

KENTUCKY SALES TAX FACTS

A REVENUE PUBLICATION FOR THE BUSINESS OWNER

JUNE 2011

2011 LEGISLATIVE UPDATE

HB 429 represents the latest Streamlined Sales Tax (SST) conforming legislation. The legislation amends KRS 139.010 to include definitions for direct mail, other direct mail, and advertising and promotional direct mail. KRS 139.105 and KRS 139.777 were also amended to clarify the sourcing of these direct mail categories, as well as florist wire sales. The sourcing of digital property was also clarified in KRS 139.105.

KRS 139.260 and KRS 139.270 were amended in relation to resale and other types of certificate exemptions. The adjustments to the timing for exemption documentation further preserves the burden of proof relief for vendors. KRS 139.795 was amended to require the department to give all retailers a 30-day notice of any sales and use tax rate change and also to allow for relief from rate-related liability for 30 days from enactment should the department fail to give notice of a rate change. The legislative changes take effect on July 1, 2011.

Sales Tax Issues

Prohibited Advertising

The department has noticed several incidents recently where advertisements have occurred in violation of KRS 139.220. In place since 1960, this law prohibits any retailer from advertising or holding out or stating to the public or customer, directly or indirectly, that the sales tax required to be collected from the customer will be assumed or absorbed by the retailer or the tax will not be added or not refunded if added. In addition, KRS 139.210 requires the retailer to collect the tax from the consumer. The department strives to immediately address those incidents when reported or found. Violators will be contacted to immediately correct or retract the advertisement. Willful violation of this law may result in penalties.

Fire, Theft, Vandalism (FTV) and Damage Waiver Charges

Fire, theft, and vandalism charges, and damage waiver charges, primarily associated with the leases of tangible personal property, are part of gross receipts subject to Kentucky sales tax. Under the rental agreements, a customer paying for one of these FTV waivers is relieved of liability for loss or damage to the equipment rented due to fire, theft or vandalism. KRS 139.010(12)(a) states “Gross receipts” and “sales price” mean “the total amount or consideration, including cash, credit, property, and services, for which tangible personal property, digital property, or services are sold, leased, or rented.” “Gross receipts” includes whatever is paid to the lessor for the rental unless some statutory exemption or exclusion applies, and there are none for such waivers. These charges are part of the lease or rental agreement regardless of whether the waivers are a mandatory or optional part of the contract. Recent litigation, *Green River Rentals, Inc. v. Department of Revenue* 09-CI-01684 confirms the department’s longstanding position that these charges are includable in gross receipts subject to tax.

Bad Debts

Bad debts may only be claimed as a deduction on the sales and use tax return by retailers that report by the accrual method of accounting. In addition, bad debts may only be claimed as a valid sales tax deduction if the uncollected receipts previously reported for sales tax purposes are eligible to be charged off as bad debts for federal income tax purposes. Once the income has been written off as uncollectable in the retailer’s books and records, it can be claimed as a deduction on the sales and use tax return on line 12, code 120, as long as doing so does not result in a negative tax due for that period. If claiming the bad debt would result in a negative tax due return, the taxpayer must amend the returns on which the tax for the items written off as

bad debt was reported or file a sales and use tax refund application (Form 51A209) for the period when the bad debt was written off. When applicable, a copy of the taxpayer's federal income tax return should be submitted with the refund application to aid in consideration of the bad debts claimed. This bad debt provision does not allow for third party lenders to become retailers for purposes of sales tax recovery of bad debts.

Regulatory License Fee on Gross Receipts of Alcohol Sales

If a city of the third or fourth class imposes a regulatory license fee upon the gross receipts of a licensed establishment's sale of alcoholic beverages provided under KRS 243.075, any portion of that fee the retailer passes on to the customer is part of gross receipts subject to the Kentucky sales tax per KRS 139.010(10)(12). This tax treatment is based upon the fact that the local license fee is imposed upon the retailer and not the retailer's customer. Affected retailers should make adjustments accordingly to their sales tax calculations.

Documenting An Exempt Sale

In order for a retailer to take a deduction from gross receipts on their sales and use tax return the business must maintain a record of the appropriate exemption certificate, other required documentation or applicable data elements. The retailer is required to keep these records for no less than four years. Because the burden of proof is on the seller, the seller is required to retain documentation in accordance with KRS 139.270 and 139.280 in order to substantiate why the customer was not charged sales tax. In audit situations and in response to departmental inquiries, the vendor must produce exemption certificates or corresponding data elements to substantiate deductions previously taken. The burden of proof and resulting tax liability shifts to the purchaser on transactions where fully completed certificates or required data elements are timely received by the retailer.

Digital Property

The retail sale of digital property accessed or obtained (transferred electronically) by the Kentucky purchaser

is subject to the 6 percent Kentucky sales and use tax. By definition in KRS 139.010(4)-(9), digital property includes digital audio works, digital books, finished artwork, digital photographs, periodicals, newspapers, magazines, video greeting cards, audio greeting cards, video games, electronic games, and digital code related to this property. Keep in mind that the digital code for digital property may be obtained through either digital or tangible means. Any retail sale of a product included within this statutory definition is subject to tax unless specifically excluded or exempted.

Admissions

Admissions, as defined in section 1 of 103 KAR 28:010 and available at www.revenue.ky.gov/laws, is a right of entrance to a display, program, sporting event, music concert, performance, play, show, movie, exhibit, fair, or other entertainment event or amusement. Section 2 explains that each "general admission" charge shall be subject to tax even if payments are designated as a donation. However, section 3 allows an exemption from sales tax if the primary intent of an event or program is for education rather than entertainment as with workshops, seminars and professional conferences. Also, any fees paying for the privilege of using the facilities, participation in the event or activity, or fees that are separate or additional to the general admission shall not be considered taxable. Gross receipts include total amounts paid to the lessor for the rental unless some statutory exemption or exclusion applies.

A few examples of taxable admissions include admissions to amusement parks, art exhibits, cabarets, dance halls, football stadiums, national park facilities (operated under lease), night clubs, and street fairs. In addition, examples of nontaxable fees include charges for amusement park rides, bowling fees, fishing or picnicking fees, miniature golf fees, and swimming fees.

As with all retail sales, a receipt shall be provided separately stating the tax charged to the customer. If the retailer of admissions obtains permission from the department not to separately display the tax (KRS 139.210(2)), then either a statement must appear on the ticket to the effect that the sales tax is included

in the price or the statement may be posted in a conspicuous place at the ticket window if **all sales are made at the ticket window.**

Sales and Use Tax Reporting Issues

Equine Breeders

KRS 230.800-.804 provides that all receipts collected under KRS 139.531(1)(a) from sales and use tax on the fees paid for breeding a stallion to a mare shall be deposited into a fund administered by the Kentucky Horse Racing Commission. This legislation was enacted in 2005, became effective June 1, 2005, and has been addressed in previous *Sales Tax Facts* articles (4/05, 6/05, 6/07). Entities who receive receipts from equine breeding fees must report the sales tax on their Kentucky sales and use tax return and submit a supplementary sales tax form (Kentucky Sales and Use Tax Equine Breeders Supplementary Schedule, Form 51A132). Taxpayers may download the form at <http://revenue.ky.gov/forms/cursalefrm.htm>, or may input figures on the form and submit electronically. The supplementary schedule may be mailed, faxed or electronically submitted for each period that sales of breeding fees are claimed on the sales tax return. Data on the supplementary schedule helps the department verify the proper amount of sales and use tax for deposit in the Breeders' Incentive Fund.

Electronic Sales Tax Payments

After the completion of an open competitive negotiations process, the Commonwealth of Kentucky has awarded the contract for General Depository Banking Services to J.P. Morgan Chase effective July 1, 2011. The department has attempted to contact all Electronic Funds Transfer (EFT) accounts during the month of June to notify them of this change and to provide updated routing and account numbers to be used. If you require assistance with an EFT payment after July 1, 2011, please respond via email to DORECommerce@ky.gov, or by calling (502) 564-7807 or (502) 564-7808. In addition, for those accounts that remit funds via EFT, please ensure the correct account number and correct reporting periods are used when making your electronic payments. Failure to use the correct number or period leads to additional administrative procedures by the

department and the taxpayer to correct the payment error. If taxpayers continue to make similar input errors on a routine basis, the department may need to issue late payment penalties.

This newsletter is intended to provide practical information to assist persons in fulfilling their sales and use tax obligations to the Commonwealth.

This newsletter is archived on the Department of Revenue website at www.revenue.ky.gov

and future editions may be accessed at the website.

To submit additional questions or suggestions for future topics, please write to:

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