# Kentucky Tax Alert

A REVENUE PUBLICATION FOR THE TAX PROFESSIONAL

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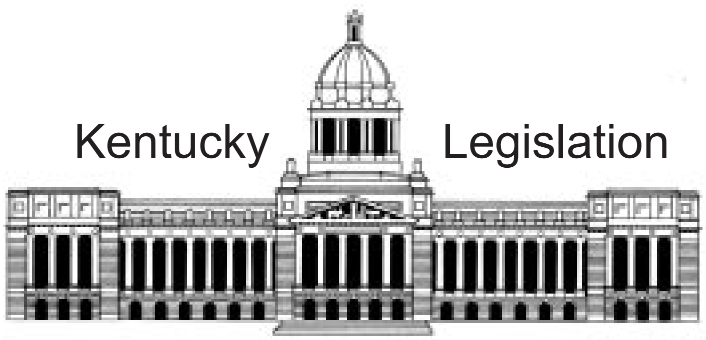
## A Review of Tax Law Changes
Enacted by the 2005 General Assembly




*NOTE: This 2005 legislative summary presents only general information concerning the major tax provisions the General Assembly has enacted and does not represent a complete analysis or specific interpretations of the law changes. The Department of Revenue (DOR) will provide more specific information as it implements these changes. Full text of enacted bills is available on the legislative home page, www.lrc.ky.gov.*

The 2005 Kentucky General Assembly created, amended or repealed numerous statutes. A total of 743 bills and 308 resolutions were introduced. In the end, 172 became law, an enactment rate of 23.15 percent. The governor vetoed one bill and 13 items in the budget bill.

Eighteen bills had substantive tax implications, with some affecting more than one tax. This review describes the tax portion of each bill. Effective dates are shown when specifically stated in the legislation. Otherwise, changes are effective June 20, 2005.

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## Administrative

**Department of Revenue Reorganization—**The Revenue Cabinet is abolished and the Department of Revenue (DOR) within the Finance and Administration Cabinet is created. The bill also establishes major divisions within the DOR. ***(SB 49)***

**Electronic Records—**DOR auditors may request taxpayer records in an electronic format when taxpayers already have them in such a format. ***(HB 497)***

**Fraud—**The definition of *fraud* is clarified to mean not only a taxpayer's failure to file required information, but also a taxpayer's intentional filing of false information. ***(HB 497)***

**Utility Gross Receipts License Tax—**The utility gross receipts license tax, which the department begins administering for local school districts in July 2005, is required to be filed and paid electronically.

*(continued on page 2)*

A taxpayer may request a waiver of this requirement. The bill also permits the DOR to share utility gross receipts license tax information with the school districts on a confidential basis. (***HB 497)***

**Refund Claims—**This bill amends various statutes to clarify that a taxpayer must file an individual refund claim setting forth the specific grounds upon which the refund claim is based. Tax refund claims may not be obtained by a class action lawsuit and the filing of a class action lawsuit does not constitute the timely filing of a refund claim for each member of the alleged class. ***(HB 498)***

## Alcoholic Beverages Tax

**Increase—**(Effective June 1, 2005.) Alcohol wholesale tax is increased from 9 percent to 11 percent. ***(HB 272)***

## Corporation Income Tax

**Corporation Income Tax Base Expansion—**(Effective for tax periods beginning on or after Jan. 1, 2005.) The corporation income tax base is expanded to include all limited liability entities (corporations, LLPs, LLCs, including single member LLCs, limited partnerships, and S corporations). General partnerships and sole proprietorships will not be subject to the expanded corporation income tax. Publicly traded partnerships and their limited partnership and limited liability company affiliates will be taxed as general partnerships. There is no pass-through of income, loss or credit to non-individual owners of pass-through entities subject to corporation income tax. Individual partners, members or shareholders of pass-through entities subject to corporation income tax will receive credit for tax paid at the entity level. ***(HB 272)***

**Rate Reduction—**(Effective for tax periods beginning on or after Jan. 1, 2005.) The top corporate rate is reduced and lower brackets expanded. The 4 percent bracket applies to taxable net income up to $50,000 and the 5 percent bracket applies to taxable net income between $50,000 and $100,000. For taxable years beginning on or after Jan. 1, 2005, and prior to Jan. 1, 2007, the top corporate rate will be 7 percent on all taxable net income over $100,000. For tax years beginning on or after Jan. 1, 2007, the top rate will be 6 percent on all taxable net income over $100,000. ***(HB 272)***

**Reference to Internal Revenue Code (IRC)—**(Effective for tax periods beginning on or after Jan. 1, 2005, except where otherwise indicated.) The IRC reference date is updated to Dec. 31, 2004, except that depreciation and Section 179 expenses are calculated based on the IRC in effect on Dec. 31, 2001. By updating the reference date, Kentucky's tax laws conform more closely with federal laws, providing ease of filing for taxpayers and ease of administration for the DOR. (***HB 272)***

**Alternative Minimum—**(Effective for tax periods beginning on or after Jan. 1, 2005.) Taxpayers must pay the greater of the income tax, the alternative minimum tax or $175. Taxpayers may choose between two methods to calculate the alternative minimum: 9.5 cents per $100 of the corporation's gross receipts or 75 cents per $100 of the corporation's Kentucky gross profits. Kentucky gross profits mean Kentucky gross receipts reduced by returns and allowances attributable to Kentucky gross receipts, less Kentucky cost of goods sold. Cost of goods sold includes direct labor and the cost of specialized transportation for gasoline and special fuels. ***(HB 272)***

**Mandatory Nexus Consolidated Returns—**(Effective for tax periods beginning on or after Jan. 1, 2005, except as otherwise noted.) All corporations with nexus in Kentucky that are connected through an ownership interest of 80 percent or more must file a consolidated Kentucky return. This includes the expanded definition of corporation, with limited liability entities included in the affiliated group. ***(HB 272)***

**Intangible Property, Management Fees and Other Related Party Expenses—**Certain deductions relating to transactions with one or more related members of an affiliated group may be disallowed unless:

1. The corporation and the related member are included in the same consolidated Kentucky corporation income tax return for the relevant taxable year;

2. A disclosure is made and evidence provided to establish that the transaction was at arm's length, that the payment made to a related member was subject to income tax in another jurisdiction, and the related member has substantial business activities other than the management or ownership of intangible property; or

3. The DOR and taxpayer agree in writing to an alternative method of apportionment. ***(HB 272)***

***Doing Business*** **Nexus Standard—**(Effective for tax periods beginning on or after Jan. 1, 2005.) The standard in Kentucky changes from a physical presence standard to a *doing business* standard. ***(HB 272)***

**Net Operating Losses (NOL)—**(Effective for tax periods beginning on or after Jan. 1, 2005.) Corporations may no longer carry NOLs back to previous years. ***(HB 272)***

**Multiple Taxing Jurisdictions (Apportionment)—**(Effective for tax periods beginning on or after Jan. 1, 2005.) All limited liability entities subject to corporation income tax that do business within and without Kentucky and general partnerships that do business within and without Kentucky will be required to utilize a three-factor apportionment formula to apportion income to Kentucky. ***(HB 272)***

**Phase II Tobacco Payments—**(Effective for tax periods beginning on or after Jan. 1, 2005.) State funds that may be paid out as an addition to or a replacement of Phase II tobacco payments are exempt from corporation income tax. ***(HB 272)***

**Conversion—**An ordinary corporation may convert to a nonprofit, nonstock corporation under KRS Chapter 273. ***(SB 142)***

## Corporation License Tax

**Repeal—**(Effective for tax periods ending on or after Dec. 31, 2005.) The corporation license tax is repealed. Returns and tax for prior periods remain due. The anticipated increases resulting from the ***Illinois Tool Works*** court decision, 00-CI-623, will not apply for any year. ***(HB 272)***

## Economic Development Incentives and Credits

**New limits on Kentucky Investment Fund Act (KIFA) Credits—**(Effective July 1, 2005.) KIFA tax credits available to any single investment fund are limited to $1.3 million for all investors and all taxable years. Total KIFA tax credits available for all investors in all investment funds shall not exceed $5 million per fiscal year. ***(HB 267)***

**Clean Coal Incentive Credit—**(Effective for tax periods ending on or after Dec. 31, 2006.) A potential credit is available to an electricity generation facility certified as using clean coal equipment and technology and burning coal subject to Kentucky's severance tax. The credit may be taken against corporation income, individual income, corporation license and public service property taxes at the rate of $2 per ton of qualifying coal burned. The credit applies to electricity generation facilities with an investment of more than $150 million that meet Natural Resources and Environmental Protection Cabinet standards. ***(HB 272)***

**Environmental Remediation (Brownfields) Credit—**(Effective for tax periods beginning after Dec. 31, 2004.) Taxpayers who agree to clean up or develop an existing abandoned brownfield area may qualify for a credit against corporation or individual income taxes in a maximum amount of $150,000. ***(HB 272)***

**Environmental Stewardship Credit—**(Effective for tax years ending on or after Jan. 31, 2007.) A credit is available against the corporation and individual income taxes for a corporation or individual that undertakes an environmental stewardship project with a minimum investment of at least $5 million. The Cabinet for Economic Development must approve these projects. The taxpayer must meet certain wage requirements in order to qualify. The credit will cover 100 percent of eligible skills upgrade training costs and up to 25 percent of eligible equipment costs. The project must produce an environmental stewardship product, which is defined to mean a new manufactured product or substantially improved existing manufactured product that has a lesser or reduced adverse effect on human health and the environment. It may also be used for improvement to human health and the environment when compared with existing products or competing products that serve the same purpose. The maximum amount of credit claimed for any single fiscal year may not exceed 25 percent of the total authorized inducement. ***(HB 272)***

**Biodiesel Credit—**(Effective for tax periods beginning on or after Jan. 1, 2005.) Credits may be taken against corporation or individual income taxes for producing or blending biodiesel fuels of up to $1 per gallon produced or blended, limited to a maximum statewide credit of $1.5 million. The credit may not be carried forward. ***(HB 272)***

**Recycling Tax Credits—**(Effective for tax periods beginning after Dec. 31, 2004.) Corporation and individual income tax recycling credits available are expanded for major recyclers who make a significant investment in plant and equipment and who meet certain employment standards. Credits are allowed for up to 50 percent of the cost of new and expanded recycling equipment, limited each taxable year to 50 percent of the total tax liability for the year the credit is claimed over the tax liability for the most recent taxable year ending prior to Jan. 1, 2005 or $2.5 million, whichever is less. This bill also provides for the recapture of the credit if the equipment is no longer used in a qualifying manner or is sold or disposed of within five years from the date it is purchased, based upon the useful life of the equipment and year of disposition. An exception to the recapture exists in the case of transfers due to death or change in business ownership or organization as long as the equipment remains qualifying equipment. ***(HB 272)***

**Historic Preservation Credit—**(Effective for tax periods ending on or after Dec. 31, 2005.) This bill allows a credit against corporation or individual income taxes for a portion of the cost of restoring a qualified residential and commercial structure listed on the National Registry of Historic Places. The credit is equal to 30 percent of the rehabilitation expenses, in the case of owner-occupied residential property, and 20 percent of the rehabilitation expenses, in the case of all other property. The total credit available is capped at $3 million annually, with each individual owner-occupied property receiving no more than $60,000.

## Enterprise Initiatives

**Enterprise Initiative Act—**(Effective Jan. 1, 2006.) A new statewide tax incentive program replaces the Enterprise Zone program. It extends to eligible companies the opportunity to receive refunds of sales and use tax paid on the purchase of building materials and research and development materials. The bill limits eligible expenditures to tourist attractions, services, technology, manufacturing and company headquarters in any industry. The plan gives preference to companies in existing enterprise zones; the minimum investment is $100,000 for companies within enterprise zone boundaries; $500,000 elsewhere. It also creates a statewide cap in each year of $20 million for building materials and $5 million for research and development on all approved projects. ***(HB 272)***

## Health Care Provider Tax

**Nursing Homes—**(Retroactive to July 1, 2004.) All state-operated veterans' nursing homes are excluded or exempted from paying health care provider tax. ***(HB 439)***

**Classifications—**(Effective July 1, 2005.) Three new classifications to health care provider tax base are created: regional community mental health and retardation services (taxed at 4 percent of gross revenues received), psychiatric residential treatment facility services and Medicaid managed care services (taxed at 5.5 percent of gross revenues received). ***(HB 461)***

## Individual Income Tax

**Reference to IRC—**(Effective for tax periods beginning on or after Jan. 1, 2005, except where otherwise indicated.) This bill updates the IRC reference date to Dec. 31, 2004, with three exceptions, as the basis for Kentucky income taxes. The exceptions are: (1) for property placed in service after Sept. 10, 2001, only the depreciation and expense deductions allowed under Sections 168 and 179 of the IRC are in effect on Dec. 31, 2001, exclusive of any amendments made subsequent to that date, shall be allowed; (2) the provisions of the Military Family Tax Relief Act of 2003, Pub. L. No. 108-121, are effective on the dates specified in that act; and (3) Kentucky will not allow the deduction for sales and use taxes in lieu of state income taxes.

By updating the reference date, Kentucky's tax laws conform more closely with federal laws, providing ease of filing for taxpayers and administration for the DOR. ***(HB 272)***

**Family Size Tax Credit—**(Effective for tax periods beginning on or after Jan. 1, 2005.) Low-income taxpayers will have increased relief. The current low-income tax credit is repealed for taxable years beginning on or after Jan. 1, 2005. The new Family Size Tax Credit is based on modified gross income (MGI) and size of the family household up to four members. Single and married taxpayers whose MGI is at or below federal poverty level for the family size will receive 100 percent tax credit. For 2005, MGI levels that qualify for the 100 percent tax credit are as follows:

| Size of Family Unit | Amount |
|---|---|
| 1 | $ 9,570 |
| 2 | $12,830 |
| 3 | $16,090 |
| 4 | $19,350 |

The Family Size Tax Credit provides benefit to individuals and families at incomes up to 133 percent of the federal poverty level, through a phase-down of the credit. ***(HB 272)***

**Rate Reduction—**(For taxable years beginning after Dec. 31, 2004.) The tax rate for taxable income between $8,000 and $75,000 drops to 5.8 percent with taxable income over $75,000 continuing to be taxed at 6 percent. ***(HB 272)***

**Net Operating Losses (NOL)—**(Effective for tax periods beginning on or after Jan. 1, 2005.) Individuals may no longer carry NOLs back to previous years. ***(HB 272)***

**Phase II Tobacco Payments—**(Effective for tax periods beginning on or after Jan. 1, 2005.) State funds that may be paid out as an addition to or a replacement of Phase II tobacco payments are exempt from individual income tax.

**Pensions—**(Effective Jan. 1, 2005.) The pension exclusion is capped at $41,110, the 2005 amount, and KRS 141.105, which provided for the cost of living adjustment, is repealed. ***(HB 272)***

**Education Tuition Tax Credit—**(Effective for tax periods beginning on or after Dec. 31, 2004.) A credit equal to 25 percent of the amount of the federal Hope Scholarship and the lifetime learning credit is available. The credit applies only to undergraduate studies, phases out for higher incomes and applies to most higher education opportunities within Kentucky. ***(HB 272)***

**Health Savings Accounts—**(Effective for tax periods beginning on or after Jan. 1, 2005.) As a part of the IRC update, Kentucky allows the same tax advantages currently available at the federal level for health savings accounts. Benefits include permitting pretax treatment of contributions to health savings accounts and more potential uses of funds than are allowed with flexible spending accounts. ***(HB 272)***

**Refund Designation—**Taxpayers may now contribute all or a portion of their individual refund to the Breast Cancer Research and Education Trust Fund. The fund replaces the Bluegrass State Games and U. S. Olympic Committee Fund on the Kentucky individual income tax returns. ***(HB 7 )***

## Motor Fuels Tax

**Refunds—**A motor fuels refund may only be requested on fuel purchased after the effective date of the refund permit. ***(HB 494)***

**Underground Storage Tank Fees—**The underground storage tank fee exclusion extends to include all the special fuels for which a credit is provided for by KRS 138.358. ***(HB 494)***

**Bulk Sales—**The motor fuels exemption for sales to the federal government is clarified as applying only to bulk sales and not retail sales. ***(HB 494)***

**Payments—**Motor fuels dealers in good financial standing may either pay by a dealer's check or electronic funds transfer payments. ***(HB 494)***

**Financial Instruments—**Substitutes the words *bond(s)* for *financial instrument(s)* in HB 662, 2002 Session. ***(HB 494)***

**Average Wholesale Price of Gas—**For purposes of the motor fuels tax calculation, the *average wholesale price* is deemed to not be less than one dollar and twenty-two cents ($1.22) per gallon; amended from one dollar and eleven cents ($1.11) per gallon. ***(HB 267)***

## Motor Vehicle Usage Tax

**Collection of Motor Vehicle Usage Tax at Titling—**(Effective July 1, 2005.) Collection of motor vehicle usage tax is required when an owner titles, rather than registers, a vehicle. Allows an owner to submit an affidavit of nonhighway use to prevent payment of motor vehicle usage tax on vehicles that will not be operated on Kentucky highways. Requires collection of sales and use tax on vehicles not used on the highway. Provides credit against motor vehicle usage tax for Kentucky sales and use tax paid when an affidavit is submitted. ***(HB 267)***

**Charter Buses—**(Effective Aug. 1, 2005.) Charter buses are exempt from the motor vehicle usage tax. ***(HB 267)***

## Pari-Mutuel Tax

**International Horse Racing Events—**(Effective Jan. 1, 2006.) An excise tax will not be imposed on pari-mutuel wagering on live racing occurring on any one day that a Kentucky track hosts an international horse racing event that distributes in excess of $10 million in purses. This tax exemption remains in effect for any such succeeding event if the event returns within three years of the previously held event. ***(HB 350; HB 497) (Effective Jan. 1, 2006.)***

## Property Tax

**Property Owned by Another State—**(Effective July 1, 2005.) All real and personal property owned by another state and used exclusively for public purposes is exempt from taxation if that state comparably exempts the commonwealth's property. ***(HB 267)***

**Local School Districts—**(Effective July 1, 2005.) Local school districts that are deemed *hold harmless* pursuant to Fiscal Year 2005-2006 Support Education Excellence in Kentucky (SEEK) tentative calculation shall not be required to levy a property tax rate lower in Fiscal Year 2005-2006 than the previous year's rate. ***(HB 267)***

**Intangible Property Tax Repealed—**(Effective Jan. 1, 2006.) Most intangible property taxes are repealed, other than some of the intangible taxes paid by financial institutions and other businesses. ***(HB 272)***

**State Real Property Tax Rate—**(Effective for tax years beginning on or after Jan. 1, 2005.) Revenue and assessment growth resulting from new property is excluded from the 4 percent growth limit established by HB 44. (***HB 272)***

**School Funding—**(Effective for assessments on or after Jan. 1, 2006.) A district board of education may levy a general tax rate that produces revenue from real property, exclusive of revenue from new property, that is 4 percent over the amount of revenue produced by the compensating rate as defined in KRS 132.010. ***(HB 272)***

**Biotechnology Products—**(Effective Jan. 1, 2002.) Biotechnology products are exempted from assessments for local property taxes and provides a definition of biotechnology products. ***(HB 308)***

**Barge Lines—**(Effective Jan. 1, 2001 to Jan. 1, 2006.) This bill simplifies the ad valorem reporting and payment requirements of affected commercial watercraft companies. ***(HB 350)***

**School Tax Recall—**(Applies to orders, ordinances, resolutions or motions passed after July 15, 2005.) A school tax recall petition in a district in a consolidated local government must include 5 percent of registered and qualified voters voting in the last presidential election. Each sheet must include names of voters from one precinct and an invalid signature shall not disqualify the entire page but result in striking the invalid signature only. ***(SB 13)***

**Airport Authorities—**KRS 382.135 now exempts deeds conveying real property to airport authorities from certain filing requirements. ***(SB 111)***

**Environmental Remediation (Brownfields) Incentive—**(Applies to tax years beginning on or after Jan. 1, 2005.) This bill reduces the real property tax rate to .015 cents per $100 of value for approved properties for three years. ***(HB 272)***

## Sales and Use Tax

**Donated Goods—**(Effective Aug. 1, 2005.) A sales tax refund equal to 25 percent (up to $1 million) of the tax collected on sales of donated goods by resident nonprofit educational, charitable or religious institutions is available, if the entity uses the refund exclusively as reimbursement for capital construction costs of additional retail locations in this state. ***(HB 267)***

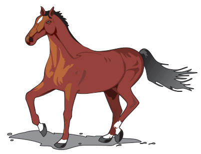
**Repair and Replacement Parts for Charter Buses—**(Effective Aug. 1, 2005.) Repair and replacement parts for directly operating and maintaining a charter bus certified by the Transportation Cabinet are exempt. ***(HB 267)***

**Vendor Compensation—**(For tax periods after June 30, 2005.) The compensation a taxpayer may receive for collecting and remitting sales and use tax is limited to $1,500 per month. ***(HB 267)***

**Commercial Printers or Mailers—**(Effective July 1, 2005.) Commercial printers or mailers engaged in business in this state are not required to collect use tax on sales of printing or direct mail advertising materials that are both printed out of state and delivered out of state to the postal service for mass mailing to third-party Kentucky residents who do not purchase the advertising materials. ***(HB 267)***

**Natural Gas—**(Effective June 1, 2005.) The sales and use tax is levied upon distributing, transmitting or transporting natural gas for storage, use or other consumption in this state, excluding natural gas classified for residential use or to a seller or reseller of natural gas. Charges for related distribution, transmission and transportation for energy that is billed to the user will be included in the cost of production when calculating the 3 percent cost of production for energy direct pay. ***(HB 267)***

**Water Withdrawal Fees—**(Effective July 1, 2005.) The DOR may not subject water withdrawal fees imposed by the Kentucky River Authority to state and local taxes. ***(HB 267)***



**Breeder Incentives—**(Effective June 1, 2005.) Sales tax receipts from stud fees for breeding of horses in this state are earmarked for use in creating breeder incentives. The sales tax will be deposited into special funds for future disbursement by the Kentucky Horse Racing Authority. ***(HB 272)***

**Nexus—**(Effective Aug. 1, 2005.) The sales tax nexus standard will broaden to include remote sellers that use in-state affiliates to facilitate remote sales. This change specifically addresses remote sellers (mail-order and Internet) that allow returns to be made to an affiliated store or location within Kentucky. ***(HB 272)***

**Study—**(Findings to be reported Dec. 1, 2006.) Legislative Research Commission will study the effectiveness of sales tax exemptions. ***(HB 272)***

**Streamlined Sales Tax Agreement—**(Effective July 1, 2005.) Various sections of KRS Chapter 139 are amended to conform to the Streamlined Sales and Use Tax Agreement. The bill also amends KRS 139.472 to exempt mobility enhancing equipment from sales and use tax. ***(HB 495)***

**County Fair Admissions—**The first $50,000 in county fair admissions are exempt from sales and use tax. ***(HB 497)***

**Telephones/Pay Phones (See Telecommunications Services)—**(Effective Jan. 1, 2006.) Switch access and pay phone receipts are no longer subject to sales tax. ***(HB 272)***

## Telecommunications Services

**Excise Tax—**(Effective Jan. 1, 2006.) An excise tax of 3 percent is imposed on multichannel video and audio programming services. Telephone services remain subject to the sales and use tax at a rate of 6 percent. Local governments will receive a guaranteed, fixed amount to replace the franchise fees and unit valuation property taxes that they will no longer receive. ***(HB 272)***

**Gross Revenues Tax—**(Effective Jan. 1, 2006.) An internal gross revenues tax is levied against telephone providers at a rate of 1.3 percent of gross revenues and against multichannel video and audio programming providers at a rate of 2.4 percent of gross revenues. ***(HB 272)***

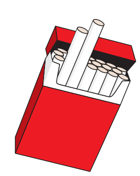
## Tobacco Taxes

**Cigarettes—**(Effective June 1, 2005.) A 26-cent-per-pack surtax is added to the existing excise tax of 3 cents per pack. Vendor compensation remains based on the previous, rather than the increased amount, except that an additional allowance for six months will follow the imposition of the surtax. ***(HB 272)***

***NOTE:*** An additional one cent cigarette tax levy is in ***HB 267***, the budget bill, which will be deposited in a special fund to be matched by the University of Kentucky and the University of Louisville, to be used for cancer research.

**Inventory Floor Tax—**(Encompasses products on the shelf and in facilities on May 31, 2005.) An inventory floor tax is imposed on cigarettes and allows for payment of the tax in three equal installments over a three-month period. ***(HB 272)***

**Other tobacco products—**(Effective Aug. 1, 2005.) A 7.5 percent gross receipts tax is imposed on other tobacco products of any wholesaler derived from wholesale sales of other tobacco products, except snuff, made within the commonwealth and 0.095 cents per unit of snuff. ***(HB 272)***



**Cigarette compensation—**(Effective June 1, 2005 to Nov. 30, 2005.) Additional compensation, for a limited time, equal to 12 cents face value for each $3 of tax evidence purchased at face value on or after June 1, 2005 and before Dec. 1, 2005 is allowed. The additional compensation shall sunset at 12 midnight Nov. 30, 2005. The qualifying compensation is limited to 150 percent of the amount of stamps purchased for the period of Dec. 1, 2004 and ending before May 31, 2005. ***(HB 272)***

**Tobacco Research Trust Fund—**The tobacco research trust fund will receive at least $3.14 million regardless of whether the half-cent cigarette tax levy produces that amount. ***(HB 497)***

## Tourism

**Transient Room Tax—**(Effective June 1, 2005.) A 1 percent state transient room tax on all room charges statewide in addition to the current 6 percent sales tax is created. Funds generated from the tax are deposited in a new fund separate from the General Fund. Language in the bill delineates the use of funds generated by this tax. ***(HB 272)***

**State or National Parks—**Enhanced tourism development credits are available for facilities in state or national parks. ***(HB 497)***

**Boxing and Wrestling—**The gross receipts tax on broadcast, television or motion picture rights for boxing and wrestling matches is repealed. ***(HB 272)***

## Utility Gross Receipts License Tax

**Utility Gross Receipts License Tax—**(Effective July 1, 2005.) New language adds direct satellite broadcast and wireless cable service to the tax base for school districts that impose the tax on cable services on or after July 1, 2005. ***(HB 272)***

## Excise Tax Changes Legislation Affecting Cigarette Retailers (HB 272)

A new section of KRS Chapter 138.130 to 138.205 is created to require that every retailer or cigarette licensee with cigarette inventories shall take a physical inventory of all cigarette packages bearing Kentucky tax stamps, and all unaffixed cigarette tax stamps possessed by them or in their control at 11:59 p.m. on May 31, 2005, and pay a one-time inventory floor tax at the rate of 27 cents per pack of 20 cigarettes (proportionate rate for packs of 25). Vendors may establish the inventory of cigarettes in vending machines by (1) taking an actual physical inventory, (2) estimating the cigarettes in vending machines by reporting one half of the normal fill capacity of the machines as reflected in individual inventory records maintained for vending machines, or (3) using a combination of these two methods.

Form 73A421, Cigarette Inventory Floor Tax, will be mailed in May. The return with payment must be filed with the DOR on or before June 10, 2005. (Taxpayers have the option to remit payment in three equal monthly installments beginning with the June 10 payment.) **This legislation does not affect the sales and use tax return, but applies to any retailer or cigarette licensee with cigarette inventories.**

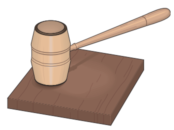
## Legislation Affecting Hotels, Motels and Other Lodging Businesses (HB 272)

A new section of KRS Chapter 142 creates a transient room tax (lodging tax), imposed at the rate of 1 percent of the rent, on every occupancy of any suite, room, rooms or cabins charged by all persons, companies, corporations, groups or organizations doing business as motor courts, motels, hotels, inns, tourist camps or like or similar accommodations businesses. Receipts from this tax will be deposited into the Tourism, Meeting and Convention Marketing Fund administered by the Commerce Cabinet. Retailers operating as motor courts, motels, hotels, inns, tourist camps or similar accommodations businesses will be contacted separately in May with filing requirements and instructions. The transient room tax is in addition to the current 6 percent sales tax and any locally assessed transient room tax and will be reported separately each month on Form 73A850, Transient Room Tax Monthly Return. **For the purposes of state sales tax calculations, the 1 percent transient room tax should be reported as part of taxable receipts just as the locally assessed transient room tax is currently reported.**

If you have any questions regarding the cigarette inventory floor tax or the transient room tax (lodging tax), contact the Excise Tax Section, 200 Fair Oaks Lane, Frankfort, KY 40620, (502) 564-6823.

## Court Case Update

**Property Tax—**In ***City of Somerset v. Bell***, 156 S.W.3d 321 (Ky. App. 2005), taxpayers brought a class action lawsuit asserting that the City of Somerset had improperly levied and collected ad valorem taxes and sought refunds. The Kentucky Court of Appeals held that the taxpayers were entitled to refunds, but could not recover interest on those refunds. The applicable legal rule is that interest is not collectible on taxes due the state, county or any subdivision thereof or on any refund of those taxes unless a statute authorizes it. The statute authorizing the refund of local ad valorem taxes, KRS 134.590, does not authorize the payment of interest.



The court recognized that KRS 134.590 requires the exhaustion of administrative remedies as a prerequisite to a taxpayer's obtaining a refund. In this case, satisfaction of this requirement consisted of filing a refund request with the City of Somerset. The Kentucky Board of Tax Appeals (KBTA) did not have jurisdiction over local ad valorem tax refund claims and consequently the taxpayers in this case did not have to appeal to the KBTA in order to receive refunds in this case.

The Court of Appeals also held that the taxpayers could seek refunds through a class action, based upon a 1996 amendment to KRS 134.590. The General Assembly's enactment of House Bill 498 in 2005 (2005 Ky. Acts., Ch. 112) has effectively overturned this ruling. That legislation clarifies that the 1996 amendments to KRS 134.590 were technical and nonsubstantive and that taxpayers must individually apply for tax refunds instead of obtaining them through a class action.

This decision is now final.

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**ERNIE FLETCHER, Governor**

**ROBBIE RUDOLPH, Secretary**
***Finance and Administration Cabinet***

**MARK TREESH, Commissioner**
***Department of Revenue***

**Editor** ................................. ***Jill Midkiff***
**Production / Design** ............. ***Support Services***
**Publications Coordinator** .... ***Sarah Gilkison***

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