

Ernie Fletcher
Governor
Commonwealth of Kentucky

Robbie Rudolph
Secretary
Finance & Administration
Cabinet



Annual Report 2003-2004

Mark Treesh
Commissioner
Department of Revenue



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UNBRIDLED SPIRIT™

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ERINE FLETCHER
GOVERNOR

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ROBBIE RUDOLPH
SECRETARY

MARK TREESH
COMMISSIONER

December 30, 2004

The Honorable Ernie Fletcher, Governor
Commonwealth of Kentucky
The State Capitol
Frankfort, Kentucky 40601

Dear Governor Fletcher:

I am pleased to present the Annual Report of the Department of Revenue for the fiscal year ended June 30, 2004. This report reflects the dedicated work of the many fine professionals who comprise the Revenue workforce.

Reorganization established Revenue as part of Finance and Administration Cabinet at the beginning of your administration. Internal reorganization of Department of Revenue became effective on July 1, 2004, and will lead to greater efficiency in tax administration.

Electronic filing continued to grow with almost half of the returns being electronically filed. There were 785,821 returns filed electronically, 243,424 2-D barcode returns, and 535,341 paper returns for a total of 1,564,586 returns filed for tax year 2003.

On behalf of all of Revenue, we want to thank you for your continued support of the Department of Revenue and its employees and for your confidence in our abilities.

Sincerely,

A handwritten signature in cursive script that reads "Mark Treesh".

Mark Treesh, Commissioner
Kentucky Department of Revenue

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Revenue Receipts

Reprinted from the Governor's Office for Economic Analysis
Fourth Quarter Report—Annual Edition
Fiscal Year 2004

As shown in Table 1, combined tax and nontax receipts for the General and Road Funds increased by 2.4 percent over the combined receipts in Fiscal Year 2003. Table 2 compares only tax receipts for the two funds, which increased by 2.2 percent. Table 3 compares combined nontax receipts, which decreased by 11.5 percent over the previous year.

Table 1
Total Receipts
(millions of dollars)

	FY04	FY03	Percent Change
General Fund	\$6,977.6	\$6,783.5	2.9
Road Fund	1,116.7	1,123.1	-0.6
Combined	\$8,094.3	\$7,906.6	2.4

Table 2
Tax Receipts
(millions of dollars)

	FY04	FY03	Percent Change
General Fund	\$6,686.3	\$6,543.2	2.2
Road Fund	1,082.2	1,059.3	2.2
Combined	\$7768.5	\$7,602.5	2.2

Table 3
Nontax Receipts
(millions of dollars)

	FY02	FY03	Percent Change
General Fund	\$291.3	\$240.0	21.2
Road Fund	48.9	63.8	-23.4
Total	\$339.2	\$304.1	11.5

General Fund

General Fund receipts for Fiscal Year 2004 increased by 2.9 percent over those reported in Fiscal Year 2003. Total General Fund receipts of \$6,977.6 million compared to \$6,783.5 million collected in Fiscal Year 2003. Receipts for Fiscal Year 2003 were influenced by a tax amnesty program that generated significant receipts, and by several “one-time” events within particular taxes that provided increases for Fiscal Year 2003 that did not recur in Fiscal Year 2004. In Fiscal Year 2003, tax amnesty and the other one-time events are estimated to have boosted General Fund revenues by \$192.0 million.

The sales tax growth rate for Fiscal Year 2004 was 3.5 percent and compares to the growth rate for Fiscal Year 2003 of 2.8 percent. Receipts of \$2,447.6 million compare to prior year receipts of \$2,364.2 million. Excluding the ‘tax amnesty’ program and other one-time collections that occurred in Fiscal Year 2003, the growth rate would likely have been nearly 6 percent for the fiscal year.

The individual income tax posted small positive growth, following a very similar gain in Fiscal Year 2003. The growth rate for Fiscal Year 2004 was 1.8 percent, compared to 1.6 percent in Fiscal Year 2003. Receipts totaled \$2,796.3 million and compared to \$2,746.4 million collected last year. Again, excluding the tax amnesty program and other one time collections that occurred in Fiscal Year 2003, the growth rate would likely have been nearly 6.0 percent for the fiscal year.

The corporation income and license tax posted a small decline of 0.7 percent for Fiscal Year 2004. Receipts of \$427.4 million compared to \$430.6 million collected in Fiscal Year 2003. Both tax amnesty and one-time collections had a positive influence on corporate tax collections during Fiscal Year 2003. Conversely, several legal challenges and decisions worked to depress collections during Fiscal Year 2004.

Coal severance tax collections reversed long-term trends by posting a gain of 4.1 percent. Receipts totaled \$147.5 million and compare to \$141.7 million collected during the prior fiscal year. Coal severance tax receipts have generally been on a long- term, slowly decreasing pattern for more than a decade. However, this increase and a similar jump in Fiscal Year 2002 demonstrate that increased energy prices in general will likely result in increased coal activity and increased coal receipts.

Total property taxes experienced a small increase of 3.2 percent during this fiscal year. Receipts totaled \$448.8 million compared to \$434.8 million collected in Fiscal Year 2003. Timing differences within some property tax accounts and relative to distributions of some collections that are made on behalf of local government continue to have a minor impact on property tax receipts.

Lottery receipts grew by 1.6 percent from the previous year. Receipts of \$173.8 million compare to the \$171.0 million remitted to the state last fiscal year.

The “all other” category finished the year with an increase of 8.4 percent. Receipts of \$536.2 million compare to \$494.8 million collected in Fiscal Year 2003. Abandoned property receipts increased significantly during Fiscal Year 2004 due to legislative changes.

Revenue Receipts

Table 4
General Fund Growth Rates
for the Four Quarters and Full Year, FY04

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY04
Total					
Receipts	-0.7	1.3%	4.5%	6.4%	2.9%
Sales & Use	-4.4	3.6	8.9	7.1	3.5
Individual					
Income	5.0	2.5	-7.5	5.9	1.8
Corporate					
Income/					
License	-19.2	-24.0	---	8.3	-0.7
Coal					
Severance	-5.7	-4.1	5.6	21.3	4.1
Property	-12.9	2.4	18.1	-10.6	3.2
Lottery	7.0	0.0	0.0	0.0	1.6
All Other	9.8	6.5	3.4	9.0	8.4

Road Fund

Total Road Fund receipts increased by 0.6 percent during Fiscal Year 2004. Total receipts of \$1,116.7 million compared to \$1,123 million collected in this fund during Fiscal Year 2003.

Motor fuels and motor fuels use taxes increased by 1.3 percent on receipts of \$459.6 million, compared to \$453.6 million collected during the previous fiscal year.

Motor vehicle usage tax receipts of \$429.2 million represent a small increase of 0.8 percent over the \$432.9 million collected in Fiscal Year 2003. This compares to an increase of 0.8 percent experienced last year. Usage tax receipts have been expected to flatten as the rapid pace of vehicle purchases of the previous two years slows down.

Weight distance tax began to increase late in the year and finished with growth of 3.5 percent. Receipts totaled \$79.6 million for this year and \$76.9 million for Fiscal Year 2003.

Motor vehicle license receipts increased by 22.6 percent on receipts of \$93.4 million, compared to 76.2 million in Fiscal Year 2003. Legislative changes resulted in large trucks paying higher license taxes in Fiscal Year 2004.

Investment income declined by 74.2 percent, as balances were spent down for various construction projects. Receipts for Fiscal Year 2004 were \$7.5 million, compared to \$29.1 million in Fiscal Year 2003.

The "all other" category decreased by 12.9 percent over the previous year. Total receipts in this category were \$47.4 million, which compares to \$54.4 million collected in Fiscal Year 2003.

Table 5
Road Fund Growth Rates
for the Four Quarters and Full Year, FY04

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY04
Total					
Receipts	1.6%	-2.7%	2.3%	-3.4%	-0.6%
MF/MF Use	0.3	-0.5	4.4	1.6	1.3
Motor					
Vehicle					
Usage	1.3	-1.2	1.4	-4.7	-0.8
Weight					
Distance	0.3	-0.5	6.2	8.5	3.5
Invest. Income	-43.3	-89.8	-74.4	-98.6	-74.2
All Other	0.0	-15.6	-16.0	-16.4	-12.9

Tax Amnesty

The Kentucky Department of Revenue conducted a *tax amnesty* program during Fiscal Year 2003. The intent of the program was to encourage taxpayers who owed back taxes to the commonwealth to voluntarily declare and remit the past due funds. Encouragement to participate was provided by waiver of penalties and interest for almost all past due taxes that were acknowledged and paid during the amnesty period. Penalties and interest rates were increased for all those who owed back taxes, but chose not to participate in the amnesty program, and for most future collection efforts. The tax amnesty program is estimated to have generated \$41.6 million in additional receipts for Fiscal Year 2003.

Revenue Receipts

GENERAL FUND

ALCOHOLIC BEVERAGE TAXES

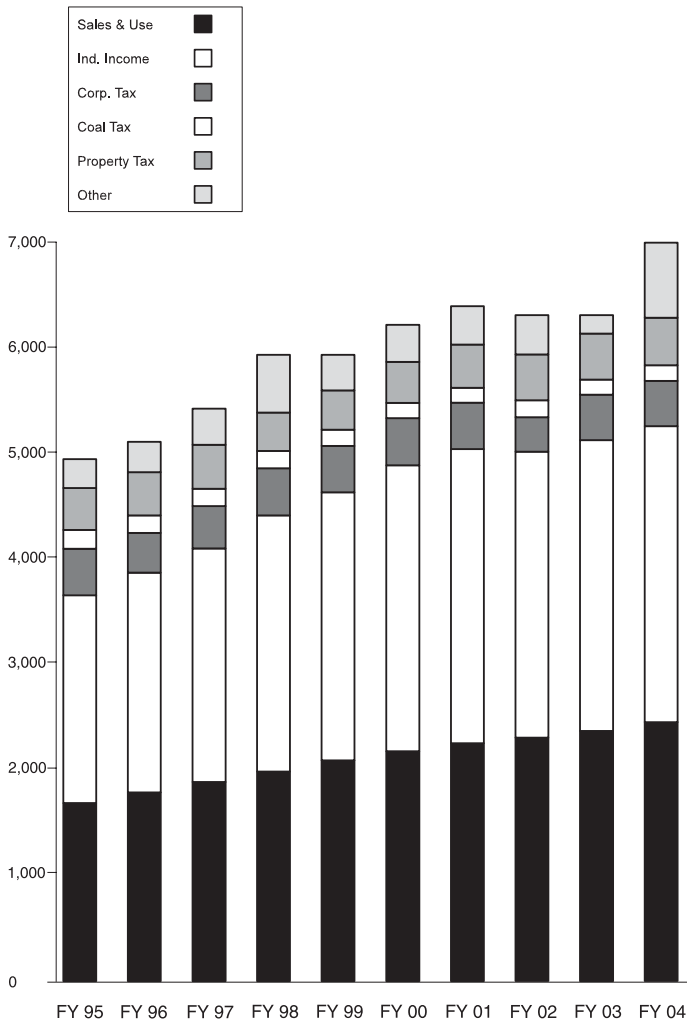
GENERAL FUND TOTAL RECEIPTS

Fiscal Year	Receipts	Percent Change
2003-04	\$6,977,623,200	2.9
2002-03	6,783,458,295	3.4
2001-02	6,560,216,551	-1.4
2000-01	6,653,897,653	2.7
1999-00	6,478,385,032	4.5
1998-99	6,198,387,525	3.1
1997-98	6,011,806,561	6.1
1996-97	5,663,553,289	6.1
1995-96	5,336,883,824	3.5
1994-95	5,154,077,980	10.9

Malt Beverage

Fiscal Year	Receipts	Percent Change
2003-04	\$43,760,805	3.4
2002-03	42,304,059	4.4
2001-02	40,883,326	5.2
2000-01	38,854,920	1.2
1999-00	38,385,890	4.1
1998-99	36,870,323	2.6
1997-98	35,937,878	3.2
1996-97	34,830,419	1.0
1995-96	34,489,349	2.0
1994-95	33,812,169	3.9

General Fund Receipts by Major Sources Millions of Dollars



Distilled Spirits

Fiscal Year	Receipts	Percent Change
2003-04	\$26,030,680	4.7
2002-03	24,854,482	5.9
2001-02	23,477,073	1.7
2000-01	23,077,057	3.3
1999-00	22,349,780	4.3
1998-99	21,432,736	2.2
1997-98	20,979,849	2.1
1996-97	20,548,503	0.3
1995-96	20,493,441	3.0
1994-95	19,897,599	-0.3

Wine

Fiscal Year	Receipts	Percent Change
2003-04	\$9,312,250	7.1
2002-03	8,698,754	6.3
2001-02	8,183,587	4.3
2000-01	7,846,391	2.3
1999-00	7,672,648	8.8
1998-99	7,049,136	7.6
1997-98	6,551,316	7.6
1996-97	6,085,828	8.5
1995-96	5,610,308	15.7
1994-95	4,847,726 ¹	7.9

¹Adjusted for small math error.

Revenue Receipts

CIGARETTE TAX¹

Fiscal Year	Receipts	Percent Change
2003-04	\$17,136,198	4.7
2002-03	16,367,947	17.4
2001-02	13,943,208	-0.5
2000-01	14,007,582	-1.2
1999-00	14,184,888	-3.3
1998-99	14,673,839	-3.0
1997-98	15,130,443	-5.7
1996-97	16,044,967	2.3
1995-96	15,680,704	3.7
1994-95	15,126,270	5.9

¹The cigarette tax is levied at the rate of 3 cents per pack. These totals reflect the 2.5 cents per pack that are deposited into the General Fund. The remaining 0.5 cent per pack is dedicated to tobacco research and is deposited in the Tobacco Research Trust Fund.

COAL SEVERANCE TAX

Fiscal Year	Receipts	Percent Change
2003-04	\$147,498,230	4.1
2002-03	141,664,981	-11.5
2001-02	160,160,116	13.1
2000-01	141,553,087	-2.5
1999-00	145,139,909	-6.0
1998-99	154,476,772	-5.7
1997-98	163,731,038	0.1
1996-97	163,545,844	-5.3
1995-96	166,101,045	-7.3
1994-95	179,116,944	-0.4

CORPORATION INCOME TAX

Fiscal Year	Receipts	Percent Change
2003-04	\$303,262,821	9.1
2002-03	278,035,794	34.1
2001-02	207,353,777	-28.5
2000-01	289,931,017	-5.4
1999-00	306,442,050	-1.8
1998-99	312,066,675	-6.5
1997-98	333,666,393	14.0
1996-97	292,753,126	2.8
1995-96	284,732,573	-16.5
1994-95	340,912,408	26.7

CORPORATION LICENSE TAX

Fiscal Year	Receipts	Percent Change
2003-04	\$124,096,012	-18.7
2002-03	152,595,257	29.9
2001-02	117,500,770	-20.3
2000-01	147,515,402	6.0
1999-00	139,127,819	10.5
1998-99	125,912,523	11.7
1997-98	112,763,160	4.9
1996-97	107,498,746	18.8
1995-96	90,515,391 ²	-7.1
1994-95	97,449,950 ¹	18.8

¹Adjusted for small math error

²Corrected for posting error.

INDIVIDUAL INCOME TAX

Fiscal Year	Receipts	Percent Change
2003-04	\$2,796,331,049	1.8
2002-03	2,746,386,944	1.6
2001-02	2,702,510,022	-2.7
2000-01	2,778,541,444	2.8
1999-00	2,701,613,908	6.7
1998-99	2,532,005,348	4.7
1997-98	2,418,144,438	9.7
1996-97	2,205,022,964	6.3
1995-96	2,074,572,167	5.6
1994-95	1,964,843,490	13.6

INHERITANCE AND ESTATE TAX

Fiscal Year	Receipts	Percent Change
2003-04	\$66,083,705	-31.1
2002-03	95,864,480	15.0
2001-02	83,359,872	-0.1
2000-01	83,461,499	12.0
1999-00	74,489,981	8.5
1998-99	81,483,083	22.8
1997-98	105,538,130	10.8
1996-97	95,287,282	17.0
1995-96	81,441,427 ¹	2.4
1994-95	79,511,634	4.4

¹Phase-in of Class A beneficiary exemption began July 1, 1995.

Revenue Receipts

INSURANCE PREMIUMS TAX

Foreign Life Insurance Companies		
Fiscal Year	Receipts	Percent Change
2003-04	\$36,735,324	-0.5
2002-03	36,904,902	2.3
2001-02	36,058,437	3.7
2000-01	34,775,487	-3.2
1999-00	35,909,807	8.5
1998-99	33,085,292	-5.8
1997-98	35,116,933	6.1
1996-97	33,086,032	-8.5
1995-96	36,165,049	6.5
1994-95	33,966,941	-10.7

MINERALS AND NATURAL GAS TAX

Fiscal Year	Receipts	Percent Change
2003-04	\$36,223,062	32.7
2002-03	27,294,398	10.7
2001-02	24,656,955	-17.9
2000-01	30,030,552	34.2
1999-00	22,369,419	18.0
1998-99	18,954,883	-6.1
1997-98	20,192,086	0.7
1996-97	20,051,609	15.4
1995-96	17,378,785	17.6
1994-95	14,783,614	-11.6

Insurance Companies Other than Life

Fiscal Year	Receipts	Percent Change
2003-04	\$79,870,778	7.2
2002-03	74,529,362	13.1
2001-02	65,899,201	11.5
2000-01	59,118,323	3.7
1999-00	57,000,964	4.7
1998-99	54,431,503	3.5
1997-98	52,600,230	4.5
1996-97	50,318,931	3.4
1995-96	48,687,419	7.0
1994-95	45,515,163	6.5

OIL PRODUCTION TAX

Fiscal Year	Receipts	Percent Change
2003-04	\$3,387,884	8.7
2002-03	3,116,954	20.3
2001-02	2,590,722	-22.9
2000-01	3,358,036	13.2
1999-00	2,967,395	120.6
1998-99	1,344,942	-37.0
1997-98	2,135,211	-29.9
1996-97	3,044,497	15.1
1995-96	2,644,656	-5.0
1994-95	2,784,562	3.2

LOTTERY RECEIPTS

Fiscal Year	Receipts	Percent Change
2003-04	\$173,800,000	1.6
2002-03	171,000,000	1.2
2001-02	169,000,000	7.6
2000-01	157,030,000	0.5
1999-00	156,300,000	1.6
1998-99	153,800,000	0.5
1997-98	153,000,000	1.3
1996-97	151,000,000	2.7
1995-96	147,000,000	8.1
1994-95	136,000,000	19.3

PARI-MUTUEL TAX

Fiscal Year	Receipts	Percent Change
2003-04	\$3,629,292	-39.0
2002-03	5,953,247	14.9
2001-02	5,179,952	-16.2
2000-01	6,182,083	-7.0
1999-00	6,645,098	-7.4
1998-99	7,179,163	48.1
1997-98	4,845,921	-18.0
1996-97	5,911,958	-17.3
1995-96	7,148,951	-1.5
1994-95	7,256,986	18.3

Revenue Receipts

PROPERTY TAXES—REAL ESTATE

Fiscal Year	Receipts	Percent Change
2003-04	\$192,534,530	3.5
2002-03	186,000,177	3.5
2001-02	179,678,050	4.8
2000-01	171,524,695	2.5
1999-00	167,326,472	3.5
1998-99	161,723,137	4.8
1997-98	154,245,453	-9.3
1996-97	170,063,059 ¹	19.2
1995-96	142,728,406	7.2
1994-95	133,200,108	0.8

¹Some tangible property tax receipts were erroneously credited to real property receipts accounts.

PROPERTY TAXES—TANGIBLE

Fiscal Year	Receipts	Percent Change
2003-04	\$149,155,206	-0.2
2002-03	149,426,286	-1.2
2001-02	151,308,795	7.7
2000-01	140,466,295	7.3
1999-00	130,960,896	4.3
1998-99	125,564,658	-0.2
1997-98	125,753,465	0.9
1996-97	124,637,468 ¹	-9.6
1995-96	137,812,773	20.8
1994-95	114,122,717	9.2

¹Some tangible property tax receipts were erroneously credited to real property receipts accounts.

PROPERTY TAXES—INTANGIBLE

Fiscal Year	Receipts	Percent Change
2003-04	\$27,547,183	6.4
2002-03	25,883,197	12.0
2001-02	23,113,567	2.5
2000-01	22,551,153	-0.8
1999-00	22,721,743	25.5
1998-99	18,103,920	-14.3
1997-98	21,129,328 ¹	-54.7
1996-97	46,631,437 ¹	-29.9
1995-96	66,489,089	-20.4
1994-95	83,479,482	7.9

SALES AND USE TAX

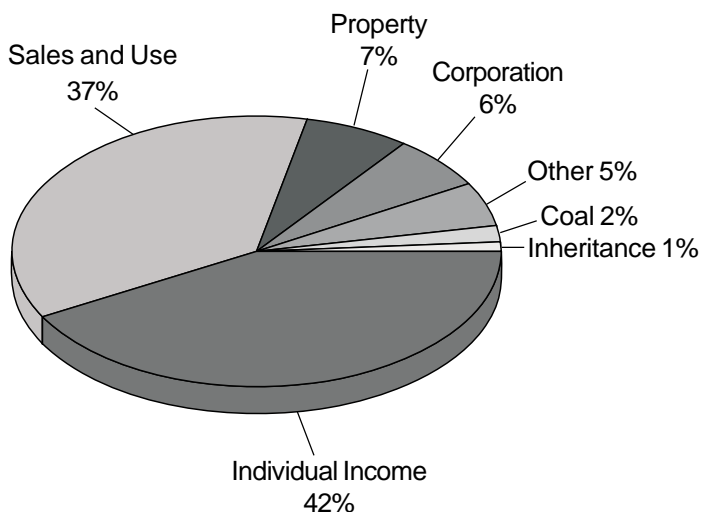
Fiscal Year	Receipts	Percent Change
2003-04	\$2,447,584,698	3.5
2002-03	2,364,182,478	2.8
2001-02	2,299,990,621	2.3
2000-01	2,248,471,100	3.5
1999-00	2,171,397,969	4.1
1998-99	2,085,899,677	5.3
1997-98	1,981,297,580	5.2
1996-97	1,882,681,995	5.5
1995-96	1,783,881,316	6.2
1994-95	1,680,520,815	7.7

BANK FRANCHISE TAX¹

Fiscal Year	Receipts	Percent Change
2003-04	\$55,467,195	3.2
2002-03	53,747,906	6.3
2001-02	50,549,168	1.9
2000-01	49,610,220	-6.5
1999-00	53,061,789	12.8
1998-99	47,059,959	34.2
1997-98	35,059,801	-14.2
1996-97	40,878,664	----

¹Kentucky's bank franchise tax was instituted in July 1996.

Makeup of FY04 General Fund



Revenue Receipts

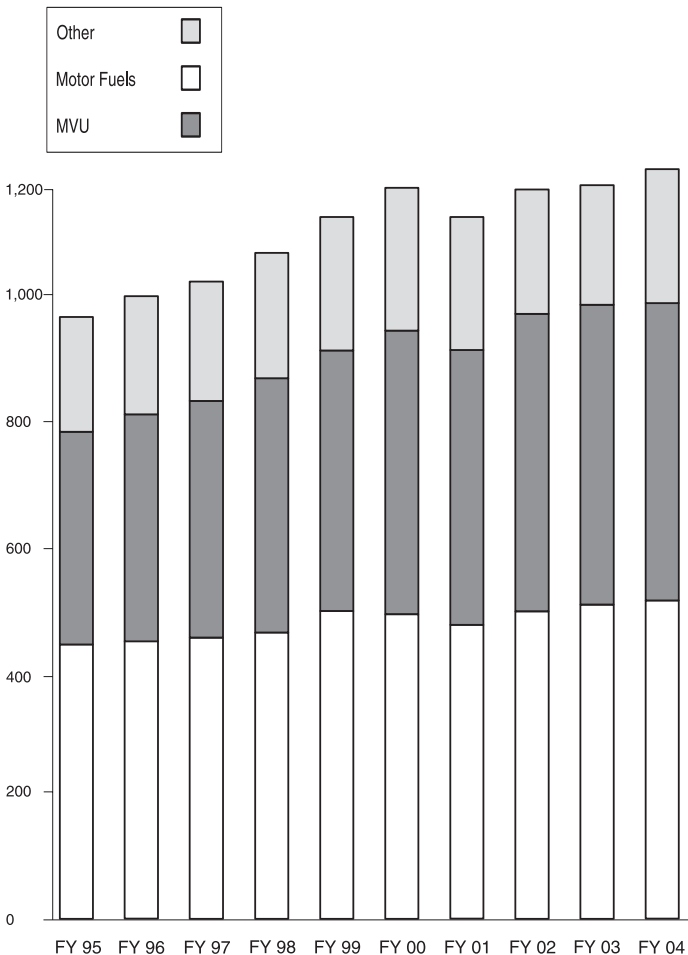
ROAD FUND

ROAD FUND TOTAL RECEIPTS		
Fiscal Year	Receipts	Percent Change
2003-04	\$1,116,734,272	-0.6
2002-03	1,123,103,133	0.4
2001-02	1,119,005,317	5.2
2000-01	1,064,181,565	-2.4
1999-00	1,090,777,822	3.2
1998-99	1,056,596,153	4.4
1997-98	1,011,789,675	5.4
1996-97	960,183,780	2.2
1995-96	939,910,490	4.4
1994-95	900,619,387	4.4

MOTOR FUELS TAXES

Motor Fuels Normal		
Fiscal Year	Receipts	Percent Change
2003-04	\$441,382,996	0.6
2002-03	438,564,438	2.0
2001-02	429,812,296	5.1
2000-01	408,801,115	-3.6
1999-00	423,876,351	-0.9
1998-99	427,848,100	8.0
1997-98	396,123,781	1.4
1996-97	390,688,336	3.3
1995-96	378,142,941	1.3
1994-95	373,316,977	4.2

Road Fund Receipts by Major Sources
Millions of Dollars



FY04 Car registration is now included in the "other" category

Motor Fuels Normal Use and Surtax

Fiscal Year	Receipts	Percent Change
2003-04	\$18,185,947	21.5
2002-03	14,969,884	6.0
2001-02	14,124,035	-8.8
2000-01	15,492,738	-2.6
1999-00	15,905,613	-5.6
1998-99	16,853,163	-3.6
1997-98	17,473,744	14.1
1996-97	15,316,702	-32.1
1995-96	22,554,473	-2.2
1994-95	23,052,951	7.7

MOTOR VEHICLE OPERATOR'S LICENSE

Fiscal Year	Receipts	Percent Change
2003-04	\$5,623,874	0.2
2002-03	5,610,829	0.8
2001-02	5,564,009	-0.5
2000-01	5,592,769	-1.7
1999-00	5,689,329	5.3
1998-99	5,400,685	3.0
1997-98	5,241,595	-2.1
1996-97	5,355,648	4.8
1995-96	5,110,387	-1.2
1994-95	5,170,423	-3.5

Revenue Receipts

MOTOR VEHICLE REGISTRATIONS

Passenger Car Registration		
Fiscal Year	Receipts	Percent Change
2003-04	*	
2002-03	\$25,793,836	1.7
2001-02	25,355,086	9.5
2000-01	23,162,962	-1.4
1999-00	23,485,625	0.6
1998-99	23,356,526	-1.1
1997-98	23,604,679	1.4
1996-97	23,276,395	-0.5
1995-96	23,389,132	0.0
1994-95	23,398,303	-0.3

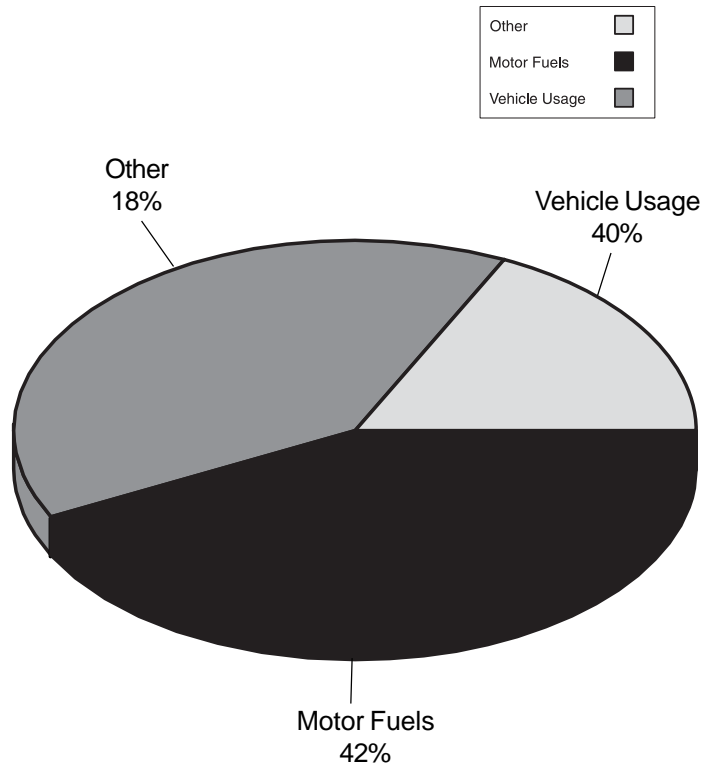
MOTOR VEHICLE RENTAL USAGE TAX

Fiscal Year	Receipts	Percent Change
2003-04	\$38,225,048	-12.9
2002-03	43,877,657	-8.3
2001-02	47,840,871	-7.3
2000-01	51,619,167	3.3
1999-00	49,957,851	12.4
1998-99	44,465,916	7.3
1997-98	41,450,720	13.3
1996-97	36,593,748	25.9
1995-96	29,054,964	26.5
1994-95	22,966,441	34.7

MOTOR VEHICLE USAGE TAX

Fiscal Year	Receipts	Percent Change
2003-04	\$390,977,268	0.5
2002-03	388,959,153	2.0
2001-02	381,398,176	10.5
2000-01	345,120,799	-4.0
1999-00	359,437,723	8.5
1998-99	331,187,817	1.8
1997-98	325,308,554	6.7
1996-97	304,868,491	2.1
1995-96	298,585,859	5.2
1994-95	283,820,829	2.0

Makeup of FY04 Road Fund



*FY04 Car registration is now included in "other" category

Accomplishments

Major DOR Accomplishments in Fiscal Year 2003-2004

Accomplishments during Fiscal Year 2003-2004 reflect employees' commitment to DOR's goals. These accomplishments emphasize the DOR's mission—to provide courteous, accurate and efficient services for the benefit of the commonwealth and administer Kentucky tax laws in a fair and impartial manner.

Major accomplishments are highlighted in individual narratives in this report. Other specific accomplishments that underscore major progress toward DOR's goals are as follows:

Taxpayer Service

- Offered extended office hours in April 2004 to accommodate taxpayers with questions regarding individual income tax returns, withholding and sales and use taxes.
- Continued the partnership with the University of Kentucky and the IRS in presenting up-to-date individual income tax information to approximately 1,400 Kentucky tax practitioners, CPAs, attorneys, insurance adjusters, realtors and other interested parties.
- Processed 1,217,151 timely and correctly filed individual income tax returns requesting refunds by May 21, 2004.
- Issued 282,261 direct deposit refunds for individual income tax returns.
- Processed 1,019,500 returns filed through electronic media, representing an increase of 9.6 percent over the previous processing cycle.
- Continued to participate in the University of Louisville's Louis A. Grief Tax Institute by presenting up-to-date individual income tax information to approximately 200 tax practitioners, CPAs, attorneys and other interested persons.
- Served as the main answering point (taxpayer assistance group) for individual, withholding and sales tax telephone inquiries. A total of 150,008 inquiries were received for the fiscal year.
- Increased voluntary electronic submission of wage and tax statements through an educational campaign conducted by the Withholding Tax Section. Electronic filing of W-2s increased 14.9 percent. The number of employers filing W-2s electronically increased by 550.
- Joined IRS on November 3 for a joint problem solving day. Taxpayers received assistance in resolving either state or federal tax issues with one-stop assistance.
- Continued partnerships with the IRS to provide education and training for volunteers participating in community-based partnerships that provide free tax preparation and electronic filing for the elderly and low-income taxpayers.

- Continued a foreign and sign language directory for DOR employees to better assist taxpayers who are unable or limited in speaking English.
- Trained newly elected sheriffs about their property tax collection duties.
- Trained county clerks on the property tax assessment appeal process.
- Developed tobacco manufacturer directories on the DOR Web site for use by cigarette wholesalers and general public. The directories list cigarette manufacturers and their respective brands that the Kentucky Office of Attorney General (OAG) has certified as having complied with the provisions of the Master Settlement Agreement (MSA).

Collection of Tax Revenues

- Implemented the Environmental Remediation Fee, also known as Tipping Fee, in cooperation with the Natural Resources and Environmental Protection Cabinet. This fee is collected from landfill operators and transfer stations. Money is deposited into the Kentucky Pride Fund and used to pay for the cost of cleaning up illegal waste dumps.
- Collected \$4,394,999 delinquent Kentucky income taxes by offsetting Federal Income Tax refunds through the IRS Tax Offset Program.
- Generated tangible and intangible property tax assessments totaling \$53.6 million.
- Collected tangible and intangible property tax receipts of \$36.8 million.
- Processed 7,875 voluntary tangible property tax returns and 2,529 voluntary intangible property tax returns.
- Completed 1,984 desk audits of tangible and intangible property tax returns.
- Reviewed and billed 1,586 tangible / intangible property tax field audits.
- Answered 9,667 personal property phone calls.
- Mailed 4.7 million MOTAX renewal notices with an assessed value of \$21.3 billion. Processed 27,837 apportioned vehicle notices with an assessed value of \$1.6 billion.
- Collected \$3.4 million state and \$6.3 million local apportioned vehicle taxes.
- Processed 1,140 county clerk reports.
- Computed 1,829 public service company (PSC) assessments.

Accomplishments

- Computed 10,509 local certifications of PSC assessments with an assessed value of \$15.3 billion.
- Collected 1,312 PSC state payments totaling \$50.3 million.
- Collected \$116.5 million in delinquent taxes.
- Coordinated over 150 training events during the fiscal year. The events covered 53 different topics and required 804 hours of instruction time. DOR also worked with the Center for Excellence in Government in developing a process for documenting the critical knowledge, skills and abilities of DOR's most tenured employees. This continuing effort is part of an overall strategy to properly plan for potential retirements by ensuring that critical knowledge is not lost when long-time employees retire.

Business Practices

- Processed approximately five million documents, deposited more than \$7.8 billion in receipts and made timely deposits into all funds.
- Continued the use of two-dimensional (2-D) bar code technology to improve the efficiency of processing paper returns. DOR used the 2-D technology to process 245,065 paper returns. DOR processed 194,876 *no-money* (refund, returns without payment) returns and 50,189 *money* (returns with payment) returns. The 2-D technology is incorporated into software packages offered by various software vendors. The 2-D process is faster, has a lower error rate and requires less human intervention than the normal paper process. The primary benefit to taxpayers is the reduction in the time required to issue refunds.
- Developed a coordinated Emergency Operations Plan (EOP) for the Fair Oaks Building Complex in conjunction with six other tenant agencies. The plan is a comprehensive emergency management program consistent with KRS Chapter 39A that serves as a guide for decision making and actions during emergencies, whether declared or sudden events. Participating in the EOP as signatory agencies are the Personnel Cabinet, Governor's Office for Technology, Cabinet for Health Services, Public Protection and Regulation Cabinet, Agriculture, Finance and Administration Cabinet and Revenue. The plan was approved by the Division of Emergency Management.
- Developed a training manual for newly elected PVAs in November 2002 and completely updated the PVA Fiscal and Personnel Manual. Trained over 60 counties on the Payroll, Time and Labor (PTL) System. Half of the PVA offices are now using the state system to record time. Conducted training for PVAs on asset management and disposal.
- Assisted PVAs with the annual inventory of fixed assets and in obtaining insurance coverage for state property in their offices. Over \$1.5 million of PVA fixed assets were added to the state inventory system.
- Expanded office hours for requesting tax forms by one hour each day during filing season. This measure was undertaken in order to provide taxpayers and tax preparers with an improved level of service during income tax filing season.

Technological Advances

- Implemented the Unmined Minerals and Severance Tax (UMAST) System to improve the assessment and billing functions for these taxes. The new system allows all entities responsible for unmined mineral property taxes to be properly associated with the mineral location.
- Began the design and development of a sales and withholding tax online filing system, KY E-Tax, to be fully implemented by the third quarter of 2004. KY E-Tax will expand its electronic payment options to e-checks and credit cards to pay sales tax and timely filed individual income tax by the second quarter of Fiscal Year 2004, and withholding tax by the third quarter of Fiscal Year 2004.
- Implemented a new interface from DOR's credit card application to the Commonwealth's E-Payment Gateway that provides a uniform method for agencies to process electronic payments.
- Expanded the use of e-checks to enable taxpayers to electronically submit installment payments. This greatly reduced the cost of processing payments and the default rate on payment agreements.
- Implemented KY E-tax to allow sales tax returns to be filed electronically.
- Implemented a system to handle no pay sales and withholding tax returns via the telephone Interactive Voice Response (IVR).
- Implemented new processes to match payments and returns received at different times during the tax filing season. This allows the DOR to better manage taxpayer accounts. More than 51,000 individual income tax returns and payments were electronically matched by the completion of Fiscal Year 2003.
- Completed the new Motor Fuels Tax System. This system replaces an existing legacy system with additional functionality. This system is more adaptable to changes in the tax laws, provides search capabilities presently not available, streamlines data entry, creates reports that are currently done by hand and is user friendly. Began the design of a special fuels module that will allow gasoline and special fuels licensed dealers to remit their taxes and the corresponding petroleum assurance tank fees by electronic funds transfer (EFT) payment.

Accomplishments

- Expanded scanning applications to allow additional documents from DOR archives to be electronically scanned and retrieved.
- Installed an in-house backup and recovery solution in order to ensure reliable backup of DOR network servers and provide the ability to efficiently recover files or entire hardware platforms in a timely manner.
- Developed an off-site storage policy for backup tapes as part of DOR disaster recovery planning and utilized state contracts for off-site media storage.
- Connected 20 more PVA offices to the Kentucky Information Highway (KIH), culminating in a full two-thirds of the PVA offices having access to the KIH services.
- Began the process of rewriting the Tax Roll Information Management (TRIM) used by PVAs and Sheriff's Automated Collection System (SACS) software. The new software is currently scheduled to be implemented in the 2005 assessment year.
- Migrated the FileNet document repository from optical platters to magnetic storage in order to provide a more stable and reliable mechanism for document committal and retrieval. This upgrade resulted in less system downtime, better performance and a reduction in hardware maintenance costs.
- Tightened DOR network security by the installation of a Virtual Private Network (VPN) firewall solution for all 12 DOR locations. This solution allows the DOR to implement one set of firewall rules across the enterprise while providing a secure connection for communications between locations.
- Upgraded the physical access control software in order to provide a better method for controlling and reporting on facilities' access through the swipe-lock system. DOR security staff provides ongoing support through centralized system administration for agencies residing in both Fair Oaks buildings and the DOR Perimeter Park location.
- Developed generic profiles for all DOR mainframe applications as an important part of standard Resource Access Control Facility (RACF) security and abandoned the use of discrete profiles based on specific dataset names.
- Implemented the electronic interface between the Cabinet for Health and Family Services' (CHFS) Child Support System and OSCAR. The system became fully operational in May 2004. During this fiscal year, the DOR collected \$366,805 in delinquent child support. Of this amount, \$177,785 or 48 percent was collected in May and June.
- Continued work on Streamlined Sales Tax Project (SSTP).
- Processed \$2.9 billion in EFT payments.

Use of Electronic Filing Increases

- The use of electronic filing methods for 2003 individual income tax returns increased over the 2002 filing season. Electronic returns fall into one of three categories: TeleFile (telephone filing); online (Internet filing); or electronic (i.e., tax preparers). By the end of Fiscal Year 2003-2004, 785,821 returns had been filed electronically compared to 707,382 returns filed by the end Fiscal Year 2002-2003.
- The number of taxpayers filing online for 2003 returns increased to 123,862 compared to 98,738 filed for 2002.
- The number of taxpayers who filed their sales tax returns online in Fiscal Year 2003-2004 totaled 4,023. In addition, 1,736 entities registered to file their sales tax returns online.
- The number of taxpayers who filed their sales tax returns via telephone Interactive Voice Response (IVR) totaled 1,859.

Compliance Initiatives

- The fully automated W-2 Reconciliation Program resulted in a 400 percent increase of assessments. The K-2 delinquency feature of the program allowed DOR staff to identify and contact 100 percent of employers who failed to submit wage and tax statements (Form W-2).
- Revenue Operations staff utilized employer information in the W-2 Reconciliation Program to reduce by 50 percent the number of inquiries to individual taxpayers when returns were received without W-2s.
- Continued to use 1099 information received from the IRS to match against Kentucky DOR returns identifying taxpayers who are not filing with DOR. The DOR collected over \$1.3 million from this initiative in Fiscal Year 2003-04.
- Continued a cooperative effort with Transportation Cabinet to identify and assess motor fuels tax violators.
- Increased compliance emphasis on pretax items such as health insurance claimed as a subtraction on Schedule M.
- Improved efficiencies of the Corporation Tax Branch by using the new Corporation Coding Program. Its new features make it more accessible to staff. The query function enables staff to better identify areas of noncompliance.
- Enhanced compliance efforts via an information exchange agreement with Tennessee on exempt out-of-state all terrain vehicles (ATV) purchases, as well as increased compliance efforts on exempt in-state ATV purchases.

Taxpayer Service

Office of Taxpayer Ombudsman

On June 3, 2004, Secretary Robbie Rudolph appointed David Fallis Ombudsman for the Department of Revenue. Fallis is a graduate of the University of Kentucky. He has worked for the Kentucky Department of Revenue (DOR) for more than 29 years primarily in the field of Taxpayer Assistance. He has served as the supervisor for the Individual Income Taxpayer Assistance area and as the Individual Income Taxpayer Assistance Response Webmaster. He is an outstanding advocate for the taxpayers of Kentucky.

The Office of Taxpayer Ombudsman serves as the taxpayers' rights advocate when taxpayers or practitioners contact the Ombudsman for assistance in the resolution of complaints and problems. It is the responsibility of the Ombudsman's Office to coordinate a fair and equitable resolution with the taxpayer and DOR.

Referrals on behalf of taxpayers are also received from fellow DOR employees, local officials and other state or federal agencies. The office also serves as liaison to both the executive and legislative branches of government and routinely works with the Offices of Constituent Services in the Governor's Office and the Legislative Research Commission to coordinate responses to correspondence and inquiries received regarding tax matters.

The staff worked on a variety of issues this year which included:

- assisted taxpayers with the resolution of a tax bill or pending refund;
- coordinated the settlement of delinquent property tax bills with local officials and DOR staff;
- obtained waiver of civil penalties when reasonable cause for waiver was demonstrated;
- participated in the implementation of allowance of credit card payments and e-payments.
- participated in phases of streamlining Kentucky sales tax;
- coordinated the reduction or removal of wage and bank levies and assisted in obtainment of payment agreements when the taxpayer would have suffered significant hardship as a result of the levy;
- coordinated release and removal of tax liens from taxpayer records when just cause was presented;
- assisted taxpayers in their requests for a payment plan;
- assisted taxpayers in the Offer in Settlement program;
- assisted taxpayers in resolving issues regarding vendor and refund offsets;
- improved *Your Rights As A Kentucky Taxpayer* brochure to increase public awareness on fairness issues;

- prompted changes to the billing method on purchases of all terrain vehicles (ATVs) in regard to exemption of sales tax;
- continued to update contacts for the department on foreign and sign language employee availability to better assist the limited-English-speaking [LEP];
- maintained notary listing and useful contact listing for the department; and
- answered the hearing impaired phone [TDD] for those requiring assistance. [502-564-3058]

As the advocate for the taxpayer, the staff of the Ombudsman's Office serves on various committees to provide input on forms, legislation and training and educational programs.

Designed Ombudsman Public Web site

Responding to the needs of the taxpayers, the ombudsman and staff worked to implement a Web site for anyone who wanted to contact or learn more about the functions of the office. The Web site is revenue.ky.gov/ombud. Categories such as the frequently asked questions, the mission of the office, and e-mail address of the ombudsman were placed on the Web site to enable easy access to the office.

Staffing of the Ombudsman Office

On Aug. 30, 2003, the taxpayer's ombudsman office went through a major transition. Betty Claycomb retired from the office after 34 years of service in state government. She was instrumental in the start-up of the office, as well as the developer of the many programs and functions of the office. It was necessary to add staffing to accommodate the demands of the public.

On Sept. 1, 2003, the acting ombudsman requested appropriation from the Personnel Cabinet for two additional staff members. By December 2003, these two positions were filled. The level of expertise in the office now includes one 19-year veteran of the DOR and one 15-year veteran. In addition, one employee was added from the division of collections, which allowed support for the taxpayer on the collection programs such as levies and liens. Finally, the office was fortunate to keep one long-time employee who had been with the office since its inception May 16, 1991. In accordance with KRS 131.071, the statute calls the Ombudsman's Office to be staffed "...with such personnel as may be deemed necessary to carry out the spirit and the specific purposes of this act."

The office will continue to serve the public in the intent of the statute with the expertise and experience of the tenured staff as well as the additional staff.

2004 General Assembly



A Review of Tax Law Changes Enacted by the 2004 General Assembly

(This legislative summary was compiled by the staff of DOR's Division of Legislative Research)

This legislative summary was compiled by the staff of the Department of Revenue's (DOR) Division of Tax Policy and is intended to present only general information concerning the major provisions of the legislation. This summary should not be construed to represent a complete analysis or specific interpretation of the law changes. Information that is more specific will be provided to taxpayers as the legislative changes are implemented. Full text of enacted bills is available on the Kentucky Legislative Research Commission home page www.lrc.state.ky.us.

The 2004 Kentucky General Assembly enacted several bills affecting Kentucky's taxpayers. The tax portion of each bill is described in this review together with other bills that have some impact on the Kentucky DOR. Unless otherwise indicated, the changes became effective July 13, 2004. For convenience, the enacted bills described in this review are grouped by tax type. When applicable, bills referencing multiple taxes are listed under each of the referenced taxes.

CENTRALIZED DEBT COLLECTION

Administrative Collection Actions—Requires each executive branch agency and the Courts of Justice to develop and maintain an accounts receivable system so that it can properly inventory all debts owed to it. Once the debts are identified, the agency and the Courts of Justice are required to commence administrative collection actions within 60 days. After the debts have become final, due and owing, i.e., all appeal remedies have either been exhausted or waived, the debts must be certified and referred to DOR to determine if it would be cost effective for the department to pursue additional collection action. **(HB 162)**

Recovery of Improper Payments—(Effective April 22, 2004) Requires the Finance and Administration Cabinet to develop an internal audit procedure for all executive branch agencies to identify *improper payments* that are defined as payments to a vendor, provider or other recipient due to error, fraud or abuse. If an executive branch agency makes an improper payment, it has 60 days after discovering the payment to recover it for the benefit of the agency. If the agency is unable to make the recovery within the allotted time, the debt must be referred to DOR to determine the feasibility and cost effectiveness of the department collecting the debt. **(SB 228)**

Disposition of Recovered Funds—Provides that if DOR pursues collection of debts on behalf of other executive branch agencies and the Courts of Justice, the recovered funds, after deductions for the department's cost of collection, will be deposited into the General Fund unless otherwise mandated by federal law. **(HB 162)**

Participation in Refund and Vendor Offset Program —Requires the participation of each executive branch agency and the Courts of Justice in DOR's Individual Income Tax Refund Offset Program and in the Vendor Offset Program through the State Treasurer's Office. **(HB 162 and SB 228)**

SCHOOL TAX

Centralized Collection of School Tax—(Effective July 1, 2005) Transfers the administration, distribution and compliance responsibilities relating to the utility gross receipts license tax (school tax) imposed by most of the commonwealth's 176 local school districts to DOR. **(HB 163)**

2004 General Assembly

TRUSTS AND ESTATES

Trusts And Estates—(Effective Jan.1, 2005) Adopts the Kentucky Principal and Income Act by creating new sections to KRS Chapter 386; establishes definitions; establishes provisions pertaining to decedent's estate or terminating income interest; establishes apportionment at beginning and end of income interest; establishes allocation of receipts during administration of trust; establishes allocation of disbursements during administration of trust; and repeals the Kentucky Revised Uniform Principal and Income Act. **(HB 517)**

INDIVIDUAL and CORPORATION INCOME TAXES

Tobacco Quota Buydown Exemption—Exempts moneys that might be received from a tobacco quota buydown from the state income taxes imposed on individuals and corporations. **(HB 97)**

INDIVIDUAL INCOME TAX

Economic Revitalization Projects—The job assessment fee that may be required of employees whose jobs are preserved or created as a result of the project may not exceed 5 percent of the gross wages subject to income tax (previously 6 percent). Employees who are assessed this fee may claim an individual income tax credit for 4/5 of the assessment (previously 2/3). However, if an appropriation agreement is consummated, then the assessment will be 4 percent of wages (previously 5 percent) and the individual income tax credit is equal to 100 percent of the assessment (previously 4/5). Also, if the project is located in an area where the local government or governments assess an occupational license fee of less than 1 percent, then the assessment fee and individual income tax credit will equal 4 percent of wages plus the amount of occupational license fee that local government agreed to forgo. The assessment fee and individual income tax credit is 4 percent of wages if the project is located in an area where the local government or governments do not impose an occupational license fee. Further, employees who are assessed this fee are also entitled to a credit against any local occupational license fee equal to 1/5 of the assessment (previously 1/6) or equal to the amount of the local occupational license fee if the appropriation agreement is consummated.

If the authority has entered into a preliminary agreement with a taxpayer prior to 90 days after the adjournment of the 2004 legislative session, then the taxpayer has a one-time option to choose whether to operate under the new or old provisions. Also, if a taxpayer has entered into a final agreement, then the taxpayer may choose whether to operate the job assessment fee under the new or old provisions. **(HB 593 and SB 248)**

CORPORATION TAXES

Bank Holding Companies—(Effective for tax returns due without regard to extension on or after April 15, 2004) Retroactively reinstates the deduction option provided by KRS 136.071 that was eliminated by the **Illinois Tool Works** decision. A bank holding company as defined in KRS 287.900 may deduct from its taxable capital the book value of its investment in the stock or securities of subsidiaries that are subject to the bank franchise tax. A bank holding company must own more than 50 percent of the outstanding stock of a bank subsidiary in order to claim the deduction for that subsidiary. This legislation does not permit the filing of disbursements during administration of trust and repeals the Kentucky Revised Uniform Principal and Income Act. **(HB 517)**

Corporation License Tax Returns for Corporations other than Bank Holding Companies—No legislation was passed by the 2004 General Assembly concerning the reinstatement for corporations other than bank holding companies of the corporation license tax benefits formerly offered by KRS 136.071. The 2003 General Assembly had enacted HB 390 to effect a partial reinstatement (90 percent) of these benefits for qualifying corporations for tax returns due without regard extension on or after April 15, 2004, but before April 15, 2005.

Former Gov. Patton vetoed these corporation license tax provisions of HB 390, however, and this veto is being challenged in the case of **Citizens National Corporation v. Rudolph**, 03-CI-00917, now pending before the Franklin Circuit Court.

2004 General Assembly

In light of the extraordinary legal uncertainty presented by this sequence of events, corporations other than bank holding companies, which are governed by HB 292, will be permitted by DOR the vetoed provisions of HB 390 for the time being, until a final and unappealable decision is rendered in *Citizens National Corporation v. Rudolph*. If the veto is upheld by the courts in *Citizens National*, and if no legislation to the contrary is enacted, the taxpayers affected will be required to pay additional amounts of corporation license tax representing the full amount of corporation license tax that would have been due had HB 390 not been enacted. However, those taxpayers will not be required to remit penalties or interest on those additional amounts if they have complied with the provisions of HB 390. Details on how to calculate license tax under the provisions of HB 390 may be found at DOR's Web site at revenue.ky.gov/pdf/hb390.pdf.

Economic Development Incentives—Increases the amount of tax credit available under the Kentucky Industrial Revitalization Act (KIRA) to 75 percent of approved costs. The KIRA corporation license tax credit language of KRS 136.0704 was changed to allow credit for the license tax attributable to the entire location of the project. This bill also tightens up the state's authority to terminate economic development projects that do not meet the targeted employment amounts. **(HB 593)**

Rural Economic Development Incentives—Exempts nonprofit corporations that employ handicapped and sheltered workshop employees at federally established subminimal wages from minimum wage requirements established for companies that seek rural economic development incentives. **(SB 231)**

Economic Revitalization Projects—Increases the amount of tax credit available under KIRA to 75 percent of approved costs. KIRA corporation license tax credit language of KRS 136.0704 was changed to allow the credit to be for the license tax attributable to the entire location of the project. These provisions were also enacted by HB 593. **(SB 248)**

Kentucky Investment Fund Act—(Effective after July 1, 2004) An investment fund approved by the Kentucky Economic Development Finance Authority (KEDFA) that qualifies for tax credits pursuant to the Kentucky Investment Fund Act may invest up to 100 percent of its committed cash contributions in a single knowledge-based entity. A city, county other local government entity or any entity approved by KEDFA may invest in an investment fund created for the purpose of investing in a single knowledge-based entity and may transfer the approved tax credits to a private entity. **(HB 292)**

TOBACCO

Escrow Payments by Nonparticipating Manufacturers—Allows the attorney general to promulgate administrative regulations requiring nonparticipating manufacturers to make quarterly escrow payments and to produce information sufficient to enable the attorney general to determine the adequacy of the escrow payments. Also requires nonparticipating manufacturers to base their escrow payments on the number of cigarette units sold in the state. **(HB 97)**

HAZARDOUS WASTE ASSESSMENT FEE

Extension of Hazardous Waste Assessment Fee— Extends collection of the hazardous waste assessment fee until June 30, 2006, rather than June 30, 2004. **(SB 222)**

Extension of Underground Storage Tanks Program— Extends the small operators assistance program and the time tank owners can file for assistance to Jan. 15, 2008; requires tanks installed after July 15, 2004 to be registered in order to participate in the fund, as well as requiring that all currently existing tanks be registered by July 15, 2006; and allows reimbursements for corrective action to be submitted through July 15, 2013. Additionally, it deletes July 15, 2010 as the deadline for submission of petroleum storage account claims. **(SB 224)**

EXCISE TAX

Reimbursement of Manufacturer's Excise Tax—Reimbursement to a manufacturer for the excise taxes as found in Subchapter A of the Internal Revenue Code will not be required more than one business day before the tax has to be remitted by that manufacturer. Subchapter A deals in part with petroleum products. **(HB 297)**

2004 General Assembly

PARI-MUTUEL TAX

Harness Track Exemption—Exempts harness tracks from paying the pari-mutuel excise tax imposed by KRS 138.510(2)

Wagering Hub—Allows for the establishment of an international wagering hub and further provides that such an entity would be exempt from the race track admissions tax, the pari-mutuel tax and the license tax on race meetings. **(HB 708)**

PROPERTY TAX

Calculation of Taxable Capital—Allows a revised method of calculating taxable capital for some Agricultural Credit Associations. **(HB 292)**

Taxation on Abandoned Urban Property—Allows any city of the second to sixth class to levy a separate rate of taxation on abandoned urban property and provide a list of abandoned properties to the county property valuation administrator. **(HB 373)**

Tax Levy by Fire District—Allows a fire protection district or a volunteer fire department district that operates an emergency ambulance service and is the primary service provider in the district to levy a tax upon the property in the district of up to 20 cents per \$100 of value. **(HB 406)**

Delinquent Property Taxes—Exempts certificates of delinquency in metro Louisville from the requirements for advertising and sheriff's sale; additional costs, including attorneys fees, allowed in liens placed upon delinquent property; expands the list of costs subject to the calculation of the 12 percent interest to include advertising costs, a \$5 sheriff's fee, the county clerk's fee and the county attorney's fee, allowed for metro Louisville and any other county that passes an enabling ordinance. **(HB 510)**

Notice of Expiration of Tax Items in Budget

The following tax provisions appeared in HB 269, the budget bill for Fiscal Years 2002-2004. These provisions, therefore, will expire with the current budget on June 30, 2004:

- the provision that limited the cap on vendor compensation for sales tax to \$1,500 will expire;
- the provision imposing sales tax on natural gas transmission and distribution charges will expire;
- the cigarette compensation to wholesalers will return from 15 cents to 30 cents face value for each \$3 of cigarette tax evidence.

For financial planning purposes, please be advised that these provisions, which expired June 30, 2004 did appear in both the House and Senate versions of the proposed budget bills this last session. There remains, therefore, the possibility that the General Assembly could re-enact these provisions retroactively in the budget when it is passed.

Legal Issues

Legal Developments and Court Decisions

Office of Legal Services for Revenue (OLS)

OLS, formerly the Division of Legal Services, represents DOR in judicial actions and in administrative proceedings before such tribunals as the Kentucky Board of Tax Appeals and Board of Claims. Its representation of DOR extends to all levels of the state and federal court systems.



OLS performs a wide range of other services and functions, which include: rendering advice and written legal opinions to DOR personnel and other government personnel and officials, as well as taxpayers; reviewing and drafting proposed statutes and regulations; analyzing tax laws and assisting with and advising on their implementation and administration; assisting with the preparation of DOR informational publications; handling open records and disclosure matters; and providing assistance and advice in connection with audits, protest conferences, and other stages of the enforcement and administration of the tax laws. OLS is not responsible for personnel, bankruptcy, collection and criminal matters, which are handled elsewhere in DOR or the Finance and Administration Cabinet.

During this past year, OLS has continued to handle a substantial caseload presenting a variety of legal issues affecting DOR and requiring work at all levels of the court system and administrative appeals process. The cases it handles frequently have a substantial potential fiscal impact or significant precedential value.

Office of Legal Services for Revenue Legal Developments and Court Decisions

The OLS for Revenue represents DOR in all cases and appeals other than personnel, bankruptcy, collection and criminal cases. In fulfilling this role, the division's attorneys appear on behalf of DOR before the Kentucky Board of Tax Appeals (KBTA) and Board of Claims and at all levels of the state and federal court systems. This representation of DOR embraces the handling of all phases of the litigation process, including discovery, trials, oral argument, motion practice, briefing, hearings and appeals.

During this past year, OLS again handled a number of cases having significant fiscal impact or precedential value. These cases presented a wide range of issues and involved a number of the taxes administered by DOR. OLS continues to experience an increase in both the complexity of the issues and amounts of money at stake in the cases it handles.

The cases handled by the OLS address issues, or have resulted in precedents, of significant importance and interest to taxpayers and the Commonwealth. Following is a discussion of a number of these cases.

Revenue Cabinet v. O'Daniel, 2001-SC-01032, Kentucky Supreme Court and *Curtsinger v. Revenue Cabinet*, 2002-SC-00204, Kentucky Supreme Court

In these motor vehicle property taxes, the taxpayers purchased vehicles before the January 1 assessment date. While the taxpayers took possession of the vehicles and executed binding purchase agreements before January 1, the automobiles in question were not registered and titled in the taxpayers' names until after that assessment date.

The taxpayers contend that they were not responsible for the property taxes on these automobiles because they were not the record owners as of the January 1 assessment date. DOR's response is that the taxpayers were the equitable owners of these vehicles as of the assessment date and this ownership suffices to impose liability.

The Court of Appeals agreed with the taxpayers in one case (*O'Daniel*); the Franklin Circuit agreed with DOR in the other (*Curtsinger*). These cases are now before the Kentucky Supreme Court, where briefs have been filed and oral argument held. The parties are currently awaiting a decision from the Supreme Court.

LWD Equipment, Inc. v. Revenue Cabinet, Ky., 136 S.W.3d 472 (2004)

On June 17, 2004, the Kentucky Supreme Court rendered a decision in the Department's favor on the occasional sale exemption issue in this sales and use tax case. The taxpayer's sole function was to purchase a variety of equipment needed by its sister corporations and to lease that equipment immediately after purchase to the sister corporation needing it. This leasing activity was engaged in by the taxpayer on a repeated, ongoing and continuous basis. The taxpayer and its sister corporations were all wholly-owned by the same parent. The taxpayer did not sell or lease tangible personal property to anyone else.

The taxpayer asserted that its leases of equipment to its sister corporations were exempt occasional sales as defined in KRS 139.070(1)(b). It contended that each lease was a "transfer of all or substantially all the property held or used by" it in the course of "an activity for which it was required to hold a seller's permit" and that after each such transfer, the real or ultimate ownership of the leased property was substantially similar to that which existed before the transfer. Essentially, the taxpayer advocated

Legal Issues

disregarding its other ongoing leases of equipment in applying this exemption.

The Kentucky Supreme Court's opinion rejects the taxpayer's argument. It rules that the occasional sale exemption does not apply. Under the taxpayer's interpretation of this exemption, all leases could be exempted from taxation even though the sales and use tax law has clearly been extended to leases. Under the taxpayer's theory, a lessor could claim that its initial purchase is not subject to tax as a purchase for resale under 103 KAR 28:051 § 1(3). Then it could claim that the subsequent lease is an occasional sale, regardless of whether the lessor was otherwise engaged in multiple leases on a continuous or ongoing basis. The Supreme Court observed that under the taxpayer's theory, "[a]ny business operation could simply set up a holding company to avoid all sales and use taxes on its equipment." The court further stated that the taxpayer's interpretation of KRS 139.070(1)(b) "would make the statute unreasonable and produce an absurd result."

Finally, the Supreme Court ruled that the KBTA did not have to be named as an indispensable party to the taxpayer's appeal from the KBTA's decision to the circuit court. This decision is now final.

Popplewell's Alligator Dock No. 1 v. Revenue Cabinet, **Ky., 133 S.W.3d 456 (2004)**

On April 22, 2004, the Kentucky Supreme Court rendered an opinion in DOR's favor in this case.

The taxpayers in this case operated Kentucky marinas. As part of their retail operations, they leased houseboats to the public for recreational and vacation purposes. A person renting a houseboat took possession with a full tank of gasoline and was required to return the houseboat at the conclusion of the rental term with a full tank of gasoline.

If upon a houseboat's return the gasoline tank was not full, the taxpayers would refill the tank and charge the lessee an additional amount for the gasoline. The taxpayers contended that these gasoline sales, as well as the houseboat rentals themselves, were exempt from sales and use tax under KRS 139.483, which states that tax "shall not apply to the sale of, or the storage, use, or other consumption of, ships and vessels, including property used in the repair or construction of, supplies and fuel consumed in the operation of, and supplies consumed by crew members aboard such ships and vessels which are used principally in the transportation of property or in the conveyance of persons for hire."

The Supreme Court held that the exemption did not apply. The court ruled that this exemption "is restricted to vessels used principally: (1) 'in the transportation of property,' and (2) 'in the conveyance of persons for hire.'" "[T]he houseboats [in question] were not used principally for either purpose; they were used principally to provide lodging to vacationers and for their recreational purposes." The court noted that "[a]ny transportation of property was extremely insignificant and, like any conveyance of persons accomplished, was ancillary to the primary purposes of lodging and recreation" served by the houseboats.

The Kentucky Supreme Court also rejected Alligator Dock's contention that denial of the exemption would result in a violation of the equal protection provisions of the state and federal constitutions. The court held that a statutory classification will withstand equal protection challenge if there is any reasonably conceivable state of facts that could provide a rational basis for the classification. The court agreed with the cabinet that a rational basis existed for the distinction in question: the General Assembly could reasonably have viewed houseboats and other recreational vessels as playing a different role in the economy and operating in a different competitive market or environment than ships and vessels used principally in the transportation of property or conveyance of persons for hire. Furthermore, the latter types of vessels could reasonably have been viewed by the General Assembly "as creating more-and-better-paying jobs than recreational vessels." Thus, the Supreme Court found that the reasons for the legislative classification assailed by Alligator Dock were at least plausible and accordingly concluded that KRS 139.483 was constitutional.



Finally, the taxpayers had sought injunctive and declaratory relief in the Franklin Circuit Court based upon their assertion that their houseboat rentals and gasoline sales were exempt from tax under KRS 139.483. The Supreme Court ruled that the circuit had correctly dismissed this original action because of the taxpayers'

failure to exhaust their administrative remedies. The court held that a taxpayer must demonstrate that the administrative remedy is inadequate or would be an exercise in futility before it can proceed directly to circuit court for relief. In this case, the taxpayers had an adequate administrative remedy available to them, which they were required to pursue. Additionally, the mere presence of a constitutional issue will not excuse a party's failure to exhaust administrative remedies prior to seeking judicial review of an as-applied constitutional challenge."

Legal Issues

These previous decisions suggested that exhaustion would not be required -- that is, the administrative process would amount to "an exercise in futility" -- only when the issue in the case was the constitutionality of a statute or regulation on its face. This decision is now final.

Morton Buildings, Inc. v. Revenue Cabinet, 2003-SC-0625, Kentucky Supreme Court

The taxpayer in this use tax case erected prefabricated buildings in Kentucky. The DOR assessed use tax for materials the taxpayer purchased outside Kentucky that were used to assemble building components that made up these prefabricated buildings. The taxpayer did not pay sales tax to the states where these materials were purchased. The taxpayer argued that use tax could not apply because these materials were purchased and used in manufacturing the building components outside Kentucky and the taxpayer had no specific intent to use the materials in Kentucky.



In an opinion rendered on July 25, 2003, the Court of Appeals rejected the taxpayer's argument that use tax did not apply. The court observed that the purpose of the use tax is to act as a backstop to the sales tax by ensuring that transactions in other states are treated just as if they had taken place in this state and been subject to the sales tax. The application of the tax in this case is supported by the sales and use tax regulation 103 KAR 26:070 §6, which states:

In the event any contractor, subcontractor, builder, or contractor-retailer is the manufacturer of the building material or supplies he uses in his construction business, the tax shall apply to the sales price to him of all tangible personal property which enters into the manufacture of such materials or supplies.

The court held that this regulation represented a proper and reasonable clarification of the use tax statute.

The court also noted that the "use" triggering the use tax's application is broadly defined in the statutes as "the exercise of any right or power over tangible personal property." In this case, the materials in question, in their altered form, were actually used in Kentucky when the taxpayer assembled the building components made up of the materials into prefabricated buildings. It was not necessary that the taxpayer know which particular items or materials would be used in erecting a particular building for tax to apply.

On Aug. 18, 2004, the Kentucky Supreme Court denied the taxpayer's motion for discretionary review of the Court of Appeals' opinion. The Court of Appeals' decision is therefore final.

Comcast Cablevision of the South v. Revenue Cabinet, 2003-CA-001007, Kentucky Supreme Court

In this case, the taxpayer was a cable television company with franchises in Kentucky and elsewhere. It was assessed, or valued, for ad valorem tax purposes as a public service corporation pursuant to KRS 136.115 et seq.

The taxpayer challenged its assessments for 1996 and 1997. It presented proof that the fair cash value of the taxpayer's Kentucky cable television "business enterprise" was \$43,100,000 for 1996 and \$44,500,000 for 1997. The taxpayer's expert witness separated this value into "two buckets," one he characterized as the taxpayer's operating property and the other he termed the taxpayer's nonoperating property. The operating property "bucket" was assigned a value of \$26,000,000 for 1996 and \$23,300,000 for 1997. The nonoperating property "bucket" was assigned a value of \$17,100,000 for 1996 and \$21,200,000 for 1997. Nonoperating property is subject to far lower tax rates than operating property.

Under KRS 136.120(1), "[e]very...cable television company shall annually pay a tax on its operating property to the state and to the extent the property is liable to taxation shall pay a local tax thereon to the county, incorporated city, and taxing district in which its operating property is located." Operating property is further defined in KRS 136.115(2) to include both the operating tangible property and the franchise.

The Court held that the property the taxpayer's alleged nonoperating property was really part of the franchise assessable as part of the taxpayer's operating property. The court stated:

After considering the statutory scheme pertaining to the public service corporation property tax, Ky. Const. § 172, and Kentucky case law, we conclude that for the purposes of taxation under KRS 136.120, a "franchise" is the earning value ascribed to the capital or a domestic public service corporation by reason of its operation as a domestic public service corporation. It comprises the operating property and is assessed by the [KRC] by its fair cash value as a unit. In this case, the franchise is the earning value ascribed to [the taxpayer's] capital by reason of its operation as a cable television provider.

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Said another way, the value of the franchise is determined by subtracting the assessed value of the tangible operating property from the "capital stock," which is the "entire operating property from the "capital stock," which is the "entire operating property, real and personal, tangible and intangible, assets on hand, and its franchise as well." ... Thus, the business enterprise value reached in the Kane appraisal is the total of Comcast's operating property--the operating tangible property and the franchise. As assessed by Kane and agreed to by the [KRC], it is the price at which a willing buyer would buy and a willing seller would sell an entire business as of the lien date. The fair cash value of [the taxpayer's] operating property is \$43,100,000 for 1996 and \$44,500,000 for 1997.

The Court of Appeals further held that non-operating intangible property is intangible property, such as certificates of stock, bonds or copyrights that a public service corporation taxpayer does not use in the provision of its public service. In this case, there was no question but that

the taxpayer was engaged solely in the provision of cable television, a public service enumerated in KRS 136.120(1).

The Court of Appeals also found it significant that the taxpayer listed no non-operating property on its public service corporation property tax returns, as it was legally bound to do so under KRS 136.130.



This decision is not yet final. The taxpayer has a motion for discretionary review pending before the Kentucky Supreme Court.

D.C. Contracting Co. v. Revenue Cabinet, 2003-SC-0351, Kentucky Supreme Court

The taxpayer in this case was a contractor performing work on the closure of a chlor-caustic waste lagoon that was part of an overall clean-up of an industrial site that had been ordered by the U.S. Environmental Protection Agency. As a contractor, its purchases of tangible personal property for use in the performance of its work were subject to sales and use tax, as pointed out in 103 KAR 26:070. The contractor did not pay tax on its purchases for the chlor-caustic lagoon project and was accordingly assessed sales and use tax by the cabinet.

The taxpayer contended that the purchases in question were exempt from tax under the pollution control facility exemption now codified at KRS 139.480(12). Agreeing with previous decisions of the KBTA and the Franklin Circuit Court, the Court of Appeals in its opinion rendered on April 11, 2003 held that the taxpayer could not qualify for the exemption because it had not applied for or obtained a pollution control tax exemption certificate, as required by KRS 139.480(12) and 224.01-310. The statutory language requires that this exemption certificate be applied for before making the purchases for which the exemption is to be claimed.

The Court of Appeals rejected the taxpayer's argument that it should receive the benefit of the exemption anyway, because the cabinet had not promulgated a regulation on this subject. The language of KRS 224.01-310(1) relied upon by the taxpayer ("in such form as may be prescribed by regulations issued by the Revenue Cabinet") did not mandate the promulgation of a regulation, by virtue of its use of the permissive term "may." (See KRS 446.010(20).) Moreover, the requirement of an application for a pollution control tax exemption certificate was unambiguously set forth in the statutory language itself, rendering a regulation concerning this facet of the exemption unnecessary.

The Kentucky Supreme Court denied the taxpayer's motion for discretionary review of the Court of Appeals' opinion on April 15, 2004. This decision is therefore now final.

Revenue Cabinet v. GTE South, Inc., 2004-SC-00519, Kentucky Supreme Court

On April 2, 2004, the Court of Appeals held that a sales and use tax assessment had not been issued in a timely manner in accordance with KRS 139.620. DOR had sent the taxpayer two documents concerning the assessment: 1) an assessment letter setting forth the basis and amount of the assessment and including as enclosures an auditor's narrative report with supporting schedules; and 2) formal notices of tax due stating the amounts of taxes, penalties and interest due.

The Court of Appeals ruled that the assessment letter was issued in a timely manner. The KBTA's decision to the contrary was not supported by substantial evidence. The timeliness of the assessment letter, however, did not result in compliance with KRS 139.620, the court ruled. The Court of Appeals held that a notification of an assessment must contain all of the information specified in KRS 131.081(8) to satisfy KRS 139.620(1). The assessment letter did not include the amounts of the penalties and interest due and thus did not satisfy KRS 131.081(1). The notices of tax due did state these amounts, but these notices were mailed beyond the four-year deadline prescribed by KRS 139.620(1).

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Nevertheless, the Court of Appeals ruled that the taxpayer was not necessarily entitled to the refund it sought for the period for which the assessment had been made. Under KRS 134.580, a taxpayer is entitled to a refund only if he can establish that he overpaid his taxes for the period in question. The Court of Appeals held that even though the assessment in question was barred by the statute of limitations KRS 139.620(1), DOR had the right to retain payments of tax already received for the period in question to the extent those payments did not exceed the amount that might have been properly assessed and collected. In other words,

the fact of the underpayment represented by the time-barred assessment could nevertheless be used by DOR to establish that there was no overpayment for the period in question and thus no entitlement to a refund.

DOR has a motion for discretionary review pending before the Kentucky Supreme Court. Therefore, the Court of Appeals' opinion is not final.

Pipefitters Joint Education and Training Fund v. Revenue Cabinet, 2004-SC-00282, Kentucky Supreme Court

On Jan. 27, 2004, the Court of Appeals ruled that property tax exemption to the Pipefitting Joint Educations and Training Fund. The specific exemption claimed by the fund was the one provided for in Ky. Const. §170 for “institutions of education not used or employed for gain by any person or corporation, and the income of which is devoted to the cause of education.”

In this case, the KBTA found that the fund's primary purpose was the promotion of union membership and that any benefit to the public was only secondary. The fund provided services, instruction and educational classes to individuals desiring to become pipefitters. While anyone could apply to attend the fund's programs, those admitted as students were required to complete an apprenticeship in a union shop with a union employer, which entailed an apprentice's joining the union. The applicants signed agreements as part of their entry into the fund's program that required them to reimburse the fund for the costs of the training program if they did not satisfy any of the program's requirements, which included the apprenticeship.

The KBTA further found that while the fund taught “certain courses that are traditional in nature, such as math, computer science and telecommunications”... “these courses [were] not taught in a general way but [were] geared to the [p]ipefitters trade exclusively.” Moreover, the attendees of the fund's program did not receive any college credits nor

were any credits obtained by the fund's program attendees recognized by the Commonwealth of Kentucky “as applicable to a college degree.”

The Court of Appeals concluded that “substantial evidence [in the record] supports the [KBTA's] determination that [the fund] is an essentially private organization with the primary intention of promoting union membership.” The court noted that exemptions from taxation must be strictly construed and the exemption for educational institutions is founded upon the ground of benefit to the public and their performance of a service the state would or should otherwise have to perform. To be exempt as an educational institution, the organization must also be “a place where systematic instruction in any or all of the useful branches of learning is given by methods common to schools and institutions of learning.” The fund did not meet these requirements.

The Court of Appeals' decision is not yet final. The fund has a motion for discretionary review pending before the Kentucky Supreme Court.



DOR Administration

DOR Administrative Expenditures

DOR administrative expenditures for Fiscal Year 2003-2004 totaled \$67,002,731. The types of appropriated funds that support ongoing operations include General, Road, Restricted and Federal funds.

ADMINISTRATIVE COSTS FISCAL YEAR 2003-2004

	General Fund	Agency Fund	Federal Fund	Road Fund	Tobacco Settlement Fund	Total
Salaries full-time	\$35,422,032	\$1,783,398	\$	\$ 0	\$ 0	\$ 37,205,430
Fringe benefits	7,892,803	328,636	0	6,222	0	8,227,661
Seasonal employees	702,034	2,722	0	0	0	704,756
Overtime/block 50s	163,564	1,770	0	0	0	165,335
Training and tuition assistance	65,453	0	0	579	0	66,033
Workers' Compensation	186,683	0	0	0	0	186,683
Unemployment Compensation	92,734	0	0	0	0	92,734
Legal/audit services/consultants	521,291	0	0	0	0	521,291
Advertising/Misc. Services	3,450	0	0	0	0	3,450
Janitorial services	274,982	0	0	0	0	274,982
Data entry/temporary services	9,945	0	0	0	0	9,945
Security	151,339	0	0	0	0	151,339
Total Personnel	\$45,486,311	\$2,116,527	\$ 0	\$ 6,801	0	\$ 47,609,639
Carpool (state motor pool)	\$ 16,485	\$ 2,997	\$ 0	\$ 15,184	0	\$ 34,666
Utilities	381,720	0	0	10,062	0	391,782
Rent/rentals	3,001,559	0	0	0	0	3,001,559
Maintenance and repairs	534,879	0	0	0	0	534,879
Postage	2,822,683	0	0	120,000	0	2,942,683
Printing/other services	946,000	240,188	0	113,982	175,000	1,234,982
Information technology (includes GOT costs)	8,673,453	0	0	570,000	0	9,243,453
Office Supplies	248,369	12,925	0	116,240	0	377,534
Furniture	83,124	0	0	1,191	0	84,316
Banking Services	21,507	0	0	0	0	21,507
Storage Fees	9,238					9,238
Travel	244,757	295,783	0	316,248	0	856,788
Filing/lien/collection fees	3,281	179,316	0	2,464	0	185,060
Dues/subscriptions services	223,412	122,341	0	128,893	0	474,646
Total Operating	\$17,210,466	\$613,362	\$ 0	\$ 1,394,265	\$ 175,000	\$ 19,393,093
Total Expenditures—Revenue	\$62,696,776	\$2,729,889	\$ 0	\$1,401,066	\$175,000	\$ 67,002,731

DOR Administration

DOR offices, divisions and their duties

The Department of Revenue is the state agency that administers the tax laws of the commonwealth and bills and collects the tax revenue necessary to support state services.

Disclosure Branch

The Disclosure Branch is the liaison between the Department of Revenue and the Internal Revenue Service, and other agencies of federal, local and state government. The branch administers the provisions of KRS 131.190 to ensure the confidentiality of taxpayer information and protect against unauthorized use or release. Additionally, this branch is responsible for granting electronic security access to Revenue information systems and physical access to Revenue facilities.

Division of Legislative Services

The Division of Legislative Services provides technical support and research assistance; performs studies, surveys and research projects to assist in policy-making decisions; coordinates development and drafts proposed tax legislation and regulations; coordinates review of tax legislation; and testifies before legislative committees on tax matters.

Office of Processing and Enforcement

The Office of Processing and Enforcement is responsible for promoting the enterprise services available to the commonwealth related to document processing, depositing of funds and collecting debt. Additionally, the office is responsible for coordinating, planning and implementing a data integrity strategy. The office consists of the following three divisions:

The Division of Operations is responsible for opening all incoming tax returns, preparing the returns for data capture, coordinating the data capture process, depositing receipts and maintaining the tax data. Additionally, the division assists other agencies with similar operational aspects as negotiated with that agency.

The Division of Collections is responsible for initiating all collection enforcement activity related to due and owing tax assessments, including issuing liens and levies. Additionally, the division is prepared to assist other agencies with similar collection aspects as negotiated with that agency.

The Division of Registration and Data Integrity is responsible for registering taxpayers and ensuring that the data entered into the department's tax systems is accurate and complete. The Taxpayer Registration Section processes all business tax applications and assists registrants as needed during the process. The Registration Compliance Section ensures a level playing field

for businesses operating in Kentucky by contacting those that may have overlooked their tax registration obligations. Additionally, the division assists the taxing areas in proper procedures to ensure that the data remains accurate over time.

Office of Taxpayer Ombudsman

The Office of Taxpayer Ombudsman is responsible for carrying out the spirit and specific purposes of the Taxpayer Bill of Rights, including: coordinating the resolution of taxpayer complaints and problems; providing recommendations for new or revised informational publications and taxpayer and department employee education programs; and providing recommendations for simplification or other improvements needed in tax laws, regulations, forms, systems and procedures to promote better understanding and voluntary compliance by taxpayers.

Office of Property Valuation

The Office of Property Valuation is responsible for administering all matters related to property and severance taxes. This includes technical tax research, compliance, taxpayer assistance, tax specific training, public announcements, publications, forms and any other matter related to those taxes. The office consists of the following divisions:

The Division of State Valuation is responsible for administering all centrally assessed taxes including public service property tax, motor vehicle property tax and the tangible/intangible program.

The Division of Local Valuation is responsible for overseeing the real property tax assessment and collection process throughout the state in the 120 PVA and sheriffs' offices.

The Division of Minerals Taxation and GIS Services is responsible for administering the taxes related to severance tax and the unmined minerals property tax. It also coordinates the department's GIS mapping efforts. It contains three branches: mineral resource valuation; mineral assessment compliance; and cartography/GIS.

DOR Administration

Office of Sales and Excise Taxes

The Office of Sales and Excise Taxes is responsible for administering all matters related to sales and use tax and the miscellaneous excise taxes. This includes technical tax research, compliance, taxpayer assistance, tax specific training, public announcements, publications, forms and any other matter related to those taxes. It includes the divisions of Sales and Use Tax and the Miscellaneous Taxes.

The Division of Sales and Use Tax is responsible for administering the sales and use tax. It has two branches: Program Compliance and Taxpayer Assistance. The branches are responsible for conducting office audits, administering various exemption programs, initiating compliance activities, assisting taxpayers and discovery of non-filer populations.

The Division of Miscellaneous Taxes is responsible for administering the following taxes: alcoholic beverage taxes; cigarette enforcement fee, stamps, meters and taxes; environmental remediation fee; gasoline tax; inheritance and estate tax; insurance premiums and insurance surcharge taxes; bank franchise tax; legal process; marijuana and controlled substance; motor vehicle tire fee; motor vehicle usage taxes; PSC annual assessment; pari-mutuel excise, racing license and admissions taxes; RECC and RTCC; special fuels taxes; and underground storage fee. It consists of two branches: Road Fund Branch and Miscellaneous Tax Branch.

Office of Income Taxation

The Office of Income Taxation is responsible for administering all matters related to the individual income, withholding, corporation income and corporation license taxes, including technical tax research, compliance, taxpayer assistance, tax specific training, public announcements, publications, forms and any other matter related to those taxes. It consists of the following divisions:

The Division of Individual Income Tax is responsible for administering the returns filed by the following taxpayers: individual income; fiduciary; employer withholding; pass-through entity withholding; and partner-

ship. It consists of two branches: Individual Income Tax Branch and Withholding Tax Branch.

The Division of Corporation Tax is responsible for administering the following taxes and programs: corporation income tax; corporation license tax; pass-through entity withholding; and partnerships. It consists of two branches: Corporation Income and License Tax Branch; and Pass-Through Entity Branch.

Office of Field Operations

The Office of Field Operations is responsible for managing the regional taxpayer service centers and field audit program.

The Audit Support and Training Branch is responsible for supporting the work of Revenue field auditors and compliance officers throughout the commonwealth, including the support related to computer-assisted audits, audit selection and training.

The 10 regional offices are geographically divided among three regional managers to oversee the field operations of the commonwealth. Region 1 consists of Ashland, Northern Kentucky and Pikeville Taxpayer Service Centers. Region 2 consists of Louisville, Corbin and Bowling Green Taxpayer Service Centers; and the Audit Selection Section. Region 3 consists of Hopkinsville, Central Kentucky, Owensboro and Paducah Taxpayer Service Centers.

PVA Offices (Accounting)

This office provides budget, fiscal, personnel and payroll administration for all 120 PVAs and more than 680 deputies throughout the commonwealth. It also coordinates open enrollment for health and life insurance and directs property tax educational KY-Courses. It conducts workshops at summer and fall PVA conferences and meetings.

**MANAGEMENT—KENTUCKY DEPARTMENT of REVENUE
JUNE 30, 2004**



Mark Treesh
Commissioner

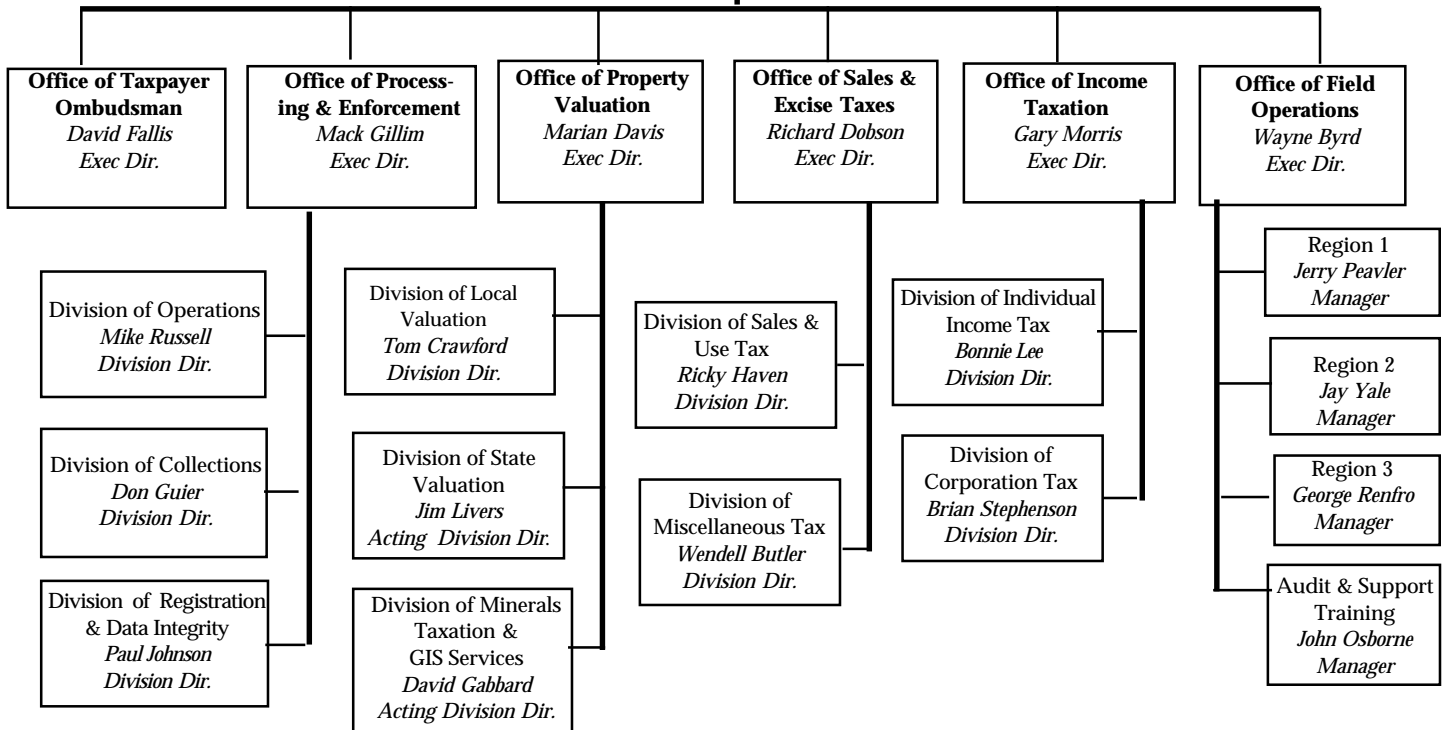
DEPARTMENT of REVENUE
Mark Treesh - Commissioner
Tim LeDonne - Deputy Commissioner



Tim LeDonne
Deputy Commissioner

Division of Legislative Services
Eddie Mattingly - Director

Disclosure Branch
Paula Fallis



David Fallis
Taxpayer Ombudsman



Mack Gillim
Processing & Enforcement



Marian Davis
Property Valuation



Richard Dobson
Sales & Excise Taxes



Gary Morris
Income Taxation



Wayne Byrd
Field Operations

TAXES ADMINISTERED BY THE DEPARTMENT OF REVENUE (In Effect as of June 30, 2004)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
Alcoholic Beverage Wholesale Sales Tax	KRS 243.884	9 percent of wholesale sales of distilled spirits, wine and malt beverages.	A wholesale sales tax on alcoholic beverage wholesalers/distributors to be reported monthly. There are statutory exemptions.
Bank Franchise Tax	KRS 136.500 et seq.	1.1 percent of net capital. Minimum tax is \$300 per year.	Tax is imposed on every financial institution regularly engaged in business in Kentucky at any time during the calendar year. A financial institution is presumed to be regularly engaged in business in Kentucky if during any taxable year it obtains or solicits business with 20 or more persons within Kentucky, or if receipts attributable to sources in Kentucky equal or exceed \$100,000. Tax is in lieu of all city, county and local taxes except for the real estate transfer taxes, real property and tangible personal property taxes upon users of utility services and the local deposit franchise tax.
Beer Consumer Tax	KRS 243.720 et seq.	\$2.50 per barrel of 31 gallons.	An excise tax imposed on distributors or retailers of malt beverages who purchase malt beverages directly from a brewer. There are statutory exemptions and credits. There is a 50 percent discount for domestic brewers up to 300,000 barrels per annum.
Cigarette Enforcement and Administration Fee	KRS 365.390	.001 cent per pack (rate subject to change annually).	Fee paid by cigarette wholesalers and unclassified acquirers to provide for the expenses of the Revenue Cabinet in administering the Cigarette Tax Law.
Cigarette Licenses	KRS 138.195	Resident wholesaler \$500 Nonresident wholesaler \$500 Subjobber \$500 Vending machine operator \$ 25 Transporter \$ 50 Unclassified acquirer \$ 50	Annual license fee imposed upon various dealers and handlers of cigarettes. More than one license may be required by the Revenue Cabinet for any dealer or handler depending upon the diversity of his business and the number of established places of business.
Cigarette Tax	KRS 138.130 et seq.	3 cents per 20 cigarettes, proportioned for other quantities.	An excise tax on cigarettes paid by resident and nonresident wholesalers and unclassified acquirer. The tax is paid by purchasing stamps within 48 hours after cigarettes are received by a resident wholesaler. The unclassified acquirer pays the tax by purchasing and affixing stamps within 24 hours of receipt of the cigarettes. A nonresident wholesaler must affix the tax stamps prior to importing them into Kentucky.
Coal Severance Tax	KRS 143.010, 143.020 et seq.	50 cents per ton minimum or 4.5 percent of gross value. (The minimum tax shall not apply to a taxpayer who only processes coal.)	Tax is based on the gross value of coal severed and/or processed in Kentucky. Partial or whole exemptions from the tax may apply to newly permitted production from "thin seams."
Corporation Income Tax	KRS 141.010 et seq., 155.170	First \$25,000 4 percent Next \$25,000 5 percent Next \$50,000 6 percent Next \$150,000 7 percent All Over \$250,000 8.25 percent Business Development Corporations 4.5 percent	Annual tax on the entire net income of the corporation apportioned and allocated to Kentucky. Corporations whose estimated tax liability will exceed \$5,000 must file a declaration of estimated tax due and pay the estimated tax in three installments. Financial institutions as defined in KRS 136.500, except bankers banks organized under KRS 287.135, insurance companies; savings and loan associations; corporations exempted by Internal Revenue Code (IRC) Section 501; and religious, educational, charitable and like corporations not conducted for profit are exempt from corporate income tax. An "electing small business corporation," (S corporation) as defined in Section 1361(a) of the IRC, is recognized as being exempt from Kentucky corporation income tax except for tax on net capital gain of such corporation as provided in KRS 141.040(5). A filing requirement will apply to a corporation that only has a partnership interest in Kentucky, under KRS 141.206. A limited liability company (LLC) is treated for Kentucky income tax purposes in the same manner as its tax treatment for federal income purposes under KRS 141.208. For taxable years ending on or after December 31, 1995, KRS 141.200 allows an affiliated group to elect to file a consolidated Kentucky income tax return with the election binding for 96 consecutive calendar months. KRS 141.200 prohibits affiliated groups from filing a combined Kentucky corporation income tax return using the unitary business concept.

TAXES ADMINISTERED BY THE DEPARTMENT OF REVENUE (In Effect as of June 30, 2004)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
Corporation License Tax	KRS 136.070 et seq.	\$2.10 per each \$1,000 of capital employed in the business. Kentucky tax is based on the amount of such capital apportioned to Kentucky. Minimum tax is \$30.	Annual license tax levied against any corporation owning or leasing property or having an employee in Kentucky. Public service companies, certified alcohol production facilities, certified fluidized bed energy production facilities, and LLCs are exempt from license tax. A corporation with gross income of \$500,000 or less is allowed a credit against the license tax of \$1.40 on each \$1,000 of the first \$350,000 of capital employed.
Distilled Spirits Case Sales Tax	KRS 243.710	5 cents per case.	Excise tax on distilled spirits sold by wholesalers to retailers in Kentucky.
Distilled Spirits and Wine Consumer Taxes	KRS 243.720 et seq.	Distilled spirits containing over 6 percent alcohol by volume per gallon \$ 1.92 per liter 0.5069 Distilled spirits containing 6 percent or less alcohol by volume per gallon \$ 0.25 per liter 0.0660 Wine per gallon \$ 0.50 per liter 0.1320 (Proportionate amount charged on smaller quantities, but not less than 4 cents on any retail container of wine.)	Excise tax imposed upon the use, sale or distribution by sale or gift of distilled spirits and wine. There are statutory exemptions.
Health Care Provider Tax	KRS 142.301 to 142.359	2.5 percent of gross receipts for hospital services. 2.0 percent of gross receipts for nursing facility services, licensed home health agency services, and ICF/MR services.	Effective July 1, 1993, a provider tax is imposed on providers of taxable medical services. Registration is required prior to the beginning of operations.
Individual Income Tax	KRS 141.010 et seq.	First \$3,000 2 percent Next \$1,000 3 percent Next \$1,000 4 percent Next \$3,000 5 percent In excess of \$8,000 6 percent	Graduated tax upon an individual's taxable income. Residents must pay on their entire taxable income. Nonresidents must pay on that portion of their income attributable to Kentucky sources. Fiduciaries must pay on that portion of income of an estate or trust not distributed or distributable to beneficiaries. Tax base is the federal adjusted gross income adjusted for differences in Kentucky and federal laws, including US government bond interest, limited pension/retirement income exclusion, Social Security benefits and Railroad Retirement Board benefits and deductions for long-term care and health insurance premiums. Taxable income is computed by using the standard deduction or Kentucky itemized deductions. Tax credits include personal credits of \$20, child and dependent care, low income, and various business credits. Standard deduction: 2002—\$1,800 2003—\$1,830 2004—\$1,870

TAXES ADMINISTERED BY THE DEPARTMENT OF REVENUE (In Effect as of June 30, 2004)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
Inheritance and Estate Taxes	KRS 140.010 et seq.	Inheritance tax 4–16 percent Estate tax an amount by which the state death tax credit allowable under the federal tax law exceeds the inheritance tax.	The Kentucky inheritance tax is a tax on the right to receive property upon the death of another person. The rate of tax and the exemptions allowed depend on the legal relationship of the beneficiary to the decedent. If the date of death is after June 30, 1998, the following list of beneficiaries are exempt from paying inheritance tax: (1) Surviving spouse, parent; (2) Child (adult or infant)—child by blood, stepchild, child adopted during infancy, or a child adopted during adulthood who was reared by the decedent during infancy; (3) Grandchild—issue of child by blood, stepchild, child adopted during infancy, or of a child adopted during adulthood who was reared by decedent during infancy; (4) Brother, sister (whole or half). The Kentucky estate tax is the amount which the allowable federal estate death tax credit exceeds the Kentucky inheritance tax.
Insurance Premium Surcharge	KRS 136.392	1.5 percent of premiums.	An insurance premium surcharge on insured Kentucky risks. There are statutory exemptions.
Insurance Premium Taxes	KRS 136.320, 136.330 to 136.390, 299.530, 304.3-270, 304.4-030, 304.11-050, 304.49-220	All domestic and foreign life companies 1.6 percent tax rate for calendar year 2003. The tax rate is being lowered by 0.1 percent per year until the rate reaches 1.5 percent. Annuities are exempt from tax. All other insurance companies 2 percent tax rate for calendar year 2003. Fire insurance* 0.75 percent *Represents additional tax on applicable premiums.	Annual tax imposed on insurance companies and risk retention groups based upon premium receipts on business done. There are statutory exemptions.
Legal Process Taxes	KRS 142.010 et seq.	Conveyances of real property (deeds) \$3.00 Mortgages, financial statements and security agreements \$3.00 Marriage licenses* \$3.50 Powers of attorney to convey real or personal property \$3.00 Lien or conveyance of coal, oil, gas or other mineral right or privilege \$3.00	Taxes imposed on the filing of an instrument subject to tax or the issuance of a marriage license. Collected by county clerk. *A \$10 Spouse Abuse Shelter Fund fee levied on marriage licenses by KRS 209.160 is, by agreement between the Revenue Cabinet and the Cabinet for Families and Children, also reported and paid to the Revenue Cabinet by county clerks as part of the monthly report of legal process taxes due.
Marijuana and Controlled Substance Tax	KRS 138.870 et seq.	\$3.50 per gram on marijuana, loose. \$1,000 per marijuana plant. \$200 per gram controlled substance by weight. \$2,000 per 50 dosage units of controlled substance.	Growers, sellers, dealers, buyers and manufacturers must obtain a tax stamp to affix to the product. Commonwealth's or county attorneys who obtain a conviction of, or guilty or Alford plea from an offender must notify the Revenue Cabinet if the product which was the subject of the conviction or plea does not bear the tax stamp.

TAXES ADMINISTERED BY THE DEPARTMENT OF REVENUE (In Effect as of June 30, 2004)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
Motor Fuels Tax—Gasoline	KRS 138.210 et seq.	9 percent of average wholesale price of gasoline, but not less than 10 cents per gallon. Rate determined quarterly. A 5 cent per gallon "Supplemental Highway User Motor Fuel Tax" also applies.	An excise tax paid by licensed dealers on all gasoline received in this state. There are statutory provisions for tax credits and partial or full tax refunds for designated users.
Motor Fuels Tax—Liquefied Petroleum Gas	KRS 234.310 to 234.440	Variable rate same as gasoline. The 5 cent per gallon supplemental tax also applies to liquefied petroleum gas.	An excise tax paid by licensed dealers on all liquefied petroleum motor fuel withdrawn to propel motor vehicles on the public highways, unless the carburetion system has been approved by the Natural Resources and Environmental Protection Cabinet.
Motor Fuels Tax—Petroleum Storage Tank Environmental Assurance Fee	KRS 224.60-145	1.4 cents per gallon.	A petroleum storage tank environmental assurance fee is levied on all taxable gasoline and special fuel reported in this state by licensed dealers. There are provisions for exemptions or refunds for qualifying gasoline or special fuels not to be used on the public highways.
Motor Fuels Tax—Special Fuels	KRS 138.210 et seq.	Variable rate same as gasoline. A 2 cent per gallon "Supplemental Highway User Motor Fuel Tax" also applies.	An excise tax is levied on all special fuels received in this state by licensed dealers. There are statutory provisions for tax credits and partial or full tax refunds for designated users.
Motor Vehicle Usage Tax	KRS 138.450 et seq.	6 percent of the consideration given or retail value as defined in KRS 138.450. Value is dependent on the type of transaction. Optional tax payment method available for U-Drive-It operators based on 6 percent of the gross rental or lease charges.	Tax imposed on new and used motor vehicles when registered for the first time in this state and when ownership is transferred. There are statutory exemptions and credits. Regular usage tax payments are made to the county clerk and forwarded to the Revenue Cabinet. U-Drive-It usage tax payments are made directly to the Transportation Cabinet on a monthly basis.
Natural Resources Severance and Processing Taxes (Minerals, Natural Gas and Natural Gas Liquids)	KRS 143A.010, 143A.020 et seq.	4.5 percent of gross value. 12 cents per ton (clay production). Limestone used in the manufacturer of cement by an integrated miner and manufacturer of cement shall be limited to 14 cents per ton of limestone mined in Kentucky.	<p>Tax of 4.5 percent of the gross value is imposed on every taxpayer engaged in the business of severing and/or processing minerals (including natural gas and natural gas liquids) in Kentucky with the exception of clay. Clay production is taxed at 12 cents per ton. A credit equal to the tax of 12 cents per ton is granted to those taxpayers who sever or process clay sold to and used as a component of landfill construction by an approved waste disposal facility within this state. Also, no tax is imposed on the processing of ball clay.</p> <p>This tax does not apply to fluorspar, lead, zinc, and barite severed for any purposes; or to rock, limestone, or gravel used for privately maintained but publicly dedicated roads; or limestone when sold or used by the taxpayer for agricultural purposes so as to qualify for exemption from sales and use tax.</p> <p>A credit equal to the tax is allowed on the gross value of limestone which is severed or processed within this state and sold to a purchaser outside this state. This credit is extended only to taxpayers who sever or process limestone through the rip-rap construction aggregate of agricultural limestone stages, and who sell in interstate commerce not less than 60 percent of such stone. The credit shall not be allowed to a taxpayer who processes the limestone beyond the agricultural limestone stages.</p> <p>A gas well, which has been plugged and abandoned for a consecutive two-year period that resumes producing, qualifies for the Recovered Inactive Well Tax Credit equal to 4.5 percent of the gross value.</p>

TAXES ADMINISTERED BY THE DEPARTMENT OF REVENUE (In Effect as of June 30, 2004)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
Oil Production Tax	KRS 137.120 et seq.	4.5 percent of market value of crude petroleum produced in Kentucky.	Tax on the production of crude petroleum is attached when the crude petroleum is first transported from the tanks or other receptacle located at the place of production. Transporter of crude petroleum, as agent, pays tax for all persons owning any interest in such oil. An oil well, which has been plugged and abandoned for a consecutive two-year period that resumes producing, qualifies for the Recovered Inactive Well Tax Credit equal to 4.5 percent of the gross value.
Property Taxes: Agricultural Products In hands of producer or agent Tobacco not at manufacturer's plant (Storage) Other agricultural products not at manufacturer's plant (Storage)	KRS 132.020(1), 132.200(6) KRS 132.020(1), 132.200(6) KRS 132.020(1), 132.200(6)	1.5 cents (per \$100 of assessment). 1.5 cents (per \$100 of assessment). 1.5 cents (per \$100 of assessment).	State rate only. Also subject to county and city rates. Also subject to county and city rates.
Aircraft (Not used in the business of transporting person or property for compensation or hire.) (For Hire non Public Service Company)	KRS 132.020(12), KRS 132.200(19) KRS 132.020(1)	1.5 cents (per \$100 of assessment). 45 cents (per \$100 of assessment).	Local option. Subject to full local rates.
Annuities or Rights to Receive Income	KRS 132.215(2)	0.1 cent (per \$100 of assessment).	State rate only.
Bank Deposits Domestic and Out-of-State	KRS 132.030(1)	0.1 cent (per \$100 of assessment).	Tax is based on deposits as of January 1 and is paid by the institution on behalf of the depositors. State rate only.
Brokers' Accounts Receivable (Also see Margin Accounts)	KRS 132.050	10 cents (per \$100 of assessment).	State rate only.
Car Lines (Private)	KRS 136.115-136.180	Subject to annual adjustment.	Subject to annual adjustment. Local tax collected and distributed by the Revenue Cabinet effective January 1, 1994.
Distilled Spirits	KRS 132.020(10), 130.180	5 cents (per \$100 of assessment).	Subject to full local rates.
Farm Machinery Used in Farming	KRS 132.020(1), 132.200(1)	0.1 cent (per \$100 of assessment).	State rate only.

TAXES ADMINISTERED BY THE DEPARTMENT OF REVENUE (In Effect as of June 30, 2004)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
Goods Held for Sale in the Regular Course of Business	KRS 132.020(10)	5 cents (per \$100 of assessment).	Subject to local rates.
Intangible Property of Banks	KRS 132.020(2)	0.1 cent (per \$100 of assessment).	State rate only.
Intangibles Money in hand, notes, bonds, accounts and other credits, except those arising from out-of-state business, or intercompany accounts between parent and subsidiary, and other not specified elsewhere. Accounts receivable, notes, bonds, credits, and other intangibles arising from out-of-state business, and intercompany accounts between parent and subsidiary, patents and copyrights, and tobacco base allotments. State rate only.	KRS 132.020(1), 136.120(2)	25 cents (per \$100 of assessment). 1.5 cents (per \$100 of assessment).	State rate only. State rate only.
Leasehold Interest (Privately owned leasehold interest in industrial buildings)	KRS 132.020(1)	1.5 cents (per \$100 of assessment).	State rate only
Life Insurance Companies (Domestic) Capital Reserves Policy Proceeds on Deposit (Individual)	KRS 136.320 KRS 132.216	14 cents (per \$100 of assessment). 0.1 cent (per \$100 of assessment). 25 cents (per \$100 of assessment).	Also subject to county and city rates. State rate only. State rate only.
Livestock and Poultry	KRS 132.020(1)	0.1 cent (per \$100 of assessment).	State rate only.
Local Government Franchise Taxes on Bank Deposits	KRS 136.575	No state rate. Tax due the following January 31. Based on June 30 deposits.	Tax is imposed on financial institutions measured by deposits in the institutions located within the jurisdiction of the county, city or urban county government at a rate not to exceed twenty-five thousandths of one percent (0.025%) of the deposits if imposed by counties and cities and at a rate not to exceed fifty thousandths of one percent (0.050%) of the deposits imposed by urban county governments.
Manufacturing Machinery	KRS 132.020(1), 132.200(4)	15 cents (per \$100 of assessment).	State rate only.

TAXES ADMINISTERED BY THE DEPARTMENT OF REVENUE (In Effect as of June 30, 2004)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
Margin Accounts (See Brokers' Accounts Receivable)	KRS 132.060; 132.070– KRS 132.090	25 cents (per \$100 of assessment).	State rate only.
Mobile Homes (Real Property)	KRS 132.751	Subject to annual adjustment. Taxed at real estate rate.	Subject to full local rates.
Motor Vehicles	KRS 132.487	45 cents (per \$100 of assessment).	Full local rates. Collected upon registration.
Historic Motor Vehicles	KRS 132.020	25 cents (per \$100 of assessment)	State rate only.
Pollution Control Facilities	KRS 132.020(1), 132.200(9)	15 cents (per \$100 of assessment).	State rate only.
Public Warehouses Goods held for sale except goods in transit Goods in transit to an out-of- state destination within six months	KRS 132.020(10) KRS 132.097 KRS 132.099	5 cents (per \$100 of assessment). Exempt.	Full local rates. Special taxing districts only.
Radio, Television and Telephonic Equipment	KRS 132.020(1), 132.200(5)	15 cents (per \$100 of assessment).	State rate only.
Railroads (Intrastate)	KRS 132.020(11); 136.115- 136.118	10 cents (per \$100 of assessment both real and tangible).	Multiplier applied to local rates. Multiplier subject to annual adjustment.
Raw Materials and Products in Course of Manufacture	KRS 132.020(10), 132.200(4)	5 cents (per \$100 of assessment).	State rate only.
Real Estate not Elsewhere Specified	KRS 132.020(1)	Adjusted annually (by July 1) per KRS 132.020(8). The state real estate rate was 14.1 cents for 2000, 13.6 cents for 2001, 13.5 cents for 2002, 13.3 cents for 2003, and 13.1 cents (per \$100 assessment) for 2004.	Full local rates.
Recreational Vehicles	KRS 132.485(1), 132.730, 132.751	Classification depends on permanency of location. 45 cents (per \$100 of assessment).	Subject to full local rates.
Recycling Machinery	KRS 132.020(1), 132.200(16)	45 cents (per \$100 of assessment).	State rate only.
Retirement Plan or Profit- Sharing Plan Tax	KRS 132.043	0.1 cent (per \$100 of assessment).	State rate only. Taxable to individual participant.
Savings and Loan Associations (Domestic) (Foreign included effective January 1, 1990)	KRS 136.290 KRS 136.300(1), KRS 136.310(1)	10 cents (per \$100 of assessment).	State rate only.

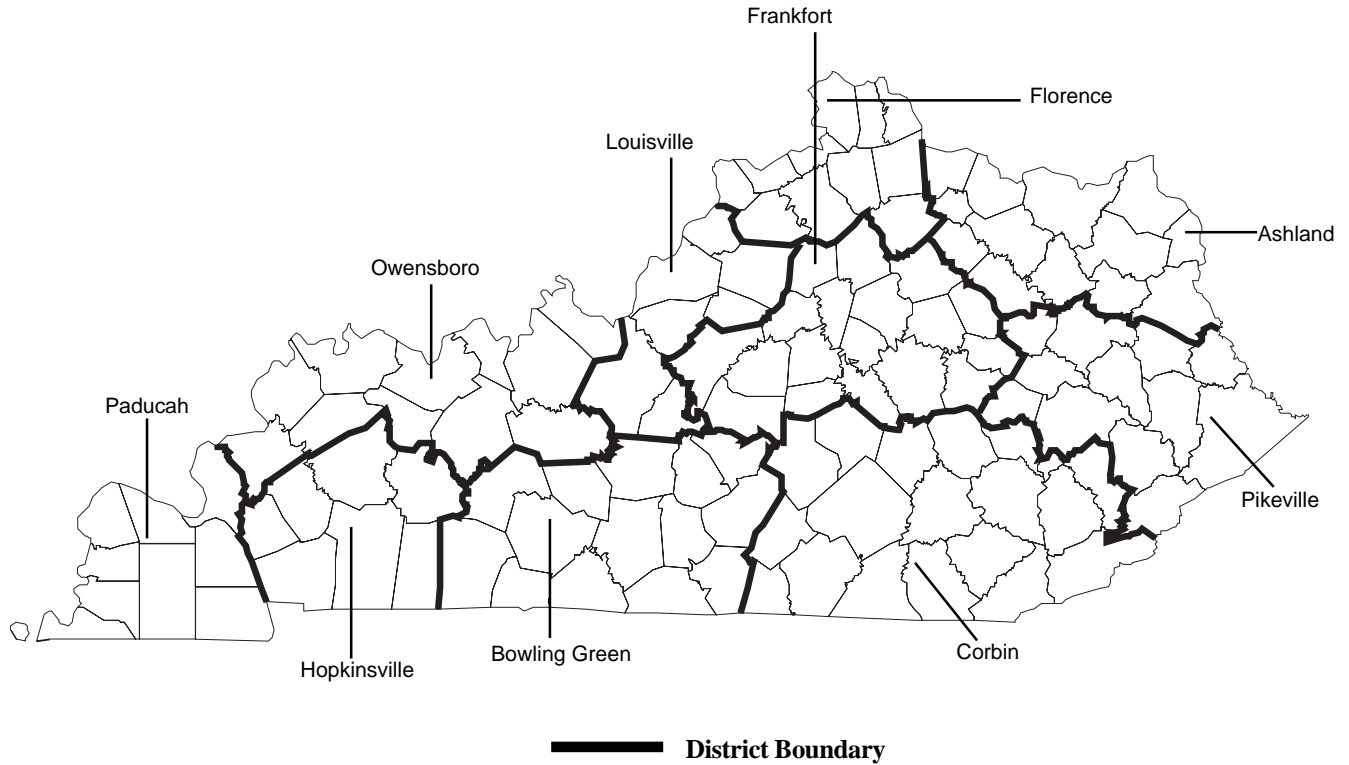
TAXES ADMINISTERED BY THE DEPARTMENT OF REVENUE (In Effect as of June 30, 2004)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION																
Tangible Property not Elsewhere Specified	KRS 132.020(1)	45 cents (per \$100 of assessment).	Full local rates.																
Trucks, Tractors, Trailers, Semi-Trailers and Buses (Interstate)	KRS 136.1873	Subject to annual adjustment.	Local tax collected and distributed by the Revenue Cabinet effective January 1, 1993.																
Unmined Coal, Oil and Gas Reserves, and Other Mineral or Energy Resources Held Separately from Surface Real Property	KRS 132.820	Adjusted annually (by July 1) per KRS 132.020(8). The state real estate rate was 14.1 cents for 2000, 13.6 cents for 2001, 13.5 cents for 2002, 13.3 cents for 2003, and 13.1 cents (per \$100 assessment) for 2004.	Full local rates.																
Watercraft Commercial Individual Federally Documented	KRS 136.181 KRS 132.020(1), 132.488 KRS 132.020(13) KRS 132.200(20)	45 cents (per \$100 of assessment). 45 cents (per \$100 of assessment). 1.5 cents (per \$100 of assessment).	Full local rates. Full local rates. Local option.																
Public Service Commission	Assessment	KRS 278.130 et seq. 1.885 mills (subject to change annually up to 2 mills) Maximum assessment 2.0 mills	Minimum assessment \$50 Assessment imposed annually on utility companies under the jurisdiction of the Public Service Commission based on proportionate share of gross intrastate revenues by each company.																
Public Service Company Property Taxes	KRS 136.115 et seq., 136;180	Property of public service corporations taxed at the same rate as property owned by any individual or corporation (see rates under Property Taxes).	Property of public service corporations taxed at the same rate as property owned by any individual or corporation (see rates under Property Taxes).																
Racing Taxes: (1) License Tax	(1) KRS 137.170 et seq.	(1) Per day of races. <table style="margin-left: auto; margin-right: auto;"> <thead> <tr> <th style="text-align: center;">Average Daily Mutuel Handle (for preceding year)</th> <th style="text-align: center;">Tax Rate Per Day</th> </tr> </thead> <tbody> <tr> <td style="text-align: center;">\$ 0 — \$ 25,000</td> <td style="text-align: center;">\$ 0</td> </tr> <tr> <td style="text-align: center;">25,001 — 250,000</td> <td style="text-align: center;">175</td> </tr> <tr> <td style="text-align: center;">250,001 — 450,000</td> <td style="text-align: center;">500</td> </tr> <tr> <td style="text-align: center;">450,001 — 700,000</td> <td style="text-align: center;">1,000</td> </tr> <tr> <td style="text-align: center;">700,001 — 800,000</td> <td style="text-align: center;">1,500</td> </tr> <tr> <td style="text-align: center;">800,001 — 900,000</td> <td style="text-align: center;">2,000</td> </tr> <tr> <td style="text-align: center;">900,001 and above</td> <td style="text-align: center;">2,500</td> </tr> </tbody> </table>	Average Daily Mutuel Handle (for preceding year)	Tax Rate Per Day	\$ 0 — \$ 25,000	\$ 0	25,001 — 250,000	175	250,001 — 450,000	500	450,001 — 700,000	1,000	700,001 — 800,000	1,500	800,001 — 900,000	2,000	900,001 and above	2,500	(1) License tax imposed upon the operation of a track at which horse races are run under the jurisdiction of the Kentucky Racing Commission. Reported and paid within 30 days of end of each race meeting. An annual recapitulation report is due on or before December 31 each year for the race year ended November 30.
Average Daily Mutuel Handle (for preceding year)	Tax Rate Per Day																		
\$ 0 — \$ 25,000	\$ 0																		
25,001 — 250,000	175																		
250,001 — 450,000	500																		
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700,001 — 800,000	1,500																		
800,001 — 900,000	2,000																		
900,001 and above	2,500																		
(2) Admission Tax	(2) KRS 138.480 et seq., 139.100(2)(c)	(2) Tracks under jurisdiction of the Kentucky Racing Commission 15 cents/person	(2) Excise tax on each paid admission to race track. There are statutory exemptions. Reported and paid within 30 days of end of each race meeting. Race track admission tax is in lieu of sales tax.																

TAXES ADMINISTERED BY THE DEPARTMENT OF REVENUE (In Effect as of June 30, 2004)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
<p>Racing Taxes: (continued)</p> <p>(3) Pari-Mutuel Tax</p>	<p>(3) KRS 138.510 et seq.</p>	<p>(3) 3.5 percent of total wagered at all thoroughbred tracks under Kentucky Racing Commission jurisdiction with average daily handle of \$1.2 million or more; 1.5 percent if average daily handle is less than \$1.2 million.</p> <p>3.75 percent of total wagered at all standardbred tracks under Kentucky Racing Commission jurisdiction with average daily handle of \$1.2 million or more; 1.75 percent if average daily handle is less than \$1.2 million.</p> <p>3 percent of telephone account wagering and the total wagered at "receiving" tracks.</p>	<p>(3) Excise tax is imposed on every person, corporation or association which operates a horse race track at which betting is conducted.</p> <p>Excise tax is also imposed on receiving tracks participating in intertrack wagering on simulcast races.</p> <p>Average daily handle is computed from the amount wagered at the host track, excluding money wagered at receiving tracks and all telephone account wagering.</p> <p>A portion of the pari-mutuel tax is allocated to the following:</p> <ul style="list-style-type: none"> • Equine Drug Research • Equine Industry Program • Higher Education Equine Trust and Revolving Fund • Thoroughbred Development Fund • Standardbred, Quarterhorse, Appaloosa and Arabian Development Fund <p>Reported and paid weekly.</p>
<p>Rural Cooperative Annual Tax</p>	<p>KRS 279.200, 279.530</p>	<p>\$10.</p>	<p>Annual payment by corporations (RECCs and RTCCs) formed under KRS Chapter 279 in lieu of certain taxes.</p>
<p>Sales and Use Taxes</p>	<p>KRS 139.010 et seq.</p>	<p>Sales tax 6 percent</p> <p>Use tax 6 percent</p>	<p>Sales tax is imposed on the retailer for the privilege of making retail sales of tangible personal property or taxable services within Kentucky.</p> <p>Use tax is imposed on the use, storage or other consumption in the state of tangible personal property purchased for use, storage or other consumption in this state. (KRS 139.310)</p> <p>Use tax is imposed on machinery tools and other equipment brought into this state for construction, building or repair projects. (KRS 139.320)</p> <p>There are statutory exemptions.</p> <p>Effective for periods after July 1, 2003 and June 30, 2004, the maximum amount of vendor's compensation per return is \$1,500. Effective July 1, 2004, the cap of \$1,500 on vendor's compensation expired and there is no limit.</p>
<p>Waste Tire Fee</p>	<p>KRS 224.50-868</p>	<p>\$1 per tire sold at retail.</p>	<p>Applies to the retail sale of new motor vehicle tires sold in Kentucky. Does not apply to new cars brought into the state for sale or use. Sales of recapped tires are exempt from the fee.</p>
<p>Withholding (Individual Income Tax)</p>	<p>KRS 141.010 et seq.</p>	<p>Deduction from salaries or wages based upon formula or tax tables.</p>	<p>Employers are required to withhold individual income tax from payment of wages or salaries each pay period. Withholding tables and formulas are provided for common pay periods.</p>
<p>(Pass through entities)</p>	<p>KRS 141.206(3)(a)</p>	<p>6% of total net distributive share income</p>	<p>(Pass through entities)</p>

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Taxpayer Assistance Branch
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