from the retail sale of tangible personal property in this state unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, § 6051.) All of a retailer's gross receipts are presumed subject to tax until the contrary is established. (R&TC, § 6091.) The law exempts from tax the sale of fertilizers to be applied to land the products of which are to be used as food for human consumption.[2] (R&TC, § 6358(d).) R&TC section 6358 does not further define what is meant by "fertilizer." R&TC section 7051 grants CDTFA the authority to prescribe, adopt, and enforce rules and regulations relating to the administration and enforcement of the Sales and Use Tax Law.[3]

CDTFA exercised its delegated lawmaking authority as set forth in R&TC section 7051, and promulgated California Code of Regulations, title 18, section (Regulation) 1588, which provides, in pertinent part, that:

> The term "fertilizer" includes commercial fertilizers … [as] defined in section[ ] 14522 (commercial fertilizer) … of the Food and Agricultural Code. . . ¶
>
> The term "fertilizer" does not include "packaged soil amendments" or "auxiliary soil and plant substances" as these terms are defined . . . in sections 14552 (packaged soil amendments) and 14513 (auxiliary soil and plant substances) of the Food and Agricultural Code.

(Cal. Code Regs., tit. 18, § 1588(b)(1).) Similar to commercial fertilizers, auxiliary soil and plant substances also include certain products influencing plant growth. (Food & Agric. Code, § 14513(h).) DFA is charged with the enforcement of the Food and Agricultural Code, including registration of commercial fertilizers and auxiliary soil and plant substances, respectively. (Food & Agric. Code, § 14502.)

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[2] The courts have concluded that statutes granting exemption from taxation must be reasonably, but nevertheless strictly, construed against the taxpayer. The taxpayer has the burden of showing that s/he qualifies for the exemption. An exemption will not be inferred from doubtful statutory language; the statute must be construed liberally in favor of the taxing authority, and strictly against the claimed exemption. (*Standard Oil Co. v. State Bd. Of Equalization* (1974) 39 Cal.App.3d 766.)

[3] The courts have concluded that the legislative delegation in R&TC section 7051 is proper even though it confers some degree of discretion on CDTFA. (*Henry's Restaurants of Pomona, Inc. v. State Bd. of Equalization* (1973) 30 Cal.App.3d 1009, 1020.)

As a preliminary matter, "[a] regulation adopted by an administrative agency pursuant to its delegated rulemaking authority has the force and effect of law." (*California Teachers Assn. v. California Com. On Teacher Credentialing* (2003) 111 Cal.App.4th 1001, 1008.) Here, because CDTFA was exercising its substantive rulemaking power when promulgating Regulation 1588, it was "truly 'making law,' [and CDTFA's] quasi-legislative rules have the dignity of statutes." (*Yamaha Corp. of America v. State Bd. of Equalization* (1998) 19 Cal.4th 1, 6.) It is important to note that for purposes of deciding this appeal, the sales taxes are administered by CDTFA pursuant to the R&TC and, as such, definitions incorporated under the Food and Agricultural Code are only relevant to the extent incorporated by the Sales and Use Tax Law, including CDTFA's authorized rules and regulations.

Appellants are correct that Regulation 1588 incorporates by reference the definition of a "commercial fertilizer" under the Food and Agricultural Code, for purposes of the sales tax exemption for sales of fertilizer. Based on the expert's analysis of the products' chemical properties, it also appears that these products meet the Food and Agricultural Code's definition of a "commercial fertilizer." Nevertheless, this is not the end of the inquiry, because we must read Regulation 1588's entire definition of "fertilizer."

Regulation 1588 goes on to incorporate by reference the Food and Agricultural Code's definition of "auxiliary soil and plant substances" and specifically excludes any such products from meeting the definition of a fertilizer for purposes of the sales tax exemption. Here, the manufacturer of Menefee Humate and Grow-Plex registered these products as "auxiliary soil and plant substances" with DFA, and did not register them as "commercial fertilizers." For purposes of applying the Sales and Use Tax Law, we believe registration of a product with the applicable licensing agency, DFA, as "auxiliary soil and plant substances," is sufficient to create an irrebuttable presumption that the product is excluded from the definition of a "fertilizer" within the meaning of Regulation 1588(b)(1). As such, we find that, because the manufacturer registered Menefee Humate and Grow-Plex as "auxiliary soil and plant substances," appellants cannot, as a matter of law, establish that they qualify for the sales tax exemption for sales of fertilizer.

Appellants further contends that the board's precedential decision in *Perry* is controlling, and stands for the proposition that a taxpayer may establish, via expert testimony, that a product meeting the chemical properties of a commercial fertilizer qualifies for the sales

tax exemption. We disagree. We believe the board's decision in *Perry* is limited to the facts presented in that case (i.e., no evidence of registration with DFA), and we decline to extend it any further. As such, we find that under *Perry*, an expert's testimony on the chemical properties of a product claimed to be an exempt fertilizer, for purposes of the exemption set forth in R&TC section 6358(d), is only relevant if there is no evidence that the product is registered as an "auxiliary soil and plant substance" with DFA.[4] Therefore, we further find that appellants' evidence pertaining to the chemical properties of Menefee Humate and Grow-Plex is not relevant because these products fall within the specific exclusion from the definition of fertilizer set forth in Regulation 1588(b)(1).

HOLDING

Appellants' retail sales of Menefee Humate and Grow-Plex do not qualify as exempt sales of fertilizer.

DISPOSITION

CDTFA's actions in denying the claims for refund are sustained.

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Andrew J. Kwee
Administrative Law Judge

We concur:

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Josh Aldrich
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Joshua Aldrich
Administrative Law Judge

DocuSigned by:
Josh Lambert
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Josh Lambert
Administrative Law Judge

Date Issued: 2/21/2020

[4] Of course, in such circumstances, the exemption would be inapplicable if it was established that the product met the definition of an excluded item, such as "auxiliary soil and plant substances."