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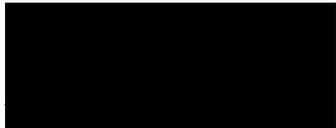
JONATHAN MILLER
Secretary

THOMAS B. MILLER
Commissioner

In the matter of:



Contact:



FINAL RULING NO. 2010-67
October 12, 2010

Assessment of License Tax
Tax Years 1997 through 2001

FINAL RULING

The Kentucky Department of Revenue has issued Corporation license tax assessments against [REDACTED] Corporation ("[REDACTED]") for the fiscal years ending December 31, 1997 through December 31, 2001 totaling \$[REDACTED] plus applicable interest and penalties. The table below provides a breakdown of the amount of tax due, as well as accrued interest, fees and penalties as of the date of this final ruling. Interest, determined in accordance with KRS 131.183, will continue to accrue daily on the unpaid balance. The penalties are assessed pursuant to KRS 131.180.

Tax Year	Tax Due	Interest	Penalties	Total
1997	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
1998	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
1999	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
2000	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
2001	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Totals	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

The above-referenced assessments were based on an office audit examination conducted by auditors from the Department of Revenue. The assessments included adjustments to ██████████'s capital employed license tax calculation and are based on information obtained from the corporate records and the Kentucky Corporation Income and License Tax Returns, Kentucky Form 720, filed for the taxable years ended December 31, 1997 through December 31, 2001. ██████████ is a Kentucky corporation based in ██████████, Kentucky and is a real estate developer.

At issue is the adjustment to capital involving the moneys borrowed for inventory deduction not allowed by the Department.

KRS 136.070(2)(a) provides:

The term "capital" as used in this section means capital stock, surplus, advances by affiliated companies, intercompany accounts, borrowed moneys or any other accounts representing additional capital used and employed in the business. Accounts properly defined as "capital" in this section shall be reported at the value reflected on financial statements prepared for book purposes as of the last day of the calendar or fiscal year.

The foregoing statute states that borrowed moneys are to be included in capital employed, without any provision for purchases of inventory. In addition, the Kentucky Board of Tax Appeals has ruled in Dana Corporation v. Revenue Cabinet, File No. K01-R38, that the borrowed moneys policy set forth in Revenue Policy 41P520 that allowed the deduction from capital of moneys borrowed to finance inventory was void because it was not authorized by the plain language of KRS 136.070(2)(a). See also KRS 13A.130. The result of this order is that no deduction or exclusion is allowed against capital for moneys borrowed to finance inventory.

██████████ states that it was in the business of developing land and developed condominiums, apartments and a retail building on its land in ██████████ County, Kentucky. In so doing, the taxpayer borrowed money to finance these developments. ██████████ believed that the borrowed moneys that financed the developments were used to improve the land for development and therefore were governed by Revenue Policy 41P530, which states:

Corporations in the business of developing real estate may exclude funds borrowed to improve land for development. Examples: Where borrowed funds are used to install utilities, roadways, sewers and such improvements, these funds are excluded since the improvements are considered similar to inventory. Moneys borrowed to purchase the land are not excludable even though the

subdivision of the land into lots will be considered inventory under the generally accepted accounting principles. The [Department of Revenue] will permit moneys borrowed for improvements to be excluded from capital only when the corporation can show by substantial evidence that the borrowed moneys were used directly for improvements to the land.

██████████ provided the Department with a construction loan agreement by which it received a loan for the purpose of financing the construction of “improvements” consisting of an apartment building containing ██████ units. The Department disagreed with the taxpayer’s interpretation of Revenue Policy 41P530, and stated that improvements to land do not include the buildings themselves as the taxpayer asserts. Land improvements consist of betterments, site preparation and site improvements (other than buildings) that ready land for its intended use. Additionally, land is an inexhaustible asset and does not depreciate over time. The buildings that the taxpayer included as inventory are depreciable assets and are capitalized over their useful lives. Revenue Policy 41P530 does not include buildings in its examples of improvements to land. The Department traditionally limited the monies borrowed for inventory deduction to land improvements reported in fixed assets on the balance sheet shown on Schedule L of the Federal Form 1120. In any event, the reasoning of the KBTA’s Dana ruling equally applies to Revenue Policy 41P530. The corporation license tax statutes do not provide for or allow the kind of exclusion or deduction from capital set forth in Revenue Policy 41P530. This policy is therefore void and cannot be used by ██████████ to obtain the deduction or exclusion from capital it seeks. See KRS 13A.130.

Finally, because the taxpayer did not remit in full the amount of tax determined to be due under the provisions of KRS 136.070 for each period for which tax was assessed, late payment penalties were appropriately applied in accordance with KRS 131.180(2).

After reviewing the available information and the applicable statutes, it is the position of the Kentucky Department of Revenue that the license tax assessments issued against ██████████ Corporation for the taxable periods ending December 31, 1997 through December 31, 2001 are valid liabilities due the Commonwealth of Kentucky.

This letter is the final ruling of the Department of Revenue.

APPEAL

You may appeal this final ruling to the Kentucky Board of Tax Appeals pursuant to the provisions of KRS 131.110, KRS 131.340-131.365, 103 KAR 1:010 and 802 KAR 1:010. If you decide to appeal this final ruling, your petition of appeal must be filed at the principal office of the Kentucky Board of Tax Appeals, 128 Brighton Park Boulevard, Frankfort, Kentucky 40601-3714,

within thirty (30) days from the date of this final ruling. The rules of the Kentucky Board of Tax Appeals, which are set forth in 802 KAR 1:010, require that the petition of appeal must:

1. Be filed in quintuplicate;
2. Contain a brief statement of the law and facts in issue;
3. Contain the petitioner's or appellant's position as to the law and facts; and
4. Include a copy of this final ruling with each copy of the petition of appeal.

The petition of appeal must be in writing and signed by the petitioner or appellant. Filings by facsimile or other electronic means shall not be accepted.

Proceedings before the Kentucky Board of Tax Appeals are conducted in accordance with 103 KAR 1:010, 802 KAR 1:010 and KRS 131.340-131.365 and KRS Chapter 13B. Formal hearings are held by the Board concerning the tax appeals before it, with all testimony and proceedings officially reported. Legal representation of parties to appeals before the Board is governed by the following rules set forth in Section 3 of 802 KAR 1:010:

1. An individual may represent himself in any proceedings before the Board where his individual tax liability is at issue or he may obtain an attorney to represent him in those proceedings;
2. An individual who is not an attorney may not represent any other individual or legal entity in any proceedings before the Board;
3. Any party appealing a final ruling to the Board other than an individual, such as a corporation, limited liability company, partnership, joint venture, estate or other legal entity, shall be represented by an attorney in all proceedings before the Board, including the filing of the petition of appeal; and
4. An attorney who is not licensed to practice in Kentucky may practice before the Board only if he complies with Rule 3.030(2) of the Rules of the Kentucky Supreme Court.

You will be notified by the Clerk of the Board of the date and time set for any hearing.

Sincerely,
FINANCE AND ADMINISTRATION CABINET



E. Jeffrey Mosley
Interim Executive Director
Office of Legal Services for Revenue