REVENUE

The Kentucky Department of Revenue presented the following information at the Tax Executive Institute annual meeting on April 24, 2019. This joint meeting with the Internal Revenue Service covered recent administrative changes at the Department of Revenue as well as a summary of legislation passed during the 2019 General Assembly.

The information in this presentation was prepared from information the Department of Revenue possessed and believed to be accurate and relevant on the date of the meeting. This information does not constitute a final ruling, order, or determination of the Department of Revenue and cannot be appealed.

2019 Kentucky Tax Changes

Tax Executives Institute

April 24, 2019

Kentucky Department of Revenue • 501 High Street • Frankfort, KY 40601 • (502) 564-3226

Introductions

- **Daniel P. Bork** — Commissioner, Kentucky Department of Revenue
- **Jessica S. Honican, CPA** — Director, Division of Corporation Tax, KDOR
- **Christy Kinney** — Director, Division of Individual Income Tax, KDOR
- **Richard Dobson** — Executive Director, Office of Sales and Excise Taxes, KDOR
- **Tiffany Adair** — Tax Policy Research Consultant, Office of Tax Policy and Regulation, KDOR

Overview of the 2019 Session

- Continued Tax Reform
  - Tax Repeal and Replacement
  - Other Reforms
- Modifications to HB 487 from 2018
  - Restoration of Certain Provisions
  - Enhancements
- Administrative Efficiency
  - Providing Clarity
  - Tax Administration
  - Tax Fairness

Agenda

- Corporation Tax
- Tax Credits
- Individual Income Tax
- Sales Tax
- Published Guidance & Upcoming Regulations

Corporation & Pass-through Entity Changes

- **2019 estimated tax rules and penalties changed to generally follow federal for *corporations* and *pass-through entities***
  - **New 1st quarter installment requirement due April 15, 2019**
  - **Four installments at 25% of the estimated tax due each**
    - **April 15, June 15, September 15, December 15**
  - **Allow Annualization and Adjusted Seasonal Installment Methods**
  - **Declaration Penalty replaced with "Addition to Tax" Penalty**
  - **See 2019 720ES Instructions**
  - KY-TAM-19-02

Corporation & Pass-through Entity Changes

- 2019 IRC reference date updated to 12/31/18
- C-corporation extensions allowed for 7 months
  - For tax years ended on or after June 27, 2019
  - Same Form 720EXT
- IRC §179 expense deduction increased to $100,000 for Kentucky in 2020
  - Property placed into service 9/10/01 - 12/31/19
    - Use 12/31/01 IRC ($25,000 § 179 max)
  - Property placed into service on or after 1/1/20
    - Use 12/31/03 IRC ($100,000 § 179 max)

Corporation & Pass-through Entity Changes

- **Bank Franchise Tax repealed and replaced with Corporation Income Tax and LLET effective 2021**
  - Applies to banks, savings and loan associations, and other financial institutions doing business in Kentucky
  - Short year returns required for bank franchise tax and subsequent corporation income and LLET returns for fiscal year filers
    - Cut off is December 31, 2020
- **New Deferred Tax Deduction**
  - Allows publicly traded corporations to offset the effects of combined reporting tax changes for financial statement reporting purposes beginning in 2024
  - See Schedule DTD (due July 1, 2019)
  - Additional info found in KY-RP-19-02
- **Clarity provided for $175 minimum LLET**
- **If a pass-through entity is billed for LLET, shareholders, partners or members are allowed the greater of the ordinary statute of limitations or 180 days from the date an assessment is final to file amended returns**

Corporation Group Filing Changes

- Unitary Filing Changes
  - 50% voting stock ownership requirement
  - "Tax haven" definition excludes countries with a comprehensive income tax treaty with the U.S.
  - Waters-edge clarified in statute
  - Intercompany eliminations required for combined income and gross receipts
  - NOLs may be shared in a unitary group; tax credits *cannot* be shared
  - U.S. Domestic members with >80% income from foreign sources excluded from group
    - Does not negate filing requirement if such corporation has Kentucky nexus
  - Non-U.S. members with >20% intangible income from other group members excluded if located in a treaty country
- Elective Consolidated Filing Change
  - Election period now 4 years instead of 8 years

Corporation Unitary Group NOL

- **Unitary Group NOL Sharing**
  - **Kentucky Net Operating Loss (KNOL) incurred by a taxpayer member prior to inclusion in a unitary combined group may be deducted from the apportioned income of:**
    - **That taxpayer member which originally incurred the KNOL ***
    - **Another taxpayer member, *but in no case shall the deduction reduce any taxpayer member's Kentucky apportioned taxable income by more than 50% in any taxable year***
  - **KNOL incurred by a taxpayer member while included in a unitary combined group may be deducted from the apportioned income of:**
    - **That taxpayer member which originally incurred the KNOL***
    - **Another taxpayer member that was a taxpayer member in the same combined group in the year in which the KNOL was originally incurred ***

*** No limitations aside from IRC Section 172 and KRS 141.011**

Corporation Unitary Group NOL

- All KNOL are subject to the limits specified in IRC Section 172 and KRS 141.011
- If the taxable income results in a net loss for a taxpayer member of the combined group, that taxpayer member has a KNOL
- No prior year KNOL carryforward shall be available to entities that were not doing business in Kentucky in the year in which the loss was incurred
- Any amount of NOL carryover that is deducted by another taxpayer member of the combined group shall reduce the amount of net operating loss carryover that may be carried over by the taxpayer member that originally incurred the loss.
- Guidance and amendments to 103 KAR 16:250 will be forthcoming

Tax Credit Changes

- **Enhancements to *major* recycling credit program**
  - **400 employees at the project location (previously 750)**
  - **Credit for 25% of the installed cost of the equipment (previously 50%)**
  - **30 year life (previously 10)**
  - **Credit may offset up to 75% of each tax liability for all years available (previously 50%)**
- **Annual *regular* recycling credit limitation clarified in statute**
  - **1st year, limited to offset lesser of 10% of the allowable tax credit or 25% of the tax liability**
  - **All subsequent years, limited to offset up to 25% of the tax liability**
- **Farmer Small Business Tax Credit**
  - **Expansion of the Small Business Tax Credit to Farmers (SB 246)**
  - **Shares $3 million FY cap with the Small Business Tax Credit**
- **Inventory Tax Credit**
  - **Rental heavy equipment now subject to ad valorem tax and thus eligible for the inventory tax credit**
- **Corrections to sunset dates for economic development credits**

Individual Changes – Estimated Payments

- **2019 estimated tax rules and penalties changed to generally follow federal for *individuals***
  - **Four installments at 25% of the estimated tax due each**
    - **April 15, June 15, September 15, January 15 of the following tax year**
  - **Allow Annualized Income Installments**
  - **Declaration Penalty replaced with "Addition to Tax" Penalty**
  - **See 2019 740-ES Instructions**
  - KY-TAM-19-02

Individual Changes

- 2019 IRC reference date updated to 12/31/18
- Tax Year 2019 Changes:
  - Itemized Deductions on Schedule A restored
    - Investment interest deduction under IRC Section 163
    - Gambling loss deduction under IRC Section 165(d)
  - "Active duty" military definition expanded to include training
  - New Kentucky YMCA Youth Assembly tax refund designation check-off
- IRC §179 expense deduction increased to $100,000 for Kentucky in 2020
  - Property placed into service 9/10/01 - 12/31/19
    - Use 12/31/01 IRC ($25,000 § 179 max)
  - Property placed into service on or after 1/1/20
    - Use 12/31/03 IRC ($100,000 § 179 max)

Individual Changes – Family Size Tax Credit

- **Tax Years 2019-2020:**
  - **Enhanced Family Size Tax Credit due to tax bracket changes**

Poverty Range	Family Size One	Family Size Two	Family Size Three
100-104%	$11	$7	$3
104-108%	$20	$13	$6
108-112%	$29	$18	$6
112-116%	$37	$22	$6
116-120%	$45	$24	$4
120-124%	$51	$26	$0
124-127%	$58	$27	$0
127-130%	$64	$28	$0
130-133%	$69	$28	$0

Emergency Provisions

Governor Bevin's March 26th signing of HB 354 had immediate impact on the application of sales tax to nonprofit sales.

Due to an emergency clause in this legislation, **sales of admissions and tangible property sales at fundraising events by all nonprofit groups and governmental organizations are now exempt from sales tax for transactions on or after March 26, 2019**.

These nonprofit, governmental, and civic organizations will no longer charge sales tax on these types of transactions as specified in Sections 28-29 of HB 354.

All of these **nonprofit organizations** should discontinue charging sales tax to their customers and benefactors immediately.

Please note that this new exemption does not apply to sales by retail businesses such as bookstores and thrift stores owned or operated by nonprofit or governmental groups.

Administrative Changes – effective July 1, 2019

- **Resale –** Provision added for taxable services enacted under HB 487.
- **Direct pay authorization –** Permits accrual of tax on purchases of newly taxable services by permit holders.
- **Poultry –** Added to the exclusion from small animal veterinary services subject to sales tax.
- **Wholesale tax on small farm wineries –** Clarifies the exclusion from the wholesale sales tax applies to the first 50,000 gallons of annual production.

Additional Exemptions – effective July 1, 2019

- **Fishing tournaments & boat ramp fees –** Excluded from the definition of admissions subject to sales tax.
- **Extended warranty services –** Does not include service contracts sold to small telephone utilities or to Tier III CMRS providers.

Additional Exemptions – effective July 1, 2019

- **de Minimis sales standard -** Exclusion from sales tax liability for certain small service providers that are only in the business of selling services that became taxable under HB 487 (landscaping services, janitorial services, small animal veterinary services, pet care services, industrial laundry and linen supply services, non-coin-operated laundry and dry cleaning, indoor tanning services, non-medical diet and weight reducing services, limousine services w/ a driver and extended warranty services). Sellers with less than $6,000 in gross receipts from sales of these services annually are not liable for sales tax and do not need to register for a sales tax account number. However, once a provider exclusively selling these services exceeds the $6,000 threshold in any calendar year, that seller is then liable for the 6% tax on all further sales of those services during the year as any other retailer. Once exceeded, the threshold does not reset for the next calendar year.

Reporting Qualifications

- **Marketplace Providers –** Requires these online sales platforms to collect and remit KY sales and use tax on transactions they facilitate for sales into the Commonwealth from third party sellers. Collection requirements apply based upon the economic nexus standard of more than $100,000 in gross receipts or 200 or more transactions from sales into KY annually. This threshold is the same as adopted in 2018 for remote retailers in HB 487 post *Wayfair*. Effective July 1, 2019.
- **Toller qualification for Energy Direct Pay –** Reverses the exclusion in HB 487 for tolling operations at KY plant facilities and establishes objective criteria to determine whether such operations are eligible for the partial EDP sales tax exemption for energy purchases.

Base Preservation

Video streaming services - HB 354 defines these services under the category of "multi-channel programming services" as "*programming that streams live events, movies, syndicated and television programming, or other audio-visual content over the Internet for viewing on a television or other electronic device with or without regard to a particular viewing schedule*."

Video streaming services provided to Kentucky customers are subject to the 3% excise tax (KRS 136.604) and the 2.4% gross revenues tax (KRS 136.616), collectively KY telecommunications taxes, as well as the utility gross receipts license tax (school tax) imposed at a local school district rate not to exceed 3% (KRS 160.614) billed on or after July 1, 2019.

Property Tax Changes

- New exemption for tangible personal property return filing
  - Less than $1,000 in property
  - Must keep property records

- Reclassification of heavy equipment rental inventory
  - Only NAICS codes 532310 and 532412
  - Eligible for inventory tax credit

- 60-day protest period for tangible personal property bills

Administrative Changes

- Certain TVA-in-lieu-of payment administrative functions returned to the Department of Revenue

- Department of Revenue personnel are exempt from criminal or civil liabilities for court-ordered information releases

- Taxpayer documents excluded from open records law

Administrative Regulation Process

- Department of Revenue has been collaborating with the KYCPA and the Kentucky Chamber of Commerce

- 60 income tax regulations have been reviewed
  - 20 were repealed
  - 6 regulations will be amended due to legislative changes
  - 1 new regulation will be promulgated for combined reporting

- All other regulations are in the process of being reviewed

- Department of Revenue welcomes feedback on regulations which should be sent through the KYCPA

- Administrative regulation process was modified by HB 4, which included increasing the public comment period from 30 days to 90 days

2019 TEI Kentucky State Tax Update

Daniel P. Bork, Commissioner

Kentucky Department of Revenue

✉ dan.bork@ky.gov

☎ (502) 564-3226

Jessica Honican, CPA

Director, Division of Corporation Tax

✉ jessicas.honican@ky.gov

☎ (502)564-7268

Christy Kinney

Director, Division of Individual Tax

✉ christy.kinney@ky.gov

☎ (502) 564-7538

Richard Dobson

Executive Director, Office of Sales & Excise Taxes

✉ richard.dobson@ky.gov

☎ (502) 564-5523

Tiffany Adair

Office of Tax Policy & Regulation

✉ tiffany.adair@ky.gov

☎ (502) 564-0926

Kentucky Department of Revenue

501 High Street • Frankfort, KY 40601

Disclaimer

The information in this presentation is for educational and informational purposes only and does not constitute legal advice. Information is presented as an overall review that is subject to law changes and may not apply to all states. For accurate information on issues related to the 2019 tax changes in Kentucky, please reference HB 354, HB 458, and SB 249 from the 2019 regular session of the Kentucky General Assembly.

Information in this presentation is believed to be accurate as of the date of publication. In the event that any information in this presentation is later determined to be in error, this presentation cannot be used by taxpayers in supporting a specific position or issue before the Department of Revenue, as it does not have the statutory or regulatory authority.

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