

KRC

ANNUAL

REPORT

1998-99



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Revenue Cabinet

Paul E. Patton
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Commonwealth of Kentucky

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1998-99

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*All information contained in this report is as of
June 30, 1999.*



The Kentucky Revenue Cabinet does not discriminate on the basis of race, color, national origin, sex, religion, age or disability in employment or the provision of services.

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PAUL E. PATTON
GOVERNOR



SARAH J. SCHAAF
SECRETARY

REVENUE CABINET
OFFICE OF THE SECRETARY
FRANKFORT, KENTUCKY 40620

December 1, 1999

The Honorable Paul E. Patton, Governor
Commonwealth of Kentucky
The State Capitol
Frankfort, Kentucky 40601

Dear Governor Patton:

Pursuant to Kentucky Revised Statute 12.110, I am pleased to present the Kentucky Revenue Cabinet's (KRC) Annual Report for Fiscal Year 1998-99.

Contained in this report is an analysis of General Fund and Road Fund receipts, a summary of major KRC accomplishments for the fiscal year and a description of our *EMPOWER Kentucky* initiatives including revenue projections and receipts.

KRC is entering a new era in tax administration by implementing an integrated tax system, the Kentucky Integrated Tax Entity System (KITES). Funding of KITES through your *EMPOWER Kentucky* program is a testament to the dedicated and hardworking staff in KRC. As we modernize our agency for the twenty-first century, our employees will continue to demonstrate their commitment to quality service to the Commonwealth. We thank you for your support and confidence in our abilities.

Sincerely,

A handwritten signature in cursive script that reads "Sarah Jane Schaaf".

Sarah Jane Schaaf, Secretary
Kentucky Revenue Cabinet



AN EQUAL OPPORTUNITY EMPLOYER M/F/D

KRC Mission

The Cabinet's mission, reflected in its philosophy and general strategy, is central to all of its work. All of the Cabinet's actions should reflect its mission and similarly, those actions should be judged by the extent to which they help the Cabinet carry out its mission.

Within this framework, it is the mission of the Kentucky Revenue Cabinet to:

Provide courteous, accurate and efficient services for the benefit of Kentucky and its citizens, and administer the tax laws of the Commonwealth in a fair and impartial manner.

To achieve its mission, the Cabinet will:

- Promote voluntary compliance with tax laws through educational programs and quality taxpayer services;
- Inform the public of taxpayer rights and responsibilities;
- Establish and maintain clear, concise, accurate and timely communication to foster positive and constructive relations and a better understanding of tax laws;
- Collect and process receipts and returns as cost effectively and efficiently as possible;
- Develop and implement new and innovative programs to minimize noncompliance with tax laws;
- Utilize information resources and expertise to serve in an advisory role;
- Acquire new technologies to implement and maintain a state-of-the-art tax administration system;
- Enforce compliance when there is an intent to defraud or evade the taxes due the Commonwealth; and
- Educate, train, develop and retain the qualified staff necessary to achieve its goals and objectives.

KRC Philosophy

Recognizing that the administration of Kentucky's tax laws is a challenging and sometimes controversial responsibility, the Revenue Cabinet complements its mission with a tax administration philosophy.

The Cabinet's philosophy, drawn from its strategy and mission, represents the fundamental beliefs that shape the approach to policy and operations within a new framework. **IT IS A COMMITMENT TO SERVICE.**

- **Commitment to High Standards of Service.** The Cabinet is committed to raising the standards of tax administration by providing professional, courteous, accurate and efficient service to taxpayers of the Commonwealth as they try to voluntarily comply with Kentucky's tax laws.

This commitment to service—the core of the Cabinet's tax administration philosophy—is pervasive and long-term, and will be a daily expression of the Revenue Cabinet's value system. The high standards set for the Cabinet on behalf of Kentucky's taxpayers will guide strategies and assist in establishing goals and objectives.

- **Commitment to Employees and the Services they Provide.** The Cabinet recognizes that its employees are its greatest asset and they should be encouraged and empowered to use their creativity and resourcefulness in fulfilling the Cabinet's mission.

Employees must be dedicated to working not only individually but as a team to fully satisfy the service needs of Kentucky's taxpayers. Only through teamwork, training and education can staff ensure adequate response and efficient delivery of service.

- **Commitment to Flexibility and Effectiveness in Serving Taxpayers.** Flexibility is essential to accommodate today's rapidly changing world. Taxpayers expect greater efficiency and responsiveness from government. Budgetary and efficiency needs as well as expectations from executive, legislative and judicial branches of government demand quicker and more accurate research and data as it impacts the tax structure. In addition, the need to effectively interact with federal, state and local government officials is becoming increasingly important.
- **Commitment to Assisting the Taxpayer.** The Cabinet will improve its efforts to educate and inform taxpayers of their responsibilities to timely file and pay tax obligations. Assistance will be given to facilitate easy and accurate reporting. Constantly striving to modernize and enhance Revenue's tax administration system will enable the Cabinet to utilize more effectively its resources to provide a greater depth and breadth of service.
- **Commitment to Fair and Impartial Administration and Enforcement.** The Cabinet is committed to administering the tax laws of the Commonwealth fairly, equitably and impartially without regard to taxpayers' status, wealth, political affiliation, race, color, creed or disability.

In its pursuit of fair tax administration for all taxpayers—particularly the vast majority of taxpayers who timely report and pay their Kentucky taxes—the Cabinet will identify and actively pursue those who do not voluntarily comply with their tax reporting and payment responsibilities.

Thus, in an effort to earn total and absolute confidence of Kentucky's taxpayers regarding its fair administration of the tax laws, the Cabinet will exhibit honesty and integrity in all dealings with taxpayers and avoid any situation or action which could result in the slightest perception of unfair practices or questionable behavior.

Promoting voluntary compliance, educating taxpayers of their responsibilities and quality service will be the Cabinet's daily commitment to Kentucky and its citizens.

The Cabinet will not lose sight of those it serves!

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Revenue Receipts

(Reprinted from the
Finance and Administration Cabinet's 1998
4th Quarter **Quarterly Economic & Revenue Report**)

As shown in Table 1, combined tax and nontax receipts for the General and Road Funds increased by 3.3 percent over the combined receipts in FY98. Table 2 compares only tax receipts for the two funds which grew by 3.7 percent. Table 3 compares combined nontax receipts which declined by 4.9 percent over the previous year.

Table 1
Total Receipts
(millions of dollars)

	FY99	FY98	Percent Change
General Fund	\$6,198.4	\$6,011.8	3.1
Road Fund	<u>1,056.6</u>	<u>1,011.8</u>	4.4
Combined	\$7,255.0	\$7,023.6	3.3

Table 2
Tax Receipts
(millions of dollars)

	FY99	FY98	Percent Change
General Fund	\$5,917.2	\$5,722.5	3.4
Road Fund	<u>991.6</u>	<u>942.1</u>	5.3
Combined	\$6,908.8	\$6,664.6	3.7

Table 3
Nontax Receipts
(millions of dollars)

	FY99	FY98	Percent Change
General Fund	\$272.3	\$284.4	-4.3
Road Fund	<u>64.3</u>	<u>69.4</u>	-7.2
Total	\$336.6	\$353.8	-4.9

General Fund

With slower growth in the fourth quarter, General Fund receipts for the year increased by a moderate 3.1 percent over those reported in FY98. This was due mostly to the decrease in inheritance tax, corporate income tax, and lottery receipts. Individual income tax experienced slower growth than in previous years. Total receipts of \$6,198.4 million compare to \$6,011.8 million collected in FY98.

The sales tax growth rate increased slightly from the previous year. Receipts of \$2,085.9 million compare to prior year receipts of \$1,981.3 million.

Performance in the individual income tax slowed from the strong growth rate posted in FY98. The growth rate for FY99 was 4.7 percent and compared to 9.7 percent in FY98. Receipts totaled \$2,532.0 million and compare to \$2,418.1 million collected last year. This increase comes despite the continued phase-in of the pension exemption and the increase in the standard deduction.

The corporate income tax declined substantially with a decrease of 6.5 percent for the year. Receipts of \$312.1 million compared to \$333.7 million collected in FY98. FY98 receipts had grown by 14.0 percent from FY97 collections.

Coal severance tax collections decreased by 5.7 percent after a slight increase in FY98. Receipts totaled \$154.5 million and compare to \$163.7 million collected during the prior fiscal year.

Total property taxes experienced a slight increase of 2.1 percent during this fiscal year. Receipts totaled \$370.4 million compared to \$362.8 million collected in FY98.

The growth in lottery receipts slowed from that experienced in previous years. Receipts of \$153.8 million grew by 0.5 percent over the \$153.0 million remitted to the state last fiscal year.

Revenue Receipts

The *other* category finished the year with a decrease of 1.6 percent. Receipts of \$589.7 million compare to \$599.2 million collected in FY98. Accounts with significant losses in this category include the inheritance tax and interest on investments.

Table 4 compares the growth rates in major General Fund categories and the fund as a whole for the entire year and the four individual quarters.

Table 4
General Fund Growth Rates
for the Four Quarters and Full Year, FY99

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY99
Total					
Receipts	1.7%	4.9%	2.9%	2.8%	3.1%
Sales & Use	5.1	5.7	6.3	4.0	5.3
Individual					
Income	3.2	4.4	4.2	6.6	4.7
Corporate					
Income	-17.5	12.6	-60.9	3.4	-6.5
Coal					
Severance	2.5	-2.9	-12.7	-9.1	-5.7
Property	-0.7	4.8	3.9	-7.9	2.1
Lottery	18.9	8.3	8.6	-25.1	0.5
All Other	-9.7	1.0	4.5	-3.3	-1.6

Road Fund

Total Road Fund receipts grew by 4.4 percent during FY99. Total receipts of \$1,056.6 million compare to \$1,011.8 million collected in this fund during FY98.

The motor fuels taxes strong growth rate of 8.0 percent compares to a growth rate of 1.4 percent during FY98. Receipts of \$427.8 million compare to \$396.1 million collected during the previous fiscal year.

Motor vehicle usage tax receipts of \$375.7 million grew by 2.4 percent over the \$366.8 million collected in FY98. This compares to a growth rate of 7.4 percent experienced last year.

The performance of the weight distance tax improved during the year and finished with a growth of 5.2 percent. Growth last year was 5.7 percent. Receipts totaled \$70.2 million and compare to \$66.7 million collected last fiscal year.

The *other* category grew by a slight 0.4 percent after a strong 10.4 percent increase last year. Total receipts in this category were \$182.9 million, which compares to \$182.2 million collected in FY98.

Table 5 displays the growth rates for the Road Fund and its major tax categories for the year as a whole and the four individual quarters.

Table 5
Road Fund Growth Rates
for the Four Quarters and Full Year, FY99

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	FY99
Total					
Receipts	5.2%	11.0%	-2.0%	4.6%	4.4%
Motor Fuels	8.8	21.6	-9.2	16.1	8.0
Motor					
Vehicle					
Usage	3.9	10.4	-3.2	-0.3	2.4
Weight					
Distance	5.4	3.8	6.2	5.6	5.2
All Other	0.5	-5.9	16.6	-6.0	0.4

EMPOWER Kentucky

The *EMPOWER Kentucky* revenue enhancement initiatives have continued and expanded during FY99. Collections during the fiscal year are shown in Table 6. *EMPOWER Kentucky* is a program that funds, among other things, specific procedures within the Revenue Cabinet. These procedures are designed to collect certain revenues that are owed to the commonwealth but are not voluntarily paid.

Table 6
EMPOWER Kentucky Collections During FY99
(millions of dollars)

Type Tax	Collections During FY99
Individual Income	\$16.5
Corporation Income	1.0
Sales and Use Tax	10.7
Property Tax	13.6
Other (See Note)	7.2
Total	\$49.0

Note: Some revenues were not classified during part of FY99. All unclassified receipts are included in the *other* category.

Revenue Receipts

GENERAL FUND

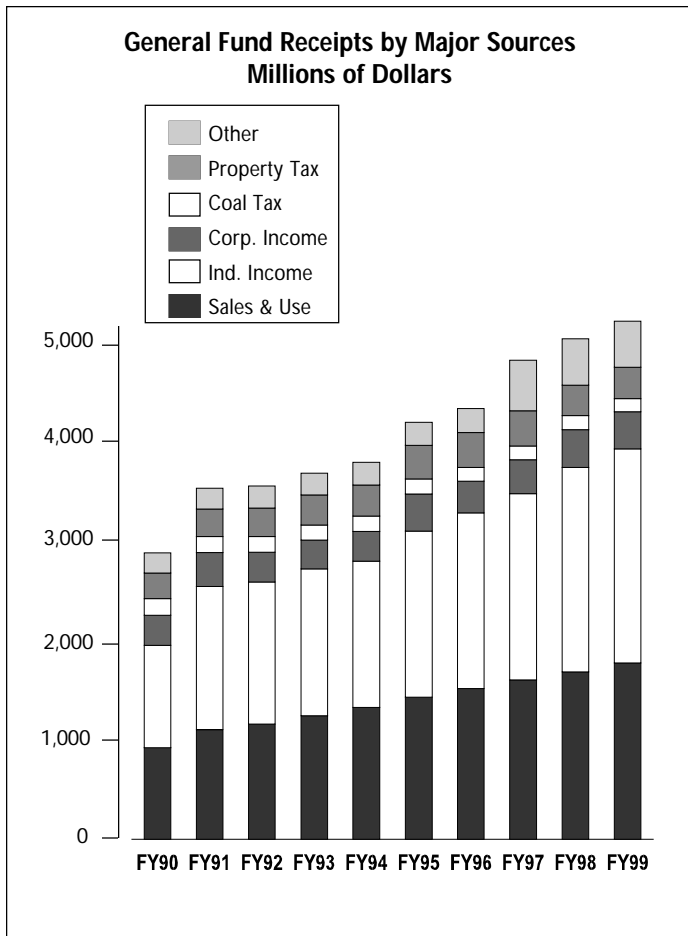
GENERAL FUND TOTAL RECEIPTS		
Fiscal Year	Receipts	Percent Change
1998-99	\$6,198,387,525	3.1
1997-98	6,011,806,561	6.1
1996-97	5,663,553,289	6.1
1995-96	5,336,883,824	3.5
1994-95	5,154,077,980	10.9
1993-94	4,647,078,322	3.0
1992-93	4,511,721,822	3.5
1991-92	4,360,835,365	1.1
1990-91	4,311,675,984 ²	21.1
1989-90	3,560,983,777 ¹	8.2

ALCOHOLIC BEVERAGE TAXES

Malt Beverage		
Fiscal Year	Receipts	Percent Change
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
1993-94	32,553,876	4.4
1992-93	31,172,541	2.5
1991-92	30,404,806	4.8
1990-91	29,002,422	5.9
1989-90	27,376,409	3.4

¹Lottery revenues were first deposited in the General Fund.

²Total corrected by Finance and Administration Cabinet.



Distilled Spirits

Fiscal Year	Receipts	Percent Change
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
1993-94	19,960,515	0.2
1992-93	19,923,344	2.2
1991-92	19,485,739	0.9
1990-91	19,314,634	2.8
1989-90	18,789,245	0.8

Wine

Fiscal Year	Receipts	Percent Change
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
1993-94	4,492,841	0.9
1992-93	4,454,161	4.2
1991-92	4,273,359	4.6
1990-91	4,085,329	0.7
1989-90	4,055,763	1.0

¹Total corrected by Finance and Administration Cabinet.

Revenue Receipts

CIGARETTE TAX¹

Fiscal Year	Receipts	Percent Change
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
1993-94	14,285,746	2.1
1992-93	13,994,590	-0.4
1991-92	14,044,608	-1.6
1990-91	14,278,438	2.7
1989-90	13,897,537	-2.1

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.

CORPORATION LICENSE TAX

Fiscal Year	Receipts	Percent Change
1998-99	\$125,912,523	11.7
1997-98	112,763,161	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
1993-94	82,031,324 ¹	-5.8
1992-93	87,061,523	6.3
1991-92	81,926,247	0.3
1990-91	81,709,060	8.5
1989-90	75,328,093	8.7

¹Total corrected by Finance and Administration Cabinet.

²Corrected for posting error by Finance and Administration Cabinet.

COAL SEVERANCE TAX

Fiscal Year	Receipts	Percent Change
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
1993-94	179,844,327	-0.2
1992-93	180,117,668	-2.7
1991-92	185,102,332	-3.1
1990-91	191,037,171	-2.3
1989-90	195,496,376 ¹	8.2

¹Total corrected by Finance and Administration Cabinet.

INDIVIDUAL INCOME TAX

Fiscal Year	Receipts	Percent Change
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
1993-94	1,729,182,293	-0.2
1992-93	1,733,415,059	3.3
1991-92	1,678,525,589	-0.9
1990-91	1,693,338,659 ¹	39.9
1989-90	1,210,284,972	8.9

¹Kentucky income tax law was amended to conform to the Internal Revenue Code in effect on December 31, 1989, and the deduction for federal income tax was repealed.

CORPORATION INCOME TAX

Fiscal Year	Receipts	Percent Change
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
1993-94	269,067,231	5.6
1992-93	254,775,357	-6.0
1991-92	271,026,952	-15.1
1990-91	319,350,654 ¹	14.3
1989-90	279,482,573	-10.1

¹Each tax rate increased one percentage point effective January 1, 1990.

INHERITANCE AND ESTATE TAX

Fiscal Year	Receipts	Percent Change
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
1993-94	76,135,351	7.3
1992-93	70,965,470	-8.3
1991-92	77,354,648	12.6
1990-91	68,726,903	2.8
1989-90	66,855,011	25.2

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
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
1993-94	38,057,960	11.1
1992-93	34,268,972	1.7
1991-92	33,703,047	15.7
1990-91	29,130,844	1.7
1989-90	28,656,062	-1.8

Insurance Companies Other than Life

Fiscal Year	Receipts	Percent Change
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
1993-94	42,720,970	5.1
1992-93	40,631,761	2.1
1991-92	39,781,751	3.3
1990-91	38,529,132	9.6
1989-90	35,164,266	0.0

LOTTERY RECEIPTS

Fiscal Year	Receipts	Percent Change
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
1993-94	114,000,000	14.0
1992-93	100,000,000	0.0
1991-92	100,000,000	37.0
1990-91	73,000,000	-18.9
1989-90	90,000,000 ¹	0.0

¹The Kentucky Lottery Corporation began sales on April 4, 1989. All receipts were initially deposited into a trust account. During the first quarter of FY90 all funds were transferred to the General Fund.

MINERALS AND NATURAL GAS TAX

Fiscal Year	Receipts	Percent Change
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
1993-94	16,718,727	8.1
1992-93	15,463,902	18.0
1991-92	13,105,878	-16.7
1990-91	15,733,934	12.1
1989-90	14,032,659	2.9

OIL PRODUCTION TAX

Fiscal Year	Receipts	Percent Change
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
1993-94	2,697,560	-38.9
1992-93	4,413,136	-7.2
1991-92	4,756,184	-18.3
1990-91	5,824,523	33.5
1989-90	4,363,731	14.0

PARI-MUTUEL TAX

Fiscal Year	Receipts	Percent Change
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
1993-94	6,134,317	-1.8
1992-93	6,247,368	-8.8
1991-92	6,852,421	6.5
1990-91	6,435,598 ¹	-42.1
1989-90	11,124,213	6.9

¹Tax rate and credit system were restructured, effectively reducing the amount of the pari-mutuel tax.

Revenue Receipts

PROPERTY TAXES—REAL ESTATE

Fiscal Year	Receipts	Percent Change
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
1993-94	132,125,477	4.6
1992-93	126,333,184	3.4
1991-92	122,146,269	5.7
1990-91	115,574,669	2.3
1989-90	112,971,186	2.1

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

PROPERTY TAXES—INTANGIBLE

Fiscal Year	Receipts	Percent Change
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
1993-94	77,393,521	-0.5
1992-93	77,751,342	11.1
1991-92	69,961,863	-2.0
1990-91	71,415,874	12.9
1989-90	63,275,797	10.9

¹Shares of stock were exempted from property tax.

PROPERTY TAXES—TANGIBLE

Fiscal Year	Receipts	Percent Change
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
1993-94	104,501,822	10.8
1992-93	94,346,047	4.5
1991-92	90,281,298	7.3
1990-91	84,110,969	7.5
1989-90	78,212,759	18.9

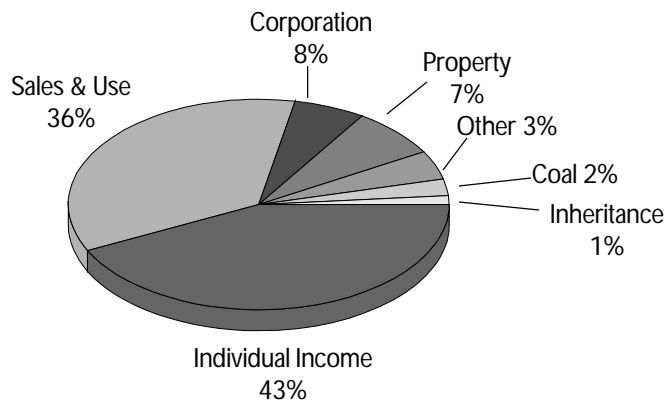
¹Some tangible property tax receipts were erroneously credited to real property receipts accounts.

SALES AND USE TAX

Fiscal Year	Receipts	Percent Change
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
1993-94	1,560,085,519	6.7
1992-93	1,462,251,261	7.2
1991-92	1,363,690,026	5.2
1990-91	1,296,310,445 ¹	19.4
1989-90	1,085,822,176	3.9

¹The tax rate was raised from 5 to 6 percent effective July 1, 1990.

Makeup of FY99 General Fund



Revenue Receipts

ROAD FUND

ROAD FUND TOTAL RECEIPTS ¹		
Fiscal Year	Receipts	Percent Change
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
1993-94	862,826,425	5.2
1992-93	820,411,480	4.9
1991-92	781,808,152	2.1
1990-91	765,598,232 ²	1.5
1989-90	754,484,154	3.5

MOTOR FUELS TAXES

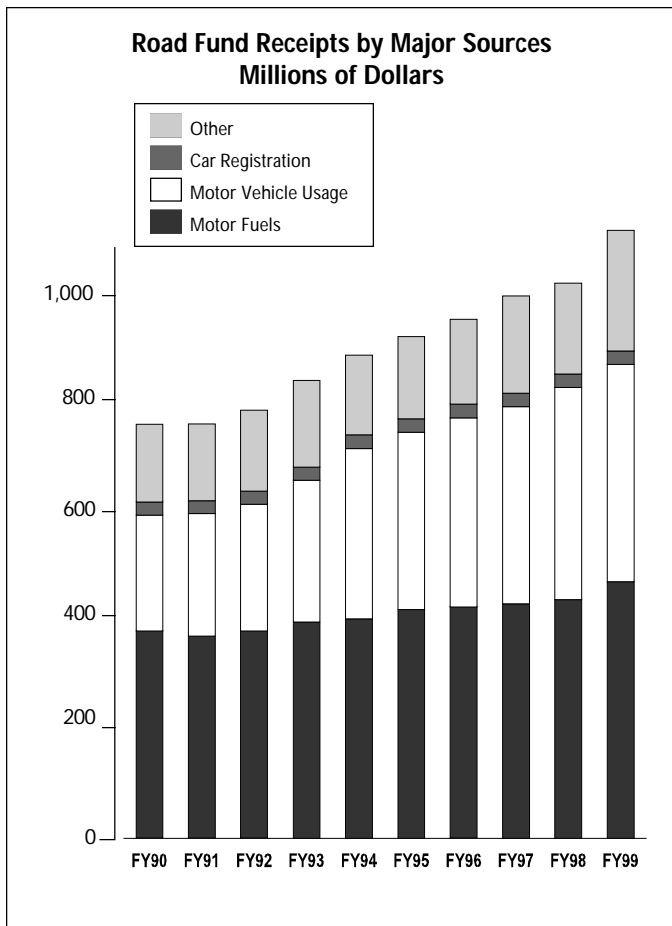
Motor Fuels Normal		
Fiscal Year	Receipts	Percent Change
1998-99	\$427,848,100	8.0
1997-98	396,123,781	1.4
1996-97	390,688,336	3.3
1995-96	378,142,941	1.3
1994-95	373,316,977	4.2
1993-94	358,435,307	1.4
1992-93	353,651,330	4.5
1991-92	338,517,487	3.4
1990-91	327,467,484	-2.7
1989-90	336,436,477	0.1

¹Does not include federal grants.

²Motor vehicle usage tax rate was increased to 6 percent effective July 1, 1990.

Motor Fuels Normal Use and Surtax

Fiscal Year	Receipts	Percent Change
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
1993-94	21,399,126	3.9
1992-93	20,591,812	-1.9
1991-92	21,000,948	-6.0
1990-91	22,331,775	-2.7
1989-90	22,943,630	5.7



MOTOR VEHICLE OPERATOR'S LICENSE

Fiscal Year	Receipts	Percent Change
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
1993-94	5,358,710	6.7
1992-93	5,020,733	-3.8
1991-92	5,221,356	3.6
1990-91	5,038,197	-6.0
1989-90	5,361,189	0.7

Revenue Receipts

MOTOR VEHICLE REGISTRATIONS

Passenger Car Registration		
Fiscal Year	Receipts	Percent Change
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
1993-94	23,473,690	1.7
1992-93	23,083,164	0.8
1991-92	22,893,363	1.6
1990-91	22,528,562	0.1
1989-90	22,504,662	3.5

MOTOR VEHICLE RENTAL USAGE TAX

Fiscal Year	Receipts	Percent Change
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
1993-94	17,055,319	40.7
1992-93	12,124,476	33.2
1991-92	9,103,767	25.3
1990-91	7,264,932 ^{1, 2}	11.5
1989-90	6,517,199	-9.8

¹Percent change corrected.

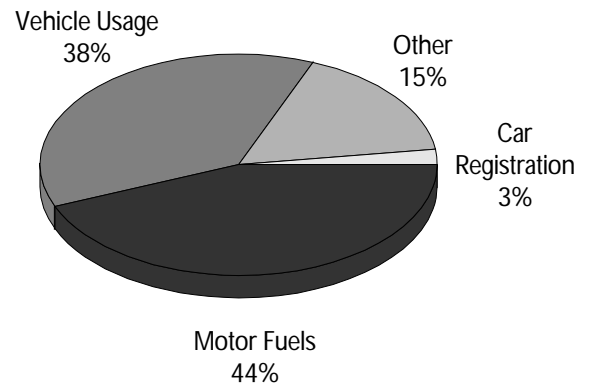
²The tax rate was increased from 5 percent to 6 percent.

MOTOR VEHICLE USAGE TAX

Fiscal Year	Receipts	Percent Change
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
1993-94	278,157,347	19.1
1992-93	233,527,651	11.4
1991-92	209,619,192	2.2
1990-91	205,055,084 ¹	5.8
1989-90	193,791,775	6.5

¹The tax rate was increased from 5 percent to 6 percent.

**Makeup of FY99
Road Fund**



Activities and Accomplishments

KRC Activities and Accomplishments in Fiscal Year 1998-99

Accomplishments during Fiscal Year 1998-99 reflect employees' commitment to KRC's goals. These accomplishments emphasize the Cabinet's mission—to provide courteous, accurate and efficient services for the benefit of Kentucky and its citizens, and administer the tax laws of the commonwealth in a fair and impartial manner.

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

Taxpayer Service

- Responded to numerous requests for Kentucky state tax and economic information from researchers, analysts, media, taxpayers, *think tanks*, and other state, local, and federal agencies.
- Offered extended hours during the period April 1-15, 1999, to better accommodate individual income taxpayers with questions. Also offered Saturday hours at three taxpayer service centers (TSCs) and provided assistance at post offices in three Kentucky cities on the filing deadline day, April 15, 1999.
- Conducted and assisted in various taxpayer education programs and seminars, including the KET call-in show and tax practitioner workshops at the University of Kentucky and University of Louisville.
- Processed 1,185,268 timely and correctly filed 1998 individual income tax returns requesting refunds by May 21, 1999.
- Assisted the Public Utility and Financial Institution Task Forces in identifying current tax policy and developing future tax policy for these industries.
- Developed a new case management system to replace four antiquated systems, providing a better method to monitor noncompliance and collections.



Collection of Tax Revenues

- Repaid the original \$36.1 million *EMPOWER Kentucky* investment by collecting \$8.4 million in the first quarter of the fiscal year, bringing total *EMPOWER* collections since the inception of the program in January 1997 to \$37 million.

- Set an all-time record for revenue generated through KRC collection programs, by collecting \$94.9 million.
- Collected and distributed nearly \$40 million in local property tax revenues.
- Registered 274 new taxpayers through the Voluntary Disclosure Program and generated more than \$2.6 million.

Business Practices

- Participated as a member in the National American Collectors Association to improve the skills and professionalism of KRC collection officers.
- Renewed an interagency agreement with the Kentucky Lottery Corporation whereby KRC collected outstanding liabilities owed by retailers to that quasi-governmental corporation.
- Processed more than 4 million documents and deposited more than \$7 billion in receipts, and made timely deposits into all funds.



Technological Advances

- Continued conversion of KRC workstations and servers to the Windows NT 4.0 operating system, which has been identified as KRC's standard operating system. Approximately 80 percent of the KRC workforce now uses NT workstations and application servers.
- Continued adding taxpayer service centers (TSCs) to the Kentucky Information Highway. The Bowling Green, Hazard, Owensboro, and Paducah TSCs were added to the network. This allows field personnel to participate in the benefits of the network environment, including E-mail and Internet access. Hardware and software was obtained for the remaining six locations not networked.
- Processed 273,571 electronically filed individual income tax returns, representing a 27 percent increase over the previous year.
- Implemented a leasing strategy for desktop workstations as a pilot project. This will allow KRC to refresh workstations every three years.



EMPOWER Kentucky

KRC Proves *EMPOWER Kentucky* Investment a Success

By collecting \$43.4 million in Fiscal Year 1998-99, KRC brought the total amount of General Fund tax revenues collected through its *EMPOWER Kentucky* initiatives to \$72.7 million. This surpasses the original \$36.1 million *EMPOWER* allocation, meaning that KRC has in effect repaid twice the investment which was made in January 1997. The financial benefits for the Simplified Revenue Systems initiative now exceed the funds allocated.

"Your individual and team efforts to make the programs succeed are greatly appreciated," Ron Bingham, chief *EMPOWER* project manager, told KRC employees. "You can be proud of the dedication the Revenue Cabinet staff made to the success of the *EMPOWER* programs."

KRC's staff continues to make great strides in implementing those projects which are not already operational and collecting revenue. For those programs requiring a great deal of long-range planning, Fiscal Year 1998-99 was a period of significant activity in progressing toward establishing these new systems.

EMPOWER Kentucky is Governor Paul E. Patton's initiative to achieve operational efficiencies, cost reductions, and improved service delivery through new technology and training. The 1996 General Assembly set aside a pool of money to fund major modernization efforts. Agencies developed detailed business cases to present their initiatives to a selection panel and compete for funding. On Jan. 15, 1997, Governor Patton announced that KRC's proposals were approved for full funding.

Five specific KRC projects were funded through *EMPOWER Kentucky*. Foremost is a complete modernization of KRC's tax administration systems. This modernization is referred to as the Kentucky Integrated Tax Entity System (KITES). Also included are the Tax Gap project, an improved Corporate Officer Assessment Program, an improved Vendor Offset Program, and an expanded Bank Levy Source Program. While KITES is the major initiative, all five programs will result in greater processing efficiency, improved service, and significant increases in tax collection.

Following is more detailed information on the progress of each of KRC's *EMPOWER Kentucky* initiatives during Fiscal Year 1998-99:

 **Kentucky Integrated Tax Entity System**—This project is comprised of four individual components or

subprojects: mail processing equipment; modernized front-end (MFE); the Master Taxpayer Index (MTI), and the Revenue Evaluation and Decision Support (READS) system. Each of these subprojects is an integral part of the overall KITES project, but each is monitored separately under its own project life cycle. KITES will improve taxpayer service and reduce the cost of taxpayer compliance. It will provide KRC employees efficient and effective access to a complete view of a tax entity's data, thereby improving overall communications with taxpayers as well as improving accounting and audit controls.

KITES will consolidate major KRC business functions into one common database using a commonwealth-standard client server architecture. KITES will provide improved and expanded functionality in areas of registration, accounting, taxpayer assistance, compliance, collection, and research. This improved functionality will provide a much more efficient and effective means of tax administration.

After the vendor evaluations in the summer of 1998 yielded no acceptable solution, it became clear that KRC needed a different approach to its proposed integrated tax system. KRC then designed a project strategy that was sensitive to operational priorities and user needs, the solutions available from the vendor community, and the amount of change KRC could absorb and still maintain adequate service to the public. The new approach phases in the system functions across tax types, beginning with registration and continuing in later phases with accounting and collections. The effect will be to reduce the impact to ongoing operations, avoid the necessity of running both systems in parallel, and leverage existing systems that are highly integrated. The adjustments were necessary to enhance the opportunity for successful vendor partnerships, to reduce project risks, and provide a quicker return of project benefits. With the new approach came a new name: Kentucky Integrated Tax Entity System (KITES). The long-term vision and goals have not changed.

The mail processing equipment strengthens the capacity for sorting incoming mail via custom programming, improves the speed of mixed mail handling and extraction, and provides remittance detection for staging work more efficiently for remittance processing. The

EMPOWER Kentucky

equipment was installed in October 1998. It consists of a sorter, which is capable of handling more than 23,000 pieces of mail per hour; an auto-extractor, which automatically opens pieces of mail identified by the sorter as containing only a payment coupon and a check; and 15 rapid extraction desks, which allow for faster opening and processing of mail which cannot be opened by the automated extractor.



KRC employee Jim Locker demonstrated the auto-extractor component of the mail processing equipment.



Secretary Schaaf pointed out features of the mail processing equipment to a Lexington television reporter.

On April 14, a media open house was held at KRC's Perimeter Park location on Louisville Road in Frankfort to showcase the mail opening equipment. KRC Secretary Sarah Jane Schaaf and staff members of the Division of Revenue Operations demonstrated the equipment for members of the print and broadcast media from Frankfort, Louisville, and Lexington.



Still photographers captured the sorter at work.

The MFE process includes wholesale hardware and software upgrades that support functions related to electronic data capture (i.e., scanning), workflow for

automated data correction/verification (i.e., electronic worklists), electronic remittance processing, and image storage and retrieval. This process will provide a much more efficient and effective method of capturing and transmitting data to the appropriate host systems. More dependable and timely data updates will reduce the amount of non-value-added activities and improve overall staff efficiencies. Electronic images of paper documents will provide immediate desktop access to documents as needed to satisfy, verify, or validate information requests, which will improve overall taxpayer assistance.

A contract was awarded in December for installation of the scanning and imaging system, and testing was underway as of June 30, 1999. The first two taxes to be processed by the system are sales and use tax and withholding tax. These two high-volume tax types were chosen because they generate the highest dollar amounts of all taxes collected by KRC.

The remaining components of KITES comprise development of two systems, MTI and READS. MTI will be the foundation for all future system integration at KRC by linking demographic and account data across taxpayer relationships (e.g., partners, subsidiaries, spouses, etc.). MTI will integrate information by taxpayer entity in order to allow KRC to provide more efficient and complete taxpayer service. READS is a data warehouse with decision support software to allow KRC to create information for decision-makers from its vast amounts of data. KITES is the first project to use the commonwealth's new Strategic Alliance Services procurement method. This method frees agencies to interact with a predetermined pool of information technology vendors in crafting their statement of project work. As of June 30, 1999, the KITES Project Team had met with all MTI and READS vendors and is expecting procurements before the end of 1999.

Tax Gap Project—The term *tax gap* refers to the difference between the amount of taxes due and the amount actually paid or collected. The program identifies sources of the gap.

The Tax Gap project consists of a new discovery and compliance section for business nonfilers and beneficiaries of income from pass-through entities. Other programs included in the Tax Gap initiative are the

EMPOWER Kentucky

Simplified Tax and Wage Reporting System, also known as the W-2 Demonstration Project; improvements in the Federal-State Match Program, a program to close the tax gap from beneficiaries of partnerships and S corporations (the Pass-Through Entity program), and an expanded property tax compliance program.

In Fiscal Year 1998-99, the W-2 Demonstration Project exceeded its revenue estimates by 17 percent. The project registered 115 nonfilers and collected more than \$3.6 million.

The Tax Gap Discovery Section, created in 1997 to administer the nonfiler discovery program, registered 743 businesses and collected more than \$4.5 million.

The Federal-State Match Program generated \$1.6 million, exceeding revenue projections of \$897,000.

The Pass-Through Entity Program generated \$2.3 million, exceeding revenue projections of \$862,500.

The property tax discovery and compliance programs resulted in more than \$20 million in revenue for local governments and taxing districts, and more than \$12 million in state revenue.

Corporate Officer Assessment Program—KRC has the authority to assess corporate officers personally for past due withholding, sales and use, coal severance, health care provider, controlled substance, and bank franchise taxes. This initiative is to automate the process of issuing officer assessments, and increase staff levels to accommodate increasing caseloads.

The Corporate Officer Assessment Program was originally presented in three segments. The first segment dealt with automating a manual process by modifying KRC's receivable system and collection system so that officer assessments could be created and monitored online. After the project was funded, the implementation time frame and cost estimates were increased by the Department of Information Systems. As a result, this project has been incorporated in KRC's KITES project. Projected revenues are being recovered by using two additional positions in the manual environment.

The second and third segments involved using additional staff to reduce an existing backlog of cases within the collection system that had not been

assessed, and to handle ever-increasing caseloads to prevent further backlogs. Eight positions were added for this purpose.

Due to the overwhelming success of the previous fiscal year, the projected revenues for Fiscal Year 1998-99 were increased from the original estimate of \$5 million to \$6 million. The initiative again exceeded its revenue estimates by collecting \$6.95 million.

Vendor Offset Program—The Vendor Offset Program was presented as an initiative designed to enhance General Fund savings by retaining payments to indebted vendors with outstanding tax obligations. The objective could be met by modifying existing commonwealth systems to automate KRC's vendor payment offset process.

The Vendor Offset Program went into production in October 1997. The process was designed to provide an efficient method by which state tax debts can be transmitted and matched against the Finance and Administration Cabinet's Vendor File. Through this process, indebted vendors are identified and any payments that may be issued to them are matched against KRC's accounts receivable file.

Payments offset through the automated vendor payment offset process are electronically transferred and applied to KRC's accounts receivable systems.

Notification is sent to the indebted vendors when their debts are submitted to the Finance and Administration Cabinet, as well as after an offset occurs.

The Division of Collections administers the program within KRC. The Vendor Offset Program was designed such that any state government agency desiring to participate in the process may do so by conducting any system modifications that may be required in order to participate.

The Vendor Offset Program exceeded revenue estimates of \$4.1 million by collecting \$4.6 million in Fiscal Year 1998-99.

Bank Levy Source—This initiative enables KRC to gather banking data electronically from information



EMPOWER Kentucky

supplied by taxpayers. This information is used to identify assets when enforced collection actions become necessary.

The program again substantially exceeded its projected revenues for Fiscal Year 1998-99. Revenues were projected to be \$4.2 million, but more than \$7.5 million was actually collected.



KRC continues to share this information with other state agencies, including the

Workforce Development Cabinet, which collected more than \$36,000 in levies as a result of information provided by KRC. KRC also continues development of an interagency agreement with the Cabinet for Families and Children to share bank account information.

KRC also participated in *EMPOWER Kentucky* projects with other agencies, including preparations for the July 1, 1999, rollout of the Management and Administrative Reporting System (MARS), part of the Finance and Administration Cabinet's Simplified Administrative Services initiative.

SEATA Conference

KRC Hosts Successful SEATA Conference

KRC hosted the 49th annual conference of the Southeastern Association of Tax Administrators (SEATA) July 10-14 at Lexington's Marriott Griffin Gate Resort.

Nearly 700 guests, including government and industry delegates, spouses, and children, spent their time in Kentucky exchanging tax administration information and enjoying Bluegrass hospitality.

Guests spoke highly of their experience in Kentucky. "This was the best conference ever," and "They should hold SEATA here every year," were two common compliments.

One comment, made to a KRC employee by a delegate from Louisiana, summed up the event. "I've been coming to SEATA conferences for 26 years. I'm retiring this year, and this is my last SEATA conference. Thanks for making this the best one yet."

"It would be impossible for me to individually mention each person who helped make SEATA such a rousing success," said KRC Secretary Sarah Jane "Susie" Schaaf. "We knew there were many talented people who work here, but we didn't realize just how talented they were until it came time to present this conference. I'd like to thank everyone who had a hand in making this conference such an outstanding event. All the activities were well-organized and enjoyable, and our employees who worked at the conference or behind the scenes at the office, and during the planning phase, did a truly first-class job."

Planning for the conference began more than a year prior to the event. A delegation from Kentucky attended the 1998 SEATA conference in Hot Springs, Ark., to observe the event and promote the 1999 conference in Kentucky. Dozens of KRC employees were involved in planning the conference, securing facilities, scheduling events, and making countless preparations for a smooth conference.

The conference officially began on Saturday, July 10, with a dinner for commissioners at the Governor's Mansion hosted by Crit Luallen, Secretary of the Executive Cabinet.



The first event open to all participants was the *Family Night* at the Kentucky Horse Park on Sunday evening. Delegates, guests, and children enjoyed a variety of activities, ending with a picnic buffet dinner and entertainment by the *Stephen Foster Story* singers. Children enjoyed face painters, jugglers, pony rides, posing for photos with Disney characters, and many other activities. Hayrides and the Horse Park's *Parade of Breeds* fascinated adults and children alike.



Family Night participants enjoyed a buffet-style picnic and a hayride at the Kentucky Horse park. Many forms of entertainment were provided, including juggling by KRC employee Steve Meuser.



SEATA Conference

On Monday and Tuesday, separate programs were held for delegates, spouses, and children. Delegates attended Monday's opening session, which included remarks by Mary Ellen Withrow, Treasurer of the United States, then participated in breakout sessions on various topics.

Spouses had their choice of a trip to Berea to tour Churchill Weavers, eat lunch at Boone Tavern, and shop in Old Town Berea; or a tour of Keeneland and a horse farm.



Trips to Churchill Weavers in Berea, and the Labrot & Graham Distillery in Woodford County, were among the options offered for spouses and guests of SEATA participants.



Children were treated to a variety of activities including visits to the Mad Potter, the UK Basketball Museum, Shillito Park, the Lexington Children's Museum, and a bowling tournament.



Children of SEATA participants visited the Mad Potter in Lexington on Monday.

Monday afternoon also saw golf and tennis tournaments at Griffin Gate for delegates and guests, which were well-attended.

Tuesday offered a full day of activities for delegates, including lunch where the featured speaker was C.M. Newton, UK athletics director, and more breakout



Remarks by KRC Secretary Sarah Jane "Susie" Schaaf, above, and United States Treasurer Mary Ellen Withrow, below, highlighted business sessions on the first full day of the conference.



sessions. Some delegates made the short trip to Frankfort to view KRC's new modernized front end mail opening and imaging systems.

Spouses visited the Labrot and Graham Distillery in Woodford County on Tuesday morning, while the children boarded buses for Louisville and Six Flags Kentucky Kingdom. The younger children returned to Lexington around 7 p.m. for a poolside pizza party and *Silly Olympics*, while the older children stayed at Kentucky Kingdom and returned around 11 p.m.



Children of SEATA participants enjoyed Kentucky Kingdom in Louisville on Tuesday.

Tuesday night was highlighted by a banquet and dance, which was attended by an overflow crowd. Photos of conference events were made available to SEATA participants.

Expenses for the conference were paid for by SEATA.

Education Pays

KRC Participates in *Education Pays* Campaign

Governor Paul Patton announced the commonwealth's *Education Pays* project at news conferences in Louisville and Lexington on July 15, 1998. The campaign features a graphic of a graduate with diploma raised in victory over a backdrop of a map of Kentucky.

"Kentucky is earning a national reputation for excellence in education. We have a good product, and it's getting better. *Education Pays* is an effort to make sure that everyone, no matter what age, becomes aware of the value of an education and the opportunities available in Kentucky," Governor Patton said. "Education is the key to improving the quality of life in Kentucky and raising our standard of living."

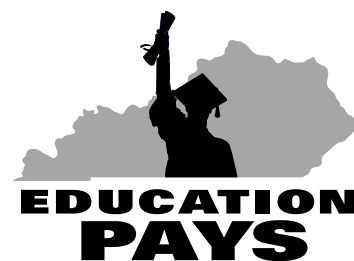
The *Education Pays* logo is printed on Kentucky state government letterhead, maps, and other appropriate places. KRC actively participated in the initiative by:

- Including the logo on all tax forms and publications produced by KRC since the inception of the program.
- Being among the first state agencies to use the logo on its Web site, and providing a link to the official *Education Pays* Web site.
- Profiling employees who have benefited by furthering their education in **Revenue Assets**, KRC's bi-monthly employee newsletter, to exhibit positive examples that *Education Pays*.
- Placing *Education Pays* posters in all KRC offices, including 120 property valuation administrators' offices and 11 taxpayer service centers across Kentucky.
- Placing *Education Pays* materials in the historical display, located on the third floor of KRC's main offices at 200 Fair Oaks Lane in Frankfort.
- Making *Education Pays* a prominent subject of discussion in the Cabinet-wide meeting held in September 1998. This included the distribution of *Education Pays* bumper stickers to all interested employees.
- Encouraging participants in KRC's Speakers' Bureau to promote the *Education Pays* program.

Kentucky business and civic groups enthusiastically joined the project. The Kentucky Chamber of Commerce and Columbia Gas are among those incorporating the *Education Pays* logo in newsletters, bills sent to customers, and in other ways. The Prichard Committee for Academic Excellence and the Partnership for Kentucky Schools, the Kentucky Press Association, Kentucky Broadcasters Association, and Kentucky Cable Television Association endorsed the campaign, which includes broadcast and print public service announcements.

"KERA, the Postsecondary Education Improvement Act, full funding of needs-based scholarships, the new merit scholarship program for high school students, increased funding for adult education, and our newly created Office of Early Childhood Development are all tools that can help us provide the best possible education to both traditional and nontraditional students in Kentucky," Governor Patton said. "But unless people understand that an education is the way to get a good job and provide for a good quality of life, they won't take advantage of these opportunities. We have to elevate the awareness of the value of learning in Kentucky and motivate people to get an education."

"Virtually every person wants a better life for their children, and we must convince the undereducated parents of the commonwealth that a better life for their children lies with education. If it is important to the parents, it will be important to the children," Governor Patton said. "With constant exposure to a consistent message, we can convince people that *Education Pays*."



Taxpayer Service

KRC Prepared for Y2K

During the past two years, KRC has focused on ensuring there will be no impact to KRC or to taxpayers because of the Year 2000 (Y2K) computer glitch.

Beginning in May 1997, mainframe applications and corresponding interfaces were assessed and converted to a Y2K-compliant format. KRC tested each of these systems as conversions were made. KRC also participated in a state disaster recovery exercise last fall that included a Year 2000 date simulation. All mainframe tax systems were Y2K-compliant by June 30. KRC also upgraded all PC-based applications for Y2K compliance, completing this project by Oct. 31.

KRC officials are confident that the Cabinet and taxpayers will experience no problems resulting from the Y2K computer glitch.



Kentucky Income Tax Forms Packet Has New Look

In 1999, for the first time, all Kentucky individual income tax forms were combined into one booklet. This included Forms 740, 740-S, and 740-EZ; Schedules A and P; and the intangible property tax return.



According to KRC Secretary Sarah Jane Schaaf, "We made this change to simplify the tax filing process and to provide Kentucky taxpayers with all the printed information necessary to complete their return in one convenient packet—whether they use a long or short form."

Governor Paul E. Patton said, "This modification reflects our commitment to cut through the bureaucratic red-tape and make government simpler and more accessible to the people of the commonwealth."

New Taxpayer Service Programs Are Successful

During the individual income tax filing season, KRC offered two new forms of taxpayer assistance. Both programs proved successful and were used by dozens of Kentucky taxpayers to receive help with filing their 1998 individual income tax returns.

Taxpayer service centers (TSCs) in Ashland, Northern Kentucky, and Owensboro were open on April 10, which was the Saturday before the filing deadline of Thursday, April 15.

The three TSCs provided assistance to 152 taxpayers who made telephone calls, and 126 taxpayers who visited the field offices. In addition, the TSCs also accepted several returns from taxpayers.

On filing day, April 15, TSCs in Hopkinsville, Lexington, and Louisville provided taxpayer assistance at the post offices in those cities. Representatives from those TSCs provided assistance to more than 150 taxpayers, and accepted more than 130 completed returns from taxpayers who chose to file in person rather than through the mail.



These programs were very successful and KRC is considering repeating them for the 1999 tax year.

Taxpayer Service

TeleFile Project Participation Quadruples Initial Estimate

During the 1999 individual income tax filing season, KRC partnered with the Internal Revenue Service (IRS) in a joint TeleFile pilot project. This pilot was offered statewide and provided the opportunity for many Kentuckians to file their 1998 federal and Kentucky individual income tax returns together electronically over the telephone in a 20-minute phone call. Indiana was the only other state involved in the pilot for 1999.

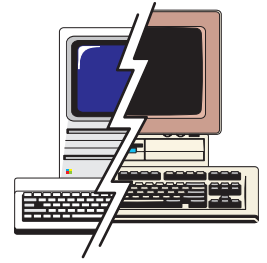


More than 40,000 Kentuckians filed their 1998 individual income tax returns using the TeleFile system, quadrupling the initial 10,000 participation estimate. According to Governor Paul E. Patton, "The TeleFile pilot project dovetails nicely with *EMPOWER Kentucky*, which promotes improved efficiency of government operations through technology. This is a win-win situation for the taxpayer and for the Revenue Cabinet. Taxpayers receive their refund faster and don't have to worry about filling out and mailing the return; and the Revenue Cabinet doesn't have to deal with manually processing all the extra paper."

The 740-T forms packet for use with the TeleFile system was mailed to more than 140,000 Kentuckians who met the federal TeleFile and Kentucky guidelines for the 1998 tax year. Preliminary plans are being made to continue this pilot for the 1999 tax year.

KRC's Web Site Redesigned

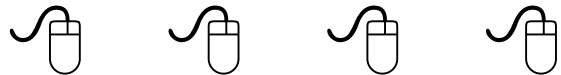
KRC's Online Taxpayer Service Center (TSC) got a facelift in December. In conjunction with the uploading of 1998 individual income, corporation income, and personal property tax forms, an entire new Web site went online shortly before Christmas.



The new site simplifies access to various categories of information, incorporates a uniform graphic navigation bar on each page, and eliminates the use of frames to reduce the number of scroll bars on each page.

New graphics provide an easy-to-read interface and a pleasing visual effect, while not slowing down the access to information through the use of exceptionally large images.

KRC's Online TSC is located at <http://www.state.ky.us/agencies/revenue>.



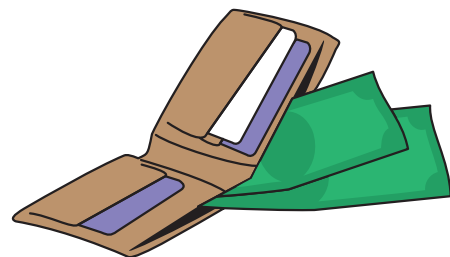
Standard Deduction, Pension Exclusion Increase for 1998 Tax Year

For the 1998 tax year, Kentucky's standard deduction for individual income tax increased from \$900 to \$1,200. The standard deduction is claimed by persons who choose not to itemize deductions on their individual income tax return. A large percentage of low income taxpayers use the standard deduction.

For 1999, the standard deduction increases to \$1,500; and for the year 2000 and forward the standard deduction will be \$1,700. In 1998, the standard deduction increased from \$650 to \$900. This was the first increase in approximately 30 years.

For the 1998 tax year, the pension exclusion for private pensions increased to 100 percent of the pension amount, up to a maximum of \$35,000. This was the fourth and final year of a four-year phase-in for this exclusion.

For the 1999 tax year, the pension exclusion for private pensions increases to \$35,700, pursuant to KRS 141.0105, which allows KRC to adjust the amount of the exclusion annually for inflation. Private pensions include any source of pension or retirement income other than Kentucky or federal public pensions, which are already exempt.



Taxpayer Service

Intangible Refund Project Completed Ahead of Schedule

It is not often that any government agency can say they have finished a project ahead of schedule, but that was the case with KRC's intangible tax refund project, which wrapped up two months early. In November, KRC completed the task of preparing and mailing checks to taxpayers who applied and were eligible for refunds of taxes paid on intangible personal property, resulting from the *St. Ledger v. Revenue Cabinet* court case.

"When this case was settled in September 1997, I asked the Revenue Cabinet to issue these refunds as expeditiously as possible. They gave me a 14-month timetable under which the refund project would be carried out, but finished their job in only 12 months. The Revenue Cabinet, in completing this project with such speed and efficiency, has underscored the primary goals of my administration to improve the quality of government services to taxpayers," said Governor Paul Patton.

A total of 114,018 checks worth \$170 million was issued.



On Sept. 10, 1997, the case was settled in Jefferson Circuit Court. The Regular Session of the 1996 General Assembly previously appropriated additional funds to hire seasonal employees to work in this court-ordered refund project. As early as the spring of 1996, KRC obtained additional office space and hired a temporary staff of 25 people to assist in working the more than 500,000 refund claims submitted by more than 100,000 taxpayers as a result of this case. The seasonal staff, along with regular KRC employees, began sorting through the refund claims and setting up a database to issue refunds. This project was originally scheduled for completion by the end of 1998.

KRC began processing refund claims in May 1996 in anticipation of the court ruling. The first refunds were issued immediately after a settlement was reached in the case in September 1997.



District Judges Asked to Accept Affidavit of Exemption for Inheritance Taxes

On June 18, KRC Secretary Sarah Jane Schaaf sent a memo to district court judges in Kentucky, requesting that they accept an *Affidavit of Exemption* instead of requiring an inheritance and estate tax return acceptance letter for the final settlement and closing of the administration of an estate. Use of the *Affidavit of Exemption* will ease the administration of estates which do not owe any Kentucky death tax and are not required to file a federal Estate and Gift Tax Return. The affidavit should be used only when the entire estate passes to nontaxable beneficiaries and the value of the estate is less than the federal unified credit exemption equivalent. Using this affidavit will eliminate expenditures of time and money for the preparation and review of inheritance and estate tax returns.

Filing the single *Affidavit of Exemption*, rather than a no tax due inheritance and estate tax return, is another KRC *EM-POWER Kentucky* initiative to relieve taxpayers of the burden of filing unnecessary paperwork.



Homestead Exemption Increases to \$25,400



The Homestead Exemption for personal property taxes increased by \$1,000 for the 1999 and 2000 tax years. The amount of the exemption is recalculated every two years to reflect inflation.

The homestead exemption, originally established under a constitutional amendment in 1971 and prescribed in KRS 132.810, will be \$25,400. This represents a \$1,000 increase over the 1997-98 exemption of \$24,400.

During the 1999 tax year, more than 320,000 elderly or disabled Kentuckians will realize millions of dollars in property tax savings through the Homestead Exemption.

To qualify for the Homestead Exemption, a person must be at least 65 years old during the tax period or be classified as totally disabled by any public or private retirement system. Prior to enactment of Constitutional Amendment #2 this past November, only taxpayers disabled under Social Security or Railroad Retirement were eligible for the disability exemption.

Eligible property must also be owned, occupied, and maintained by the taxpayer as a personal residence on the Jan. 1 assessment date.

Taxpayer Service

Filing Extension Granted for Troops Serving in Kosovo Conflict

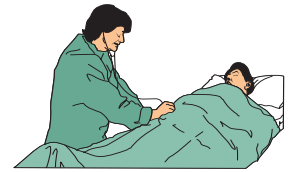
On April 13, President Clinton signed an executive order declaring the Federal Republic of Yugoslavia (Serbia/Montenegro), Albania, the airspace above, and adjacent waters as a combat zone, effective March 24. This declaration was made pursuant to the United States Constitution and Section 112 of the Internal Revenue Code of 1986 (26 U.S.C. 112).



When the president signs an executive order designating certain areas combat zones, a provision of KRS 141.215 is automatically activated. The law provides for deferred filing of Kentucky individual income taxes and payment of taxes due. Under Kentucky law, a one-year extension of the filing date went into effect for those persons serving in the combat zone on April 15. The one-year period begins when service in the combat zone ends. No penalty or interest will accrue on tax payments made during the one-year deferment period.

Kentucky law is based upon the Internal Revenue Code in effect on Dec. 31, 1997. The president's designation of the combat zone activated Section 112 of the Internal Revenue Code. Under this provision, enlisted military personnel may exclude from their gross income all service income received each month for active service in the combat zone. For commissioned officers, the exclusion is limited to the highest rate of basic pay at the highest pay grade that enlisted personnel may receive, plus the amount of hostile fire-imminent danger pay received each month for active service in the combat zone.

The effective date is for pay received in the combat zone on or after March 24, and includes income for any month in which the military member is hospitalized as a result of injury or disease incurred while serving in the combat zone.



KRC Offers Grace Period for Vehicle Valuation to Benefit Taxpayers

A new law for valuing motor vehicles in Kentucky for usage tax purposes, House Bill 74, enacted by the 1998 Kentucky General Assembly, went into effect on Aug. 1. Since this is such a major change, KRC worked with consumers, automobile dealers, and county clerks to ensure compliance with the new law.

KRC granted a grace period until August 15, during which county clerks were authorized to value vehicles purchased prior to August 1, under the old valuation provisions or the new valuation provisions, whichever was most beneficial to the taxpayer.

As of August 1, motor vehicle usage tax is based on the total consideration given for a vehicle as attested to by both buyer and seller in an affidavit. A reduction for the trade-in allowance assigned by the seller is deducted in the case of most used vehicle purchases. Total consideration given does not include manufacturer or dealer rebates, interest payments made over the life of a loan, the value of extended warranties, and service contracts. After the buyer and the seller agree on the total

consideration given, they must complete an affidavit. The affidavit must be signed by both the buyer and the seller. Each signature must be individually notarized.

HB 74 made provisions for the valuation of both new and used vehicles in the event an affidavit is not available. In the case of new vehicles, taxable value will be determined using 90 percent of the manufacturer's suggested retail price (MSRP) (81 percent for trucks weighing in excess of 10,000 pounds). In the case of used vehicles the taxable value is based on the average retail value from the appropriate reference manual prescribed by KRC.



Taxpayer Service

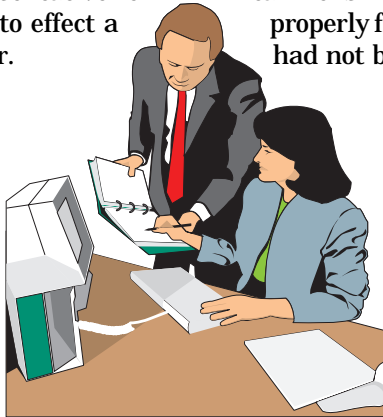
Office of Taxpayer Ombudsman

The Office of Taxpayer Ombudsman serves a very important and effective role within KRC. The staff of the Ombudsman's office facilitates the resolution of complaints and problems when a taxpayer or his representative requests assistance or an independent voice to effect a fair and impartial resolution of a tax matter.

In addition to direct calls from taxpayers or their representatives, the office receives frequent referrals on behalf of taxpayers from fellow KRC 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 Office of Constituent Services in the Governor's Office and the Legislative Research Commission.

Referrals to the Ombudsman's office include requests for general information as well as specific assistance. In Fiscal Year 1998-99, the staff worked on a variety of issues, including waiving of civil penalties when reasonable cause

for waiver was demonstrated, removing wage and bank levies when the taxpayer would have suffered significant hardship as a result of the levy, releasing and removing tax liens from taxpayer records when the lien was improperly filed, and facilitating the review of protests that had not been resolved. The office also assisted taxpayers in their requests for a payment plan, assisted in the negotiations with taxpayers in the offers in settlement program, and provided assistance to taxpayers in resolving issues regarding vendor offsets.



As the advocate for the taxpayer, the staff of the Ombudsman's office serves on various KRC committees to provide input into forms design, legislation, training, and educational programs. The staff led roundtable discussions on taxpayers' rights and the role of the Office of Taxpayer Ombudsman at the 1998 Department of Property Valuation's Annual Conference. The office also works closely with local officials throughout Kentucky in the resolution of delinquent property tax bills.

Collection of Tax Revenue

KRC Employees Certified by American Collectors Association

Four employees of KRC's Division of Collections were honored for becoming certified by the American Collectors Association (ACA). Chris Fasoldt, Phyllis Oakley, Paul Olds, and Mick Vest were presented certificates for completing training seminars and passing a certification test administered by ACA. These employees were honored and recognized by KRC Secretary Sarah Jane "Susie" Schaaf during a Cabinet-wide meeting.

ACA is an international organization comprised of businesses involved in accounts receivable management. It has more than 3,400 members in 55 countries. It provides assistance in leadership, direction, education, and service to members, including training. Only about 10 percent of ACA's members successfully complete certification requirements.



Left to right: Mick Vest; Paul Olds; Mack Gillim, Director, Division of Collections; Phyllis Oakley; Revenue Secretary Sarah Jane Schaaf; Chris Fasoldt; and then-Commissioner Alex Rose of the Department of Law.

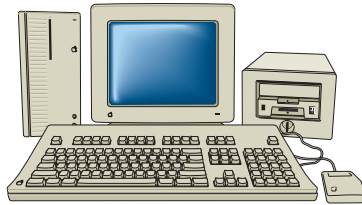
Technological Advancement

KRC Awards \$243,591 for Technology Projects

KRC's Department of Property Valuation, in conjunction with the Kentucky Property Valuation Administrators (PVA) Association, awarded \$243,591 in grants under the Innovative Technology Fund Grant Program. The PVA offices in the 15 counties awarded grants will contribute a total of \$62,163 in matching funds, for a total project expenditure of \$305,754.

Award winners were:

Ballard County PVA Delores Hatler proposed to establish a geographic information system (GIS)-based farm assessment system, utilizing global positioning system (GPS) equipment and software, and a network upgrade. This project was funded in the amount of \$23,019, with a local match of \$5,755.



Bell County PVA Geraldine Jeffers proposed to develop GIS capability for implementing the conventional mapping project currently in operation, as well as integrating with the 911 system, in cooperation with the Bell County Fiscal Court and the Cumberland Valley Area Development District. This project was funded in the amount of \$28,190, with a local match of \$7,047.

Former Boone County PVA David Turner proposed to initiate an automated data collection project utilizing laptop computers. This project was funded in the amount of \$12,000, with a local match of \$3,000.

Crittenden County PVA Ronnie Heady proposed to upgrade his old Computer Assisted Drafting and Design (CADD)-based farm assessment system to GIS, for use with all classes of property. This project was funded in the amount of \$15,990, with a local match of \$3,997.

Edmonson County PVA Benton Cowles proposed to acquire a scanner and upgrade his existing Tax Roll Information Management (TRIM) network with a Y2K-compatible computer and a digital camera. This project was funded in the amount of \$5,287, with a local match of \$1,322.

Fleming County PVA Connie Crain proposed a GIS with GPS control, digital photography and NT network

upgrade. This project was funded in the amount of \$14,560, with a local match of \$3,640.

Hart County PVA Mary Bunnell proposed a network upgrade for the existing TRIM system and to accommodate a proposed GIS project, including a new server/workstation, scanner, and Windows NT operating system. This project was funded in the amount of \$15,026, with a local match of \$3,757.

Lincoln County PVA David Gambrel proposed a major upgrade of his existing TRIM network, enhanced with GIS/GPS, and digital camera capability. This project was funded in the amount of \$28,428, with a local match of \$7,107.

Logan County PVA Ben Brown proposed implementing a GIS data collection project, acquiring GPS equipment and software. This project was funded in the amount of \$9,040, with a local match of \$2,260.

Marshall County PVA Ann Riley proposed adding GPS capability to the PVA office, utilizing Trimble GPS equipment, training, and a notebook computer. This project was funded in the amount of \$11,995, with a local match of \$2,999.

Morgan County PVA Darrell Bradley proposed acquiring digital photography capability, utilizing a Sony Mavica camera and a Photo Smart printer. This project was funded in the amount of \$770, with a local match of \$193.



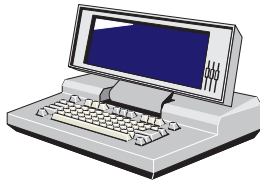
Pike County PVA Lonnie Osborne proposed a full scale GIS implementation, with access to the software from 15 workstations on a Windows NT network, and five digital cameras. This project was funded in the amount of \$34,942, with a local match of \$10,000.

Rowan County PVA C. J. Baker proposed a system to give the PVA office and taxpayers access to the county clerk's computerized (deed) indexing system. This project was funded in the amount of \$6,000, with a local match of \$1,500.

Trigg County PVA Mike Bryan proposed the implementation of a GIS/GPS system in cooperation with the Trigg County Fiscal Court and the Pennyriple Area Development District. This project was funded in the amount of \$18,344, with a local match of \$4,586.

Technological Advancement

Webster County PVA Jeff Kelley proposed a GIS/GPS system, including a server, three workstations, GPS equipment, a notebook computer, a digital camera, and a plotter. This project was funded in the amount of \$20,000, with a local match of \$5,000.



In addition to the 20 percent match requirement, grant recipients were required to submit progress reports on project implementation, as well as offer workshops or other demonstrations at the request of the Department of Property Valuation. The results of this funding should

also be apparent in the methods utilized in 21 PVA offices, with improved assessment quality and taxpayer service as the ultimate result.

The Innovative Technology Fund was established in 1996 as a means to promote the use of technology among the state's PVA offices. The initial funding was in the amount of \$300,000. Last year, \$178,562 was awarded to six counties, leaving \$121,438 in the fund. This year, PVAs proposed projects totaling over \$500,000. KRC was able to more than double the amount of money in the grant pool so that more projects could be funded. Grant awards were determined by a committee of information technology and management personnel.

Pike County Receives \$50,000 for Countywide GIS System

On Aug. 26, Governor Paul Patton awarded a \$50,000 check to the Pike County Fiscal Court for the state's share of start-up costs for the Pike County Geographic Information System (GIS) Consortium.



"A county-wide Geographic Information System for Pike County is an exciting concept, putting them on the cutting-edge of technology. We are optimistic about the potential it holds for both public and private users alike. It provides an effective tool for public utility relay, health care delivery systems, and many, many more public services such as roads," said Governor Patton.

Governor Patton also announced that the Kentucky Revenue Cabinet's Department of Property Valuation is further assisting with this project by funding a full-time position in the Pike County Property Valuation

Administrator's Office to collect and verify field data which will be used to complete the property ownership layer of GIS.

GIS technology is a rapidly growing technological innovation already in use in the state's larger counties. GIS has many public uses such as water, sewer, and other utility expansion; economic development planning; and in many counties provides a critical linkage with emergency 911 systems. It ties local agencies together under one system, which eliminates the need for multiple databases and provides consistent information to the taxpayer.

One of the unique features of the Pike County GIS Consortium is the private/public partnership it represents. According to Mike Haydon, commissioner of the Department of Property Valuation at the time of the award, "The participation of coal companies, state and local government, and public utilities in the consortium is an appealing model for other rural counties still exploring this technology, reducing the costs for each of the end users."

Legal Issues

1998-99 Legal Developments and Court Decisions Impacting KRC

KRC's Division of Legal Services handles a substantial number of cases presenting a variety of issues arising under and concerning Kentucky's tax laws. The division continues to experience an increase in both the complexity of the issues and amounts of money at stake in these cases. The division's responsibilities have been expanded in recent years to include litigation and other legal services relating to the ad valorem taxation of intangible and tangible property and unmined minerals.

The division represents KRC in all cases before the Kentucky Board of Tax Appeals (KBTA) and other administrative tribunals of this state and before the state and federal courts. This representation includes handling all phases and levels of litigation, including discovery, trials, hearings, and appeals.

In addition to its litigation responsibilities, the Division of Legal Services performs a number of other duties and functions. These duties and functions include providing legal advice, rendering written legal opinions, participating in protest conferences, and reviewing and drafting proposed legislation and regulations and documents implementing or explaining KRC policy and the tax laws of this state.

The cases handled by the Division of Legal Services address issues, or have resulted in precedents, of great importance and interest to taxpayers and the commonwealth. A number of these cases are discussed below.

Children's Psychiatric Hospital of Northern Kentucky, Inc. v. Revenue Cabinet, Ky., 989 S.W.2d 583 (1999)

In this case the Kentucky Supreme Court upheld the health care provider tax enacted by the Kentucky General Assembly in 1993 (House Bill 1) and in 1994 (House Bill 250) against a number of constitutional challenges brought in an action filed by Kentucky hospitals and the Kentucky Hospital Association. The court first held that the exemption for institutions of purely public charity provided for in Section 170 of the Kentucky Constitution did not apply to the health care provider tax, as that constitutional provision applied only to ad valorem or property taxes.

The court further held that the health care provider tax was not impermissible special legislation. On this point, the court declared that its previous decision in ***Revenue Cabinet v. Smith, Ky., 875 S.W.2d 873 (1994)*** was controlling. The court also rejected arguments that the tax violated the equal protection and due process provisions of the state and federal constitutions because a rational basis existed for the law. The purpose of the law was to provide medical care for the indigent and the classifications utilized in the health care provider tax were based on federal law, grounded in public interest and not arbitrary or unreasonable.

Finally, the court held that the title of House Bill 250, "An Act relating to health care reform and providing funding therefor," did not violate Section 51 of the Kentucky Constitution, which provides that "no law enacted by the General Assembly shall relate to more than one subject, and that shall be expressed in the title..." This title gave fair and reasonable notice of the bill's contents, the court ruled.



Yeoman v. Commonwealth, Ky., 983 S.W.2d 459 (1998)

The Kentucky Supreme Court upheld House Bill 250 enacted by the 1994 Kentucky General Assembly against a number of legal challenges. This legislation consisted of a number of health care reforms, including the creation of a health policy board, provider arbitration, certificate of need procedures, insurance reform, medical education, and the current health care provider tax.

The challenge to House Bill 250 was based upon the following assertions: (1) The bill was special legislation enacted in violation of § 59 of the Kentucky Constitution. (2) The bill violated the equal protection guarantees of the United States and Kentucky Constitutions. (3) The bill was a revenue-raising measure that violated § 47 of the Kentucky Constitution because it originated in the Senate or because the Senate amendments to House Bill 250 were unrelated to revenue. (4) House Bill 250 delegated certain powers of the governor to a third party in violation of the separation of powers provisions of the Kentucky Constitution. (5) The privacy rights of the citizens of the

Legal Issues

Commonwealth of Kentucky were violated by the release of certain information pursuant to House Bill 250. (6) Actions of certain officials of the health policy board created by House Bill 250 violated the Kentucky Open Meetings Act. (7) House Bill 250 provided for payment of government officials by a nongovernmental organization in violation of § 246 of the Kentucky Constitution and KRS 11A.040(5) and 64.640. (8) The provider tax violated the United States Constitution's supremacy clause in that it was contrary to the federal Medical Voluntary Contribution and Provider-Specific Tax Amendments of 1991. (9) The title of House Bill 250 was not properly titled in accordance with Section 51 of the Kentucky Constitution.

The Kentucky Supreme Court rejected all of the foregoing contentions in holding that House Bill 250 was constitutional.

Kentucky-American Water Company v. Revenue Cabinet, Ky., 997 S.W.2d 2 (1999)

The issues in this sales and use tax case were (1) whether the machinery for new and expanded industry exemption, KRS 139.480(10), applied to the taxpayer water company's purchases of service mains, valves, and meters for use in its 1,197 mile-long water distribution system extending from its water treatment plant to water haulers, other public and private water systems, and end users, and (2) whether the energy exemption, KRS 139.480(3), applied to energy used in that distribution system. The Kentucky Supreme Court ruled for KRC on both issues, reversing decisions of the Kentucky Court of Appeals and Fayette Circuit Court, and reinstating the determination of the KBTA.

The Supreme Court first noted that for the machinery for new and expanded industry exemption to apply, the machinery in question must be (1) used directly in a manufacturing or processing production and (2) installed in a plant facility. Neither requirement was met in this case.

The manufacturing process in question was water purification, which ended with the generally accepted saleable product being deposited in the clear well, a storage tank in the water treatment plant. During the audit period, water was withdrawn from the clear well and sold to customers such as water haulers and bulk customers. Thus, the court held, the water distribution system was not part of the manufacturing process and the items in question were consequently not used directly in a manufacturing process.

In addition, the Supreme Court reaffirmed the precedential value of *Kentucky Electric Co. v. Buechel*, 146 Ky., 660, 143 S.W. 58 (1912) and *Covington Gas-Light Co. v. City of Covington*, 84 Ky., 94, 8 K.L.R. 442 (1886) which held that electricity and gas distribution systems were not part of the manufacturing plant for purposes of the ad valorem tax exemption for manufacturing now found in KRS 132.200(4). Because of the common purpose behind this ad valorem tax exemption and the machinery for new and expanded industry sales and use tax exemption, these precedents were applicable here to warrant a holding that the water distribution system was separate from the water company's manufacturing plant facility. On this point, the court further noted that the purpose of any pressurization used in the distribution system was for movement of the water, not manufacturing, and that water treatment plants are regulated by the Public Service Commission and Natural Resources and Environmental Protection Cabinet separately from water distribution systems.

The court also observed that KRC had consistently interpreted the machinery for new and expanded industry exemption as not applying "to pipes, valves, fittings and meters for both water distribution systems and local utilities that deliver gas." Such a longstanding administrative construction should be honored by a reviewing court, the court declared.

In addition, the Supreme Court held that the courts below erred in overturning findings of fact by the KBTA that were supported by substantial evidence. Specifically, the KBTA had found that the purpose of the pressurization of the water in the distribution system was to transport the water and maintain its quality and not manufacturing.

Finally, the court held that the energy exemption did not apply because the water distribution system is not engaged in manufacturing and the distribution system does not constitute one location, as required by KRS 139.480(3).

Camera Center, Inc., d/b/a Murphy's Camera Center, 99-SC-00283, Kentucky Supreme Court

The question in this case is whether machinery purchased by a taxpayer for use in its photo processing operations qualified for the machinery for new and expanded industry sales and use tax exemption. Affirming decisions of the Jefferson Circuit Court and KBTA, the Kentucky Court of Appeals held that the "plant facilities" requirement of the exemption was not met, as the machinery in question was used in locations that were predominantly retail establishments and not plant facilities.

Legal Issues

The Kentucky Supreme Court granted the taxpayer's motion for discretionary review of the Court of Appeals' decision.

Revenue Cabinet v. Humana, Inc., No. 1997-CA-000568-MR, Kentucky Court of Appeals

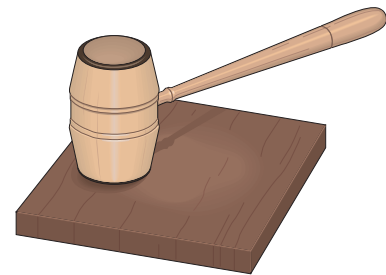
In this case, the taxpayers, for-profit hospitals, challenged KRC's application of the sales and use tax exemptions provided for in KRS 139.472 for prescription medicine and prosthetic devices and physical aids. The taxpayers asserted that these exemptions apply to items of tangible personal property purchased for use in the rendition of professional medical services. KRC disagreed, determining that the requirements of the exemptions prescribed in KRS 139.472(1)(a) and (2) were not met, and assessed tax accordingly.

Affirming decisions of the Franklin Circuit Court and KTBA, the Kentucky Court of Appeals held that KRC was precluded from assessing tax by the doctrine of contemporaneous construction. The court ruled that the exemption statute, KRS 139.472, was ambiguous, which rendered the doctrine applicable. Because KRC had previously permitted the application of KRS 139.472's exemptions to these or similar taxpayers in the past, it could not refuse to do so now.

KRC's motion for discretionary review of the Court of Appeals' opinion has been denied.

USX v. Revenue Cabinet, 95-CI-0490, Franklin Circuit Court

USX Corporation has filed an action in Franklin Circuit Court seeking a judicial determination that the corporation license tax statute KRS 136.071 is unconstitutional as violative of the United States Constitution's commerce, due process, and equal protection clauses, and also various provisions of the Kentucky Constitution. USX seeks an order enjoining KRC from implementing KRS 136.071's provisions allowing corporations with commercial domiciles inside Kentucky (but not those with commercial domiciles outside Kentucky) to exclude, under certain circumstances, their investments in other corporations from the computation of their taxable capital. This case is currently in the pretrial stage.



KRC Administration

KRC Wins National Recognition for Business Recovery Exercise

In January, KRC conducted a business recovery exercise, to better prepare the agency for a possible business disruption extending beyond a three-to-five-day period. As a result of that, in May, the Federal Emergency Management Agency (FEMA) recognized KRC and the Division of Disaster and Emergency Services (DES) by presenting the collaboration with the Exemplary Practices in Emergency Management Exercises Award. Kentucky was selected for this award on the basis of the Terrorism Recovery Exercise. According to Ronn Padgett, executive director of DES, these awards are highly competitive and this was the only one of its type presented.



The exercise was a tabletop exercise, in which decision-making personnel, appointed officials, and key agency staff are presented with a simulated emergency situation. Participants attempt to analyze a scenario and resolve potential problems, leading to constructive recommendations about existing emergency operations plans and procedures. DES disaster recovery planners and analysts assisted in moderating and facilitating the exercise.

The scenario required staff at Perimeter Park to relocate for approximately 30-40 days. An irate taxpayer drove his four-wheel drive pickup truck through the front of the building, causing considerable damage to the Accounts Branch and mail room. Before leaving the building, he spilled a couple of barrels of diesel fuel, contaminating all the mail, and threw a smoke bomb into the computer room. There were no deaths, but employees were injured, and the building suffered extensive damage. The Frankfort Fire Department and Kentucky State Police closed access to the building, an investigation ensued, as did planning and determining KRC needs for returning to business operations.

The exercise was divided into three parts: (1) Scene Assessment; (2) Short Term Recovery; and (3) Long Term Restoration. Eleven other agencies participated, including the Department of Facilities Management; Department of Environmental Protection; Department of Housing, Buildings, and Construction; Department of Treasury; Frankfort Fire Department; Franklin County Fire Department; Kentucky State Police; Department of Information Systems; and Disaster and Emergency Services which facilitated the exercise. An *After-Action Meeting* followed the next week to review comments and other KRC needs for recovery purposes.

The Business Recovery Plan provides direction and strategy for the management of and recovery from a major business interruption adversely affecting the mission of KRC. The objectives of the test were to verify responsibilities of participants and establish what agencies have primary and secondary responsibilities. The test allowed for the documentation and identification of resources, and the length of time required for each response. The exercise also tested KRC's strengths and exposed weaknesses, to bring to light problems that could be better managed in a real situation.

"We are certainly pleased to have received this recognition. It was a good experience for us, and a perfect place to have an exercise such as this. The business functions at P-Park are so vital to the Cabinet, and to state government. The funding for many services and programs are due to tax revenues, which are received and processed there. The most significant finding was realizing the support from other agencies. Other agencies have policies and procedures for assisting agencies recovering from an incident. KRC was able to see the boundaries of its role and responsibilities in a recovery process," said Kathy Gilliland, KRC business recovery coordinator.

KRC Secretary Sarah Jane Schaaf Named to FTA Board

In June, KRC Secretary Sarah Jane Schaaf was appointed to fill an unexpired one-year term on the Federation of Tax Administrators' (FTA) board of trustees.

FTA, a national organization founded in 1937, serves as a source of information and expertise for state tax authorities and administrators. It monitors the workings of state tax agencies and systems as well as issues generally affecting tax policy and administration. The work of FTA is directed and governed by a 15-member board of

trustees composed of tax administrators representing all regions of the country. It is in this capacity that Secretary Schaaf represents Kentucky on the board.



KRC Administration

KRC Administrative Expenditures

KRC administrative expenditures for Fiscal Year 1998-99 totaled \$62,346,470, an increase of 3.25 percent from Fiscal Year 1997-98. KRC's administrative expenditures reflect the cost to continue the Cabinet's day-to-day ongoing operations. The types of appropriated funds that support ongoing operations include General, Road, Restricted, and Federal Funds. Excluded from these administrative costs are *EMPOWER Kentucky* costs for one-time expenditures funded through accounts maintained by the Finance and Administration Cabinet. Also separate from these administrative expenditures are costs incurred in purchasing major equipment from Capital Construction Funds. Those expenditures totaled \$348,847 for KRC's Network Infrastructure Support Project.

Personnel costs represented 66 percent, or \$41,181,633, of the total administrative expenditures for Fiscal Year 1998-99. The average number of full-time permanent employees during Fiscal Year 1998-99 was 984, down one position from the previous year's average of 985. The number of permanent full-time employees on June 30, 1999, was 970. KRC's highest number of permanent

full-time employees during the fiscal year was registered in July 1998 with 1,005 employees. The high number of employees was attributed to KRC converting 37 seasonal employees to full-time permanent employees prior to the beginning of the fiscal year. The conversion of seasonal positions was due to personnel laws passed during the 1998 Regular Session of the General Assembly.

Operating costs for rent, postage, printing, information technology, travel, and other costs rose 6.83 percent, or \$1,350,423. Much of that increase was related to reprogramming of mainframe and PC-based systems to ensure Year 2000 compliance.

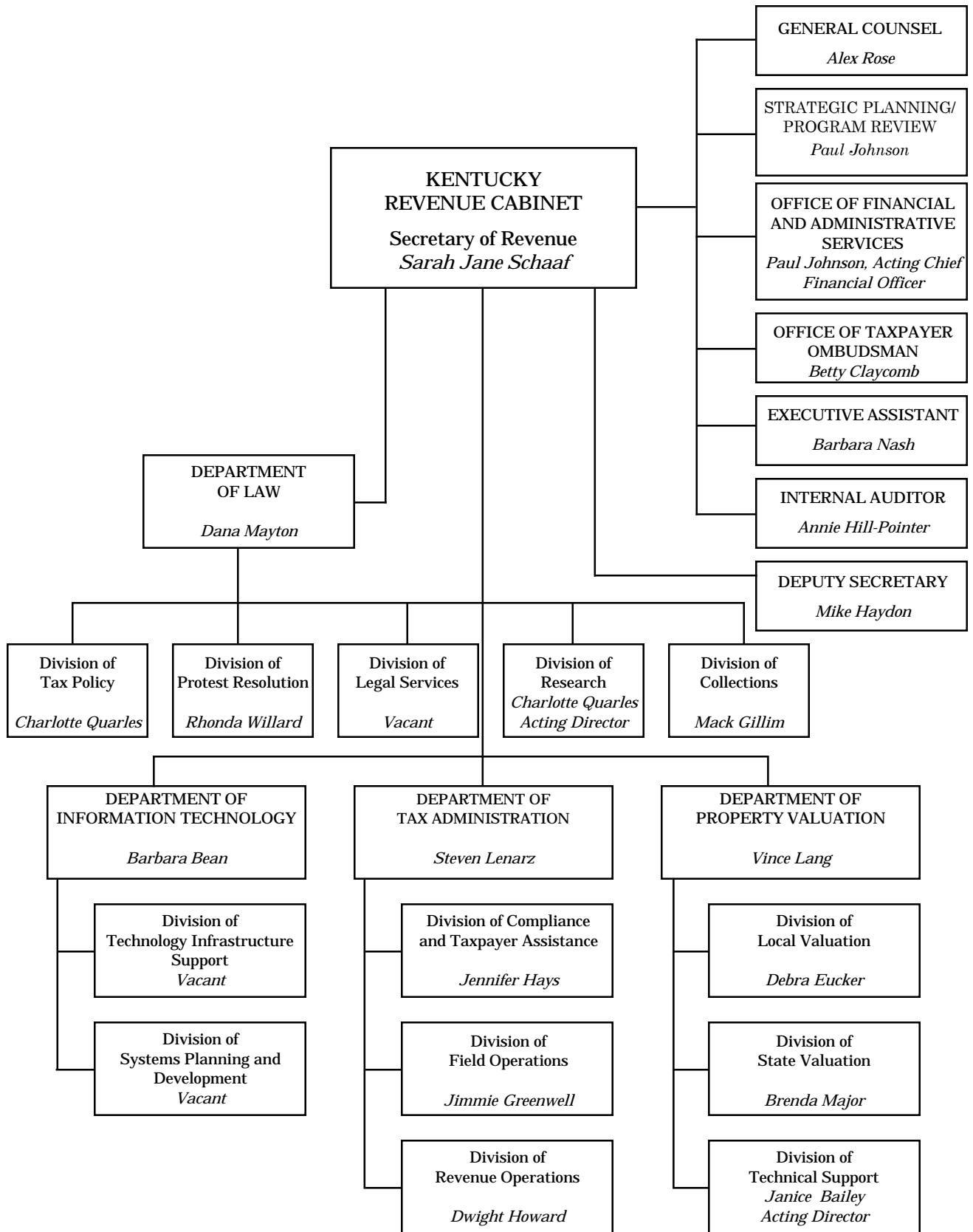
Upon completion of the fiscal year, KRC had a year-end General Fund balance of zero. In addition, all Road and federal funds were spent as appropriated with an ending balance of zero. The only appropriated funds that had a year-end balance were nonlapsing funds from restricted agency accounts. Restricted agency accounts had a year-end appropriation balance of \$121,430 due to a reduction in expenditures from Lien and Filing Fee accounts.

ADMINISTRATIVE COSTS, FISCAL YEAR 1999

(Excluding PVA's, EMPOWER Kentucky and Capital Construction Costs)

	General Fund	Agency Fund	Federal Fund	Road Fund	Total
Salaries full-time	\$ 29,805,301	\$ 913,825	\$ 40,000	\$ 717,000	\$31,476,126
Fringe benefits	7,316,177	0	0	0	7,316,177
Seasonal employees	538,787	0	0	0	538,787
Overtime/block 50s	545,687	0	0	0	545,687
Training and tuition assistance	70,968	0	0	0	70,968
Worker's compensation insurance	138,887	0	0	0	138,887
Unemployment insurance	83,905	0	0	0	83,905
Legal/audit services/consultants	484,086	0	0	0	484,086
Janitorial services	236,591	0	0	0	236,591
Data entry/temporary services	134,849	0	0	0	134,849
Security	155,570	0	0	0	155,570
Total Personnel	\$ 39,510,808	\$ 913,825	\$ 40,000	\$ 717,000	\$41,181,633
Carpool (State Motor Pool)	\$ 31,543	\$ 0	\$ 0	\$ 0	\$ 31,543
Utilities	315,794	7,500	0	0	323,294
Rent/rentals/carpool	2,803,219	65,000	0	55,000	2,923,219
Maintenance and repairs	881,169	0	0	14,000	895,169
Postage	2,499,786	50,000	0	306,000	2,855,786
Printing/other services	1,583,847	409,500	0	20,000	2,013,347
Telecommunications	375,585	134	0	7,646	383,365
Information Technology (includes DIS costs)	6,474,952	1,144,000	0	173,000	7,791,952
Computer equipment	656,340	80,806	0	0	737,146
Supplies	486,906	0	0	0	486,906
Commodities/furniture	336,482	0	0	0	336,482
Software/telephone equipment	348,947	0	0	0	348,947
Travel	1,275,179	0	0	547	1,275,726
Filing/lien/collection fees	2,740	125,805	0	0	128,545
Dues/subscriptions/other	528,860	10,000	0	58,807	597,667
Total Operating	\$ 18,601,349	\$1,892,745	\$ 0	\$ 635,000	\$21,129,094
Computer equipment over \$5,000	35,743	0	0	0	35,743
Total Capital Outlay	\$ 35,743	\$ 0	\$ 0	\$ 0	\$ 35,743
Total Administrative Costs	\$ 58,147,900	\$2,806,570	\$ 40,000	\$1,352,000	\$62,346,470

MANAGEMENT—KENTUCKY REVENUE CABINET
JUNE 30, 1999





J. Bailey



B. Bean



Secretary Sarah Jane Schaaf



B. Claycomb



D. Eucker



M. Gillim



J. Greenwell



M. Haydon



J. Hays



A. Hill-Pointer



D. Howard



P. Johnson



V. Lang



S. Lenarz



B. Major



D. Mayton



B. Nash



C. Quarles



A. Rose



R. Willard

KRC Administration

KRC Management Appointments

On *Aug. 16, 1998*, Dr. James Coffman was given additional duties as the director of the Division of Research.

Coffman has held several technical and administrative positions in his career of more than 20 years with KRC, including seven years as commissioner of the Department of Property Taxation. He previously worked as training director for a mass appraisal and cadastral mapping firm, and as a university teacher. He is also a veteran of the U.S. Air Force.

Coffman holds a bachelor's degree from Eastern Kentucky University, and his master's and doctorate degrees in geography from the University of Wisconsin-Milwaukee. He was serving as director of the Division of Tax Policy at the time the additional duties were assigned to him.

On *Aug. 16, 1998*, Rhonda Willard was appointed director of the Division of Protest Resolution.

Willard was formerly involved with KRC's integrated tax system *EMPOWER Kentucky* initiative, and also served as director of the former Division of Tax Administration. She has also held several auditing and supervisory positions in KRC since beginning her career in July 1978.

She holds a bachelor of science degree in accounting from the University of Kentucky.

On *Jan. 16, 1999*, Vince Lang was appointed commissioner of the Department of Property Valuation. He was previously KRC deputy secretary.

Lang had served as county judge-executive of Hart County for 10 years prior to joining KRC in June 1996. While serving as county judge, Lang held leadership positions with several regional agencies and also served as president and legislative chairman of the Kentucky County Judge-Executives Association.

He holds a bachelor's degree in history from the University of Notre Dame.

On *Jan. 17, 1999*, Mike Haydon was appointed deputy secretary of KRC. He was previously commissioner of the Department of Property Valuation.

Haydon was assistant state treasurer when he joined KRC in April 1996, and has held numerous public service positions, including 17 months as KRC deputy secretary from August 1990 through December 1991.

Haydon is a graduate of Western Kentucky University and is also a veteran of the U.S. Army.

On *Feb. 16, 1999*, Dana Mayton was appointed commissioner of the Department of Law.

Mayton returned to KRC from the Legislative Research Commission (LRC). She served as a staff attorney in KRC's Division of Legal Services and as director of the Division of Compliance and Taxpayer Assistance before taking the LRC position.

Prior to joining KRC, Mayton worked for the Arkansas Legislative Council, that state's equivalent of Kentucky's LRC.

Mayton holds a bachelor of arts degree in criminology from Arkansas State University, and a juris doctorate degree from the University of Arkansas at Little Rock.

On *April 1, 1999*, Alex W. Rose was named KRC's general counsel. He was previously commissioner of the Department of Law.

Rose is a 30-year KRC veteran who began his career as a staff attorney in 1969. He holds a bachelor of arts degree in history and his law degree from the University of Kentucky.

On *May 16, 1999*, Charlotte Quarles was appointed director of the Division of Tax Policy.

Quarles was a tax consultant with KRC's Division of Tax Policy at the time of her appointment. She is a 21-year KRC veteran employee who has worked in the sales tax area as an auditor, audit selection and review officer, section supervisor, and tax consultant.

She holds a bachelor of science degree in accounting from Kentucky State University.

KRC Administration

KRC Departments, Divisions, and Their Duties

The Kentucky Revenue Cabinet consists of 13 divisions, headed by the Office of the Secretary. The divisions are organized into four departments—Information Technology, Law, Property Valuation, and Tax Administration.

Office of the Secretary

The Secretary of the Revenue Cabinet is the agency's top administrative official. The Office of the Secretary is established under Chapter 131 of the Kentucky Revised Statutes. The Secretary of the Revenue Cabinet is authorized under the statute to appoint assistants and personnel as necessary to perform functions of the office.

The Office of the Secretary includes the offices of Financial and Administrative Services, Internal Audit, Strategic Planning/Program Review, and Taxpayer Ombudsman.

The **Financial and Administrative Services** office assists KRC in personnel and fiscal services, and training and development. It provides office supplies and equipment, educational, budget and fiscal, and personnel services for KRC.

The **Internal Audit** office is responsible for auditing the accounting, control, and custodial activities of KRC to ensure compliance with applicable federal and state laws, administrative regulations, policies, and procedures. In addition, the Disclosure Branch, responsible for the disclosure of confidential state and federal information, reports to the Internal Audit office.



The **Strategic Planning/Program Review** office directs and coordinates the long-term planning of KRC and recommends strategies to achieve goals and objectives. The planner also coordinates work of the commissioners with respect to long-term planning and is responsible for guiding plan implementation throughout KRC.

The **Taxpayer Ombudsman** office is responsible for coordinating the resolution of taxpayer complaints and problems if requested by taxpayers or their representatives; recommending publications and education programs to improve voluntary compliance with Kentucky's tax laws; and otherwise ensuring the rights of taxpayers under KRS 131.041-131.081, the Kentucky Taxpayers' Bill of Rights.

Department of Information Technology

The Department of Information Technology consists of two divisions, the Division of Technology Infrastructure

Support and the Division of Systems Planning and Development. It provides strategic planning for the development of information resource policies and offers overall support for information technologies available within KRC. The focus is on efficient delivery of information services in support of KRC's mission and objectives.

The **Division of Systems Planning and Development** is responsible for application development support services, including electronic commerce, Web development, and end-user support and production control.



The **Division of Technology Infrastructure Support** provides network support services, Cabinet technology procurement support, and computer operations support.

Department of Law

The Department of Law administers KRC's collection efforts, communication efforts, tax policy, and legal services; settles protested issues; and performs tax research studies. It consists of the Division of Collections, the Division of Legal Services, the Division of Protest Resolution, the Division of Research, and the Division of Tax Policy, as well as the Public Information and Communication Services Branch, which is attached to the commissioner's office.

The **Division of Collections** is responsible for the collection of delinquent taxes and the administration of collection-related compliance programs including Voluntary Disclosure and Offers in Settlement. The division is also responsible for administering the Criminal Referral Program.

The **Division of Legal Services** represents KRC in administrative proceedings before the Kentucky Board of Tax Appeals and Board of Claims and in legal actions involving tax and a variety of other issues at every level of the state and federal court system. The division also performs a wide range of other services and functions which include rendering advice and written legal opinions concerning the state's tax laws to KRC personnel, other state government personnel, and taxpayers; reviewing and drafting proposed statutes and regulations; analyzing tax laws and assisting with their implementation and administration; assisting with the preparation of KRC informational publications; and providing assistance and advice in connection with audits, protest conferences, and other stages of the enforcement and administration of the tax laws.

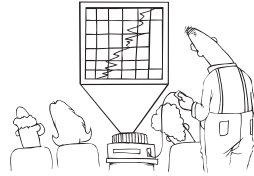
The **Division of Protest Resolution** reviews and bills tax audits performed by the audit staffs of KRC's 11

KRC Administration

taxpayer service centers. The division is responsible for responding to and resolving taxpayers' protests of the field audit adjustments and resulting tax assessments. In resolving protests, the division conducts conferences and issues final rulings upon request or whenever deemed necessary. The division is also required to resolve protests of office audits conducted by other taxing sections within KRC.



The **Division of Research** is responsible for providing analyses of tax-related issues and fiscal impact studies of legislative proposals, administrative changes, and court decisions; gathering and maintaining data for the Office of Financial Management and Economic Analysis to assist in revenue forecasting; performing internal studies of administrative practices and procedures to improve efficiency of tax administration; responding to external requests for tax-related information or analysis; and assisting in the design of tax forms, returns, and related instructions.



The **Division of Tax Policy** is responsible for providing oral and written technical advice on Kentucky tax law; drafting proposed tax legislation and regulations; testifying before legislative committees on tax matters; analyzing tax legislation; reviewing and revising tax returns and forms; drafting and reviewing articles and publications; reviewing and approving final ruling letters; providing expert witnesses in tax litigation; providing consultation and assistance in protested tax cases; and conducting training and education programs.

The **Public Information and Communication Services Branch** is responsible for KRC publications, forms, media/public relations, printing, and the Online Taxpayer Service Center Internet site.

Department of Tax Administration

The Department of Tax Administration administers KRC's taxpayer assistance, general tax administration, field operations, and tax processing efforts. It consists of the Division of Compliance and Taxpayer Assistance, the Division of Field Operations, and the Division of Revenue Operations.

The **Division of Compliance and Taxpayer Assistance** is responsible for providing taxpayer assistance, administering taxes levied under the Kentucky



Revised Statutes, managing compliance programs, and conducting office audits.

The **Division of Field Operations** is responsible for providing quality taxpayer service from the 11 taxpayer service centers. The centers provide taxpayer assistance and education, prepare returns, distribute forms, collect delinquent taxes, and perform field audits. The division also provides instructors, develops training materials, and coordinates training for most in-house tax schools.

The **Division of Revenue Operations** is responsible for receiving and processing revenues for deposit into the state treasury, registering firms for business taxes, processing tax returns, and making additional assessments or refunds. This division also has responsibility for records management.

Department of Property Valuation

The Department of Property Valuation administers all property taxation matters. It is composed of the Division of Local Valuation, the Division of State Valuation, and the Division of Technical Support.

The **Division of Local Valuation** is responsible for certifying property valuations submitted by property valuation administrators (PVAs), coordinating property tax collection, and providing technical and administrative support to PVAs, county clerks, sheriffs, county attorneys, and local taxing districts.



The **Division of State Valuation** is responsible for overseeing the assessment of intangible and tangible personal property, motor vehicles, public service company property, and omitted personal property.

The **Division of Technical Support** is responsible for providing assistance to the 120 PVAs in the areas of mapping projects, mineral valuation and compliance, and computer technology.



TAXES ADMINISTERED BY THE REVENUE CABINET (In Effect as of June 30, 1999)

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 user 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.
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 acquirers. The tax is paid by purchasing stamps within 48 hours after cigarettes are received by a resident wholesaler. A nonresident wholesaler must affix the tax stamps prior to importing them into Kentucky.
Coal 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.

TAXES ADMINISTERED BY THE REVENUE CABINET (In Effect as of June 30, 1999)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
<p>Corporation Income Tax</p>	<p>KRS 141.010 et seq., 155.170</p>	<p>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</p>	<p>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.</p> <p>An "electing small business corporation," (S Corporation) as defined in Section 1371(b) 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."</p> <p>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 141.120 prohibits affiliated groups from filing a combined Kentucky corporation income tax return using the unitary business concept.</p>
<p>Corporation License Tax</p>	<p>KRS 136.070 et seq.</p>	<p>\$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.</p>	<p>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 corporations exempt from income tax (except S corporations) are also exempt from license tax.</p> <p>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.</p>
<p>Distilled Spirits Case Sales Tax</p>	<p>KRS 243.710</p>	<p>5 cents per case.</p>	<p>Excise tax on distilled spirits sold by wholesalers to retailers in Kentucky.</p>
<p>Distilled Spirits and Wine Consumer Taxes</p>	<p>KRS 243.720 et seq.</p>	<p>Distilled spirits containing over 6 percent alcohol by volume per gallon \$ 1.92 per liter 0.5073 Distilled spirits containing 6 percent or less alcohol by volume per gallon \$ 0.25 per liter 0.0661 Wine per gallon \$ 0.50 per liter 0.1321 (Proportionate amount charged on smaller quantities, but not less than 4 cents on any retail container of wine.)</p>	<p>Excise tax imposed upon the use, sale or distribution by sale or gift of distilled spirits and wine. There are statutory exemptions.</p>

TAXES ADMINISTERED BY THE REVENUE CABINET (In Effect as of June 30, 1999)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
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, HMO services (excluding premium receipts) and ICF/MR services. 1998-1999: One-half of one percent (0.5%) of gross receipts for physician services. 15 cents per outpatient prescription.	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 trusts not distributed or distributable to beneficiaries.
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 136.330 to 136.390, 299.530, 304.3-270, 304.4-030	All insurance except domestic life 2 percent 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.

TAXES ADMINISTERED BY THE REVENUE CABINET (In Effect as of June 30, 1999)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
Marijuana and Controlled Substance Tax	KRS 138.870	\$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. Law enforcement agencies must notify the Revenue Cabinet of seizure of product not bearing tax stamp.
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 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 and/or location of purchase. 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.

TAXES ADMINISTERED BY THE REVENUE CABINET (In Effect as of June 30, 1999)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
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).	<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, tar sands 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>
Oil Production Tax	KRS 137.120 et seq.	4.5 percent of market value of crude petroleum produced in Kentucky.	<p>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.</p> <p>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.</p>
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), 32.200(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.
Annuitants or Rights to Receive Income	KRS 132.215(2)	0.1 cent (per \$100 of assessment).	State rate only.

TAXES ADMINISTERED BY THE REVENUE CABINET (In Effect as of June 30, 1999)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
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 136.120(4), 136.180(3)	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)	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.
Goods Held for Sale in the Regular Course of Business	KRS 132.020(10)	5 cents (per \$100 of assessment).	Subject to local rates.
Intangibles Money in hand, notes, bonds, accounts and other credits, except those arising from out-of-state business, and other not specified elsewhere. Accounts receivable, notes, bonds, credits, nondomestic bank deposits and other intangibles arising from out-of-state business, patents and copyrights, and tobacco base allotments.	KRS 132.020(1), 136.120(1) KRS 132.020(2), 132.120(2)	25 cents (per \$100 of assessment). 1.5 cents (per \$100 of assessment).	State rate only. State rate only.

TAXES ADMINISTERED BY THE REVENUE CABINET (In Effect as of June 30, 1999)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
Leasehold Interest (Owned by tax-exempt governmental unit)	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	70 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.
Manufacturing Machinery	KRS 132.020(1), 132.200(4)	15 cents (per \$100 of assessment).	State rate only.
Margin Accounts (See Brokers' Accounts Receivable)	KRS 132.060	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	KRS 132.020(10) KRS 132.095	5 cents (per \$100 of assessment). 0.1 cent (per \$100 of assessment).	Full local rates. May be subject to local taxation.

TAXES ADMINISTERED BY THE REVENUE CABINET (In Effect as of June 30, 1999)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
Radio, Television and Telephonic Equipment	KRS 132.020(1), 132.200(5)	15 cents (per \$100 of assessment).	Full local rates.
Railroads (Intrastate)	KRS 132.020(11)	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 16.7 cents for 1995, 16.3 cents for 1996, 15.7 cents for 1997, 15.3 cents for 1998 and 14.8 cents for 1999.	Full local rates.
Recreational Vehicles	KRS 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 136.300(1)	10 cents (per \$100 of assessment).	State rate only.
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 136.183	Subject to annual adjustment.	Local tax collected and distributed by the Revenue Cabinet effective January 1, 1993.

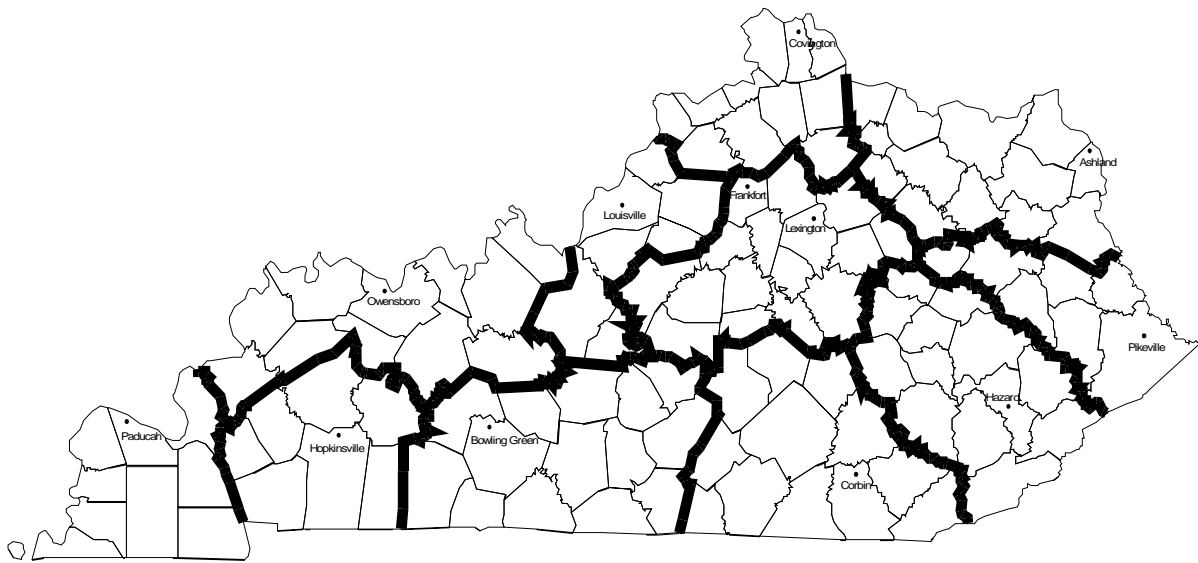
TAXES ADMINISTERED BY THE REVENUE CABINET (In Effect as of June 30, 1999)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
Unmined Coal	KRS 132.020(5)	Real estate rate: 16.7 cents for 1995, 16.3 cents for 1996, 15.7 cents for 1997, 15.3 cents for 1998 and 14.8 cents for 1999.	Full local rates.
Watercraft Commercial Individual	KRS 136.181 KRS 132.020(1), 132.488	45 cents (per \$100 of assessment). 45 cents (per \$100 of assessment).	Full local rates. Full local rates.
Public Service Commission Assessment	KRS 278.130 et seq.	Maximum assessment 1.667 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.	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. Average Daily Mutuel Handle (for preceding year) \$ 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.
(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.

TAXES ADMINISTERED BY THE REVENUE CABINET (In Effect as of June 30, 1999)

TAX	LEGAL REFERENCE	STATE RATE	DESCRIPTION
<p>Racing Taxes: (continued) (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.</p> <p>There are statutory exemptions.</p>
<p>Waste Tire Fee</p>	<p>KRS 224.2613</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>

KENTUCKY TAXPAYER SERVICE CENTERS



• Taxpayer Service Center

— District Boundary

Ashland, 41105-0687

P.O. Box 687
134 Sixteenth Street
Telephone: (606) 920-2037
Fax: (606) 920-2039

Bowling Green, 42102-2040

P.O. Box 2040
1502 Westen Street
Telephone: (270) 746-7470
Fax: (270) 746-7847

Corbin, 40702-3298

P.O. Box 1298
Falls Road Plaza, Suite 5
1707 18th Street
Telephone: (606) 528-3322
Fax: (606) 523-1972

Frankfort, 40620

200 Fair Oaks Lane, Second Floor
Individual Income Tax Branch
Telephone: (502) 564-4581
Fax: (502) 564-3685

Hazard, 41702-4194

P.O. Box 419
233 Birch Street
Telephone: (606) 435-6017
Fax: (606) 435-6018

Hopkinsville, 42241-0695

P.O. Box 695
105 Hammond Plaza
4011 Ft. Campbell Blvd.
Telephone: (270) 889-6521
Fax: (270) 889-6563

Lexington, 40507-1556

301 East Main Street
Suite 500
Telephone: (606) 246-2165
Fax: (606) 246-2164

Louisville, 40202-2446

620 South Third Street
Suite 102
Telephone: (502) 595-4512
Fax: (502) 595-4205

Northern Kentucky, 41042-1385

Turfway Ridge Office Park
7310 Turfway Rd., Suite 190
Florence
Telephone: (606) 371-9049
Fax: (606) 371-9154

Owensboro, 42302-0128

P.O. Box 128
401 Frederica Street
Building C, Suite 201
Telephone: (270) 687-7301
Fax: (270) 687-7244

Paducah, 42002-2336

P.O. Box 2336
555 Jefferson Street, Suites 302/306
Telephone: (270) 575-7148
Fax: (270) 575-7027

Pikeville, 41501-2913

Uniplex Center, 126 Trivette Drive
Suite 203
Telephone: (606) 433-7675
Fax: (606) 433-7679