# SALES AND USE TAX

## Background

Kentucky’s first entry into the sales tax field occurred in 1934 when the General Assembly enacted a tax of 3 percent on general retail gross receipts. The tax was subsequently repealed by the 1936 General Assembly.

Kentucky again enacted a sales and use tax effective on July 1, 1960. The sales tax is imposed upon all retailers for the privilege of making retail sales in Kentucky. The retailer must pass the tax along to the consumer as a separate charge. The use tax is imposed on the storage, use, or other consumption of tangible personal property in Kentucky. Tangible personal property, the sale of which is subject to Kentucky sales tax, is not subject to the use tax.

From its inception in 1960 until 1986, the sales and use tax was the most productive tax in the General Fund. In 1986, it was surpassed by the individual income tax and continues to be the second most productive today. Receipts for FY03 totaled $2,364.2 million, which was a growth of 2.8 percent over the prior year. This tax represented 34.9 percent of total General Fund tax receipts in FY03.

## Current Rate Structure

Sales and use taxes are imposed at the rate of 6 percent of gross receipts or purchase price.

## Tax Base

The tax base for the sales tax is gross receipts derived from both retail sales of tangible personal property and sales of certain services to the final consumer in Kentucky. Retail sales are defined as any sales other than sales for resale. The lease and rental of tangible personal property for a consideration is considered a sale or purchase, the receipts of which are subject to the sales and use tax.

The tax base for the use tax is the purchase price of tangible personal property purchased for storage, use, or other consumption in Kentucky. The use tax is a “back stop” for sales tax and generally applies to property purchased outside the state for storage, use, or consumption within the state.
purchaser’s liability for the use tax is not extinguished until the tax has been paid to the state, either by the purchaser or by the retailer from whom the property was purchased. However, the purchaser will not be held liable for the tax provided a receipt is obtained from a retailer engaged in business in this state, or from a retailer authorized to collect Kentucky use tax, showing that the tax was collected by the retailer as a separately stated charge and the receipt is maintained in the purchaser’s files.

**Taxable Unit**

The sales tax is imposed on gross receipts from the sale, lease, or rental price of retail sales of tangible personal property and certain services in Kentucky. The use tax is imposed on the storage, use, or other consumption of tangible personal property in Kentucky, measured by the purchase price.

**Tax Due**

The tax must normally be reported and remitted on a monthly basis. In some cases, the taxpayer may be permitted to file on a quarterly or annual basis. For most taxpayers, the tax return and payment of the tax liability are due on the twentieth day of the month following the close of the tax period. Large taxpayers must file monthly returns and include an estimate of the first fifteen days of the following calendar month. The return is due on the twenty-fifth day following the close of the calendar period. The Revenue Cabinet notifies taxpayers required to file on this alternate basis of their obligation.

**Tax Expenditures Enacted During Fiscal Years 2002-2003**

The following changes were enacted by the 2002 General Assembly:

**Expanded Application of Tourism Tax Credits** – This change expands the availability of tourism tax credits to include large lodging renovations or construction, and removes the sunset date, which was June 30, 2002. *HB 372*

The following changes were enacted by the 2003 General Assembly:
Streamlined Sales Tax Project – Kentucky’s sales tax laws were aligned with those of a significant number of other states, so these states can pursue sales tax collection from out-of-state vendors. Several of Kentucky’s definitions of taxable items required amending. These provisions take effect July 1, 2004.  

*HB 293*

Exemption of repair parts for large trucks – Repair parts for trucks and their towed units over 44,001 pounds that are used exclusively in interstate commerce are exempt from the sales tax, for purchases on or after January 1, 2004. *HB 293*

### Table 15. Total Sales And Use Tax Expenditures

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Tax Expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>$2,269.7 million</td>
</tr>
<tr>
<td>2005</td>
<td>$2,320.8 million</td>
</tr>
<tr>
<td>2006</td>
<td>$2,381.3 million</td>
</tr>
</tbody>
</table>

The total sales and use tax exemptions do not include the cost of excluding services from the sales tax. These sales were never included in the tax base, are generally not part of most states’ sales tax base and therefore do not meet the technical qualifications of a tax expenditure. We have continued to estimate the amount of lost revenue from excluding certain services from the tax and have listed these on pages 110-112 in the back of this section. They are not considered tax expenditures for the purpose of this publication.
Tax Expenditures

1. Food Items

*Kentucky Revised Statute 139.485, effective 1972, revised 1986*

Food for human consumption is exempt from sales and use tax. The exemption does not apply to meals served in restaurants, to meals served on or off the premises, or to meals sold on a “take out” or “to go” basis. This exemption does include purchases made with food stamps.

- FY2004 .................................... $414.6 million
- FY2005 .................................... $427.0 million
- FY2006 .................................... $439.8 million

Baked goods prepared by the seller and sold without eating utensils are exempt from sales tax. This exemption becomes effective July 1, 2004.

- FY2004 .................................... $-0-
- FY2005 .................................... $4.1 million
- FY2006 .................................... $4.1 million

2. Non-profit Educational, Charitable and Religious Institutions

*Kentucky Revised Statute 139.495, effective 1976*

Sales to resident, nonprofit educational, charitable, and religious institutions qualified for exemption from federal income taxation under Section 501(c)(3) of the Internal Revenue Code, for use solely within their exempt function, are exempt.

- FY2004 .................................... $140.5 million
- FY2005 .................................... $144.7 million
- FY2006 .................................... $149.0 million
3. **Labor or Services Used in Property Sold**  
*Kentucky Revised Statute 139.050(3)(c), effective 1960*

A separately stated price received for labor or services used in installing or applying property sold is exempt from sales and use tax.

- FY2004 ......................... $171.1 million
- FY2005 ......................... $176.2 million
- FY2006 ......................... $181.5 million

4. **Residential Utilities**  
*Kentucky Revised Statute 139.470(8), effective 1979*

Sales of electricity, sewer services, water, and fuel to Kentucky residents for use in heating, cooking, lighting, and other residential uses are exempt from sales and use tax.

- FY2004 ......................... $134.4 million
- FY2005 ......................... $138.4 million
- FY2006 ......................... $142.6 million

5. **Prescription Medicine, Prosthetic Devises and Physical Aids**  
*Kentucky Revised Statute 139.472, effective 1971*

Prescription medicine, prosthetic devices, and physical aids are exempt from sales and use tax. Prosthetic devices include artificial limbs, artificial eyes, hearing aids, crutches, and wheelchairs.

- FY2004 ......................... $244.0 million
- FY2005 ......................... $251.3 million
- FY2006 ......................... $258.8 million
6. Machinery for New and Expanded Industry and Certain Industrial Machinery

*Kentucky Revised Statute 139.170 and 139.480(10), effective 1960*

Machinery for new and expanded industry that is used directly in manufacturing or processing and is incorporated for the first time into plant facilities in this state, and does not replace machinery in such plant, is exempt.

*Kentucky Revised Statute 139.487, effective 1982*

Industrial machinery manufactured in Kentucky is exempt from sales tax when the industrial machinery is delivered to a manufacturer or processor or their agent for use out-of-state.

- FY2004 ....................................$67.5 million
- FY2005 ....................................$68.8 million
- FY2006 ....................................$70.2 million

7. Coal Used in the Manufacture of Electricity

*Kentucky Revised Statute 139.480(2), effective 1960*

Coal used in the manufacturing of electricity is exempt.

- FY2004 ....................................$55.0 million
- FY2005 ....................................$57.1 million
- FY2006 ....................................$59.2 million

8. Energy and Energy Producing Fuels

*Kentucky Revised Statute 139.480(3), effective 1960*

Energy and energy producing fuels used in manufacturing, processing, mining, or refining, to the extent that the cost of the energy or energy producing fuels used exceeds 3 percent of the cost of production, are exempt.

- FY2004 ....................................$55.5 million
- FY2005 ....................................$56.2 million
- FY2006 ....................................$56.9 million
9. **Retailers’ Compensation for Collecting and Remitting the Tax**

*Kentucky Revised Statute 139.570, effective 1960*

As reimbursement for the cost of collecting and remitting tax, the taxpayer shall deduct 1.75 percent of the first $1,000 of tax due and 1 percent of the tax due in excess of $1,000 if the amount due is not delinquent at the time of payment.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Compensation Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$11.2 million*</td>
</tr>
<tr>
<td>FY2005</td>
<td>$18.3 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$18.6 million</td>
</tr>
</tbody>
</table>

Note: FY04 compensation is reduced by FY03-FY04 Budget Bill, HB 269.

10. **Enterprise Zones**

*Kentucky Revised Statute 154.45-090(2)(3), effective 1992*

Building materials used in remodeling, rehabilitation, or new construction in a qualified enterprise zone and new and used equipment and machinery purchased by a qualified business for use in the enterprise zone are exempt.

Enterprise Zones are scheduled to expire 20 years after initial designation as a zone. The first zones approved (Jefferson County and Fulton County) will expire on December 31, 2003, with additional zones expiring thereafter.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Compensation Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$38.0 million</td>
</tr>
<tr>
<td>FY2005</td>
<td>$14.0 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$10.0 million</td>
</tr>
</tbody>
</table>

11. **State, Cities, Counties and Special Districts**

*Kentucky Revised Statute 139.470(1)(7), effective 1960 and 1976*

Sales to any cabinet, department, bureau, commission, board, or other statutory or constitutional agency of the state, and to cities, counties, and special districts defined in KRS 65.005 are exempt.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Compensation Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$85.8 million</td>
</tr>
<tr>
<td>FY2005</td>
<td>$88.4 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$91.0 million</td>
</tr>
</tbody>
</table>
12. Textbooks

*Kentucky Revised Statute 139.480(17), effective 1978*

Textbooks, related workbooks, and other course material purchased for use in a course of study conducted by an institution qualifies as a non-profit educational institution are exempt.

- FY2004 .................................... $4.2 million
- FY2005 .................................... $4.3 million
- FY2006 .................................... $4.5 million

13. Recycling Machinery and Equipment

*Kentucky Revised Statute 139.170, 139.480(23), effective 1991*

Replacement machinery that will increase the consumption of recycled materials by not less than 10 percent and machinery and equipment purchased or leased by a business, industry or organization in order to collect, source separate, compress, bale, shred or otherwise handle waste materials, if that machinery or equipment is primarily used for recycling purposes, are exempt.

- FY2004 .................................... $3.5 million
- FY2005 .................................... $3.6 million
- FY2006 .................................... $3.7 million

14. Pollution Control Facilities

*Kentucky Revised Statute 139.480(12), effective 1974*

Property certified as a pollution control facility as defined by KRS 224.01-300 is exempt.

- FY2004 .................................... $13.5 million
- FY2005 .................................... $13.9 million
- FY2006 .................................... $14.3 million
15. Tombstones and Other Grave Markers

*Kentucky Revised Statute 139.480(13), effective 1976*

Tombstones and other grave markers are exempt.

- FY2004 .................................... $2.8 million
- FY2005 .................................... $3.0 million
- FY2006 .................................... $3.1 million

16. Lodgings of Thirty Days or More

*Kentucky Revised Statute 139.100(2)(a), effective 1992*

Rooms, lodging or accommodations supplied for a continuous period of 30 days or more to an individual are exempt.

- FY2004 .................................... $2.3 million
- FY2005 .................................... $2.3 million
- FY2006 .................................... $2.4 million

17. Garage or Yard Sales

*Kentucky Revised Statute 139.496, effective 1976*

Sales and use tax does not apply to the first $1,000 of sales made in any calendar year by an individual or nonprofit organization not engaged in the business of selling.

- FY2004 .................................... $2.2 million
- FY2005 .................................... $2.2 million
- FY2006 .................................... $2.3 million
18. Semi-Trailers and Trailers  
*Kentucky Revised Statute 139.050(3)(f), effective 1978*

The sales of semi-trailers and trailers as defined by KRS 189.010(12) and KRS 189.010(17) are exempt.

- FY2004 .................................... $11.2 million
- FY2005 .................................... $11.7 million
- FY2006 .................................... $12.1 million

19. Vessels and Maritime Supplies  
*Kentucky Revised Statute 139.483, effective 1966*

Ships and vessels, including their repair and construction, supplies and fuel used in their operation and supplies consumed by crew members aboard such ships and vessels, used principally in transporting property for hire are exempt.

- FY2004 .................................... $4.2 million
- FY2005 .................................... $4.2 million
- FY2006 .................................... $4.3 million

20. Sales by Elementary and Secondary Nonprofit, School-Sponsored Clubs and Organizations  
*Kentucky Revised Statute 139.497, effective 1984*

Sales made by elementary and secondary schools, nonprofit elementary or secondary school-sponsored clubs and organizations and nonprofit elementary or secondary school affiliated groups such as parent-teacher organizations and booster clubs are exempt.

- FY2004 .................................... $5.9 million
- FY2005 .................................... $5.9 million
- FY2006 .................................... $6.0 million
21. Interstate Cargo and Passenger Aircraft, Parts and Supplies

*Kentucky Revised Statute 139.480(19), effective 1982*

Aircraft and their repair and replacement parts and supplies for the direct operation of aircraft in interstate commerce and used exclusively for the conveyance of property or passengers for hire are exempt from sales and use tax. Nominal intrastate use will not subject the property to sales and use tax.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
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</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$36.2 million</td>
</tr>
<tr>
<td>FY2005</td>
<td>$37.4 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$38.8 million</td>
</tr>
</tbody>
</table>

22. Sales by Nonprofit Higher Educational School-Sponsored Clubs and Organizations.

*Kentucky Revised Statute 139.495(4), effective 1980*

Sales made by nonprofit school-sponsored clubs and organizations, provided such sales do not include tickets for athletic events, are exempt.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$1.2 million</td>
</tr>
<tr>
<td>FY2005</td>
<td>$1.2 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$1.3 million</td>
</tr>
</tbody>
</table>

23. Sales to Motion Picture Companies

*Kentucky Revised Statute 139.538-.5386, effective 1986*

Motion picture production companies filming or producing motion pictures in Kentucky are exempt from the tax. The exemption is accomplished by granting a refundable credit of taxes paid on purchases made in Kentucky in connection with the filming or producing of a motion picture in this state.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$100,000</td>
</tr>
<tr>
<td>FY2005</td>
<td>$100,000</td>
</tr>
<tr>
<td>FY2006</td>
<td>$100,000</td>
</tr>
</tbody>
</table>
24. **Admissions to and Purchases by Historical Sites**  
*Kentucky Revised Statute 139.482, effective 1976*

Sales of admissions and purchases made by an historical site operated by a non-profit corporation, society, or organization and listed by the United States Department of Interior in the National Register of Historic Places are exempt.

- FY2004 $3.0 million
- FY2005 $3.1 million
- FY2006 $3.2 million

25. **Credit Unions**  
*Kentucky Revised Statute 290.365, effective 1984*

Sales to credit unions organized under Kentucky law are exempt.

- FY2004 $1.2 million
- FY2005 $1.2 million
- FY2006 $1.2 million

26. **Coin-Operating Bulk Vending Machines**  
*Kentucky Revised Statute 139.470(6), effective 1966, revised 1998*

Vending machine sales of 50 cents or less are exempt from tax. Prior to the 1998 legislative change the amount exempt was 25 cents or less.

- FY2004 $2.1 million
- FY2005 $2.1 million
- FY2006 $2.2 million
27. Non-returnable and Returnable Containers

*Kentucky Revised Statute 139.470(2), effective 1960*

Non-returnable and returnable containers sold without contents to persons who place the contents in the containers and sell contents and containers together, and returnable containers sold with the contents at retail or sold for refilling are exempt.

FY2004 ....................................$1.2 million
FY2005 ....................................$1.2 million
FY2006 ....................................$1.2 million

28. Occasional Sales

*Kentucky Revised Statute 139.070, 139.470(4), effective 1960*

Casual or isolated sales of property not held or used by a seller in the course of an activity for which he is required to hold a seller’s permit are exempt.

FY2004 ....................................$120.0 million
FY2005 ....................................$120.0 million
FY2006 ....................................$120.0 million

29. Locomotives and Rolling Stock

*Kentucky Revised Statute 139.480(1), effective 1960*

Locomotives or rolling stock, including materials for their construction, repair, or modification, or fuel and supplies for the direct operation of locomotives and trains used in interstate commerce are exempt.

FY2004 ....................................$1.5 million
FY2005 ....................................$1.5 million
FY2006 ....................................$1.5 million
30. Procurement, Processing, or Distribution of Blood or Human Tissue
   Kentucky Revised Statute 139.125, effective 1968

Whole blood, plasma, blood products, tissues such as corneas, bones, or organs for the purpose of injecting, transfusing, or transplanting any of them into the human body are exempt.

   FY2004 ....................................$900,000
   FY2005 ....................................$900,000
   FY2006 ....................................$910,000

31. Rate Increase for School Taxes added to Residential Telephone Bills
   Kentucky Revised Statute 139.470(9), effective 1979

Any rate increase for school taxes and any other charges or surcharges added to the total amount of a residential telephone bill is exempt.

   FY2004 ....................................$4.0 million
   FY2005 ....................................$4.1 million
   FY2006 ....................................$4.3 million

32. Raw Materials and Industrial Supplies
   Kentucky Revised Statute 139.470(11), effective 1990

Raw materials and industrial supplies are exempt from sales and use tax if they enter into and become an ingredient or component part of the manufactured product or they are directly used in manufacturing or industrial processing.

   FY2004 ....................................$453.2 million
   FY2005 ....................................$466.8 million
   FY2006 ....................................$480.8 million
33. Federal Taxes Imposed on Sales of Tangible Personal Property  
_Kentucky Revised Statute 139.050(3)(d), 139.130(3)(d), effective 1960_

Taxes (not including any manufacturer’s excise or import duty) imposed by the United States upon or with respect to retail sales are exempt.

- FY2004 ....................................$4.1 million
- FY2005 ....................................$4.3 million
- FY2006 ....................................$4.5 million

34. Sales to Common Carriers Under a Bill of Lading  
_Kentucky Revised Statute 139.470(5), effective 1960_

Gross receipts from sales of tangible personal property to a common carrier, shipped by the seller via the purchasing carrier under a bill of lading, whether the freight is paid in advance or the shipment is made freight charges collect, to a point outside this state and the property is actually transported to the out-of-state destination for use by the carrier in the conduct of its business as a common carrier are exempt.

- FY2004 ....................................$-0-
- FY2005 ....................................$-0-
- FY2006 ....................................$-0-

35. Lease or Rental of Films by Commercial Theaters  
_Kentucky Revised Statute 139.484, effective 1990_

The lease or rental of films by commercial motion picture theaters, when the lease or rental is for the sole purpose of use in the normal course of business, if an admission fee is charged and if the commercial motion picture theater collects and remits all other applicable sales and use taxes, is exempt.

- FY2004 ....................................$1.1 million
- FY2005 ....................................$1.1 million
- FY2006 ....................................$1.2 million
36. Tourism Attraction Project Credit/Refund

*Kentucky Revised Statute 139.536, effective 1996 – Kentucky Revised Statute 154, effective 1998, amended 2001*

A credit is allowed against the sales tax generated by or arising from a tourism attraction project. The amount of the credit is calculated and refunded on an annual basis.

- FY2004 .................................... $4.5 million
- FY2005 .................................... $4.8 million
- FY2006 .................................... $5.1 million

37. Alcohol Production Facilities

*Kentucky Revised Statute 139.480(18), effective 1980*

Any sale, use, storage or consumption of tangible property certified as an alcohol production facility as defined in KRS 247.910 is exempt.

- FY2004 .................................... $-0-
- FY2005 .................................... $-0-
- FY2006 .................................... $-0-

38. Property Certified as a Fluidized Bed Energy Production Facility

*Kentucky Revised Statute 139.480(20), effective 1986*

Any sale, use, storage or consumption of tangible property that has been certified as a fluidized bed energy production facility, as defined in KRS 211.390, is exempt.

- FY2004 .................................... $-0-
- FY2005 .................................... $-0-
- FY2006 .................................... $-0-
39. Catalogs and Newspaper Inserts Shipped Outside Kentucky
   
   *Kentucky Revised Statute 139.470, effective 1988*
   
   Catalogs and newspaper inserts purchased for storage, use or other consumption outside this state and delivered by the seller’s own vehicle, postal service, common carrier or contract carrier to a location outside this state are exempt.
   
<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$3.0 million</td>
</tr>
<tr>
<td>FY2005</td>
<td>$3.0 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$3.0 million</td>
</tr>
</tbody>
</table>

40. 4-H Sales
   
   *Kentucky Revised Statute 139.497, effective 1998*
   
   Sales made by nonprofit educational youth programs affiliated with a land grant university cooperative extension service are exempt if the net proceeds from the sales are used solely for the benefit of the affiliated programs.
   
<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$100,000</td>
</tr>
<tr>
<td>FY2005</td>
<td>$100,000</td>
</tr>
<tr>
<td>FY2006</td>
<td>$100,000</td>
</tr>
</tbody>
</table>

41. Jet Fuel
   
   *Kentucky Revised Statute 144.132, effective July 1, 2000*
   
   Certified air carriers are allowed a credit after payment of the first $1.0 million in sales and use tax on the purchase of aircraft fuel including jet fuel.
   
<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$19.3 million</td>
</tr>
<tr>
<td>FY2005</td>
<td>$20.0 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$20.7 million</td>
</tr>
</tbody>
</table>
42. Repair Parts for Large Trucks  
*Kentucky Revised Statute 139.480, effective January 1, 2004*

Repair parts for those trucks and their towed units over 44,001 pounds that are used exclusively in interstate commerce are exempt from sales tax for purchases on or after January 1, 2004.

- FY2004 ....................................$1.5 million
- FY2005 ....................................$4.0 million
- FY2006 ....................................$4.1 million

**Sales Tax Exemptions for Farmers**

The following tax expenditures pertain to the farming industry.

43. Livestock, Poultry, Ratite Birds, Embryos and Semen, Alpacas, Llamas, Buffalo, Farm Work Stock and Feed, Seeds and Fertilizers  
*Kentucky Revised Statute 139.480(4),(5), (6),(7),(9), (24), (25), (26), and (29) effective 1960, 1994,1996*

Livestock that ordinarily constitutes food for human consumption, provided the sales are made for breeding or dairy purposes and by or to a person regularly engaged in the business of farming; poultry for use in breeding or egg production; ratite birds and eggs to be used in an agricultural pursuit for the breeding and production of ratite birds, feathers, hides, breeding stock, eggs, meat, and ratite by-products; embryos and semen used in the reproduction of livestock; llamas and alpacas used as beasts of burden or in the breeding and production of hides, breeding stock, fiber and wool products, meat, and llama and alpaca by-products; and farm work stock for use in farming operations are exempt from the tax. Seeds, feed, and fertilizer, the products of which ordinarily constitute food for human consumption or which are to be sold in the regular courses of business are exempt.

- FY2004 ....................................$87.1 million
- FY2005 ....................................$89.7 million
- FY2006 ....................................$92.4 million
44. Horses Purchased for Breeding

*Kentucky Revised Statute 139.531(2)(a), effective 1976*

The sales and use tax does not apply to horses, interests in horses, or shares in horses, provided the purchase or use is made for breeding purposes only.

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$12.3 million</td>
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<tr>
<td>FY2005</td>
<td>$12.5 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$12.6 million</td>
</tr>
</tbody>
</table>

45. Farm Machinery, Attachments, and Replacements, On-Farm Grain Storage Facilities, and On-Farm Facilities for Raising Chickens, Livestock, Ratite Birds, Llamas and Alpacas, and Buffalo

Farm machinery and repair and replacement parts for the operation of farm machinery are exempt. *Kentucky Revised Statute 139.480(11), effective 1968*

On-farm facilities used exclusively for grain or soybean storing, drying, processing or handling, including all construction, renovation, or repair materials, parts, and equipment, are exempt. *Kentucky Revised Statute 139.480(14), effective 1978*

On-farm facilities used exclusively for raising chickens and livestock, ratite birds, and llamas and alpacas, the products of which ordinarily constitute food for human consumption, including equipment, machinery, attachments, repair and replacement parts, and any materials incorporated into the construction, renovation, or repair of the facility are exempt. *Kentucky Revised Statute 139.480(15), (24), (26), and (29), effective 1990, 1994, and 1996*

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
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<tbody>
<tr>
<td>FY2004</td>
<td>$12.9 million</td>
</tr>
<tr>
<td>FY2005</td>
<td>$13.3 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$13.7 million</td>
</tr>
</tbody>
</table>
46. Fuel Used for Farm Purposes

*Kentucky Revised Statute 139.480(16), effective 1978, revised 1998*

Gasoline, special fuels, and liquefied petroleum gas used to operate or propel stationary engines or tractors for agricultural purposes are exempt.

- FY2004 ....................................$7.1 million
- FY2005 ....................................$7.3 million
- FY2006 ....................................$7.5 million

47. Water Used for Farm Purposes

*Kentucky Revised Statute 139.480, effective 1998*

Water sold to persons regularly engaged in the business of farming and used in the production of crops, milk for sale, or raising and feeding livestock, poultry, ratites, llamas, alpacas, buffalo or aquatic organisms is exempt.

- FY2004 ....................................$50,000
- FY2005 ....................................$50,000
- FY2006 ....................................$50,000

48. Equine Water

*Kentucky Revised Statute 139.470, effective 1998*

Water used in the equine-raising business is exempt.

- FY2004 ....................................$50,000
- FY2005 ....................................$50,000
- FY2006 ....................................$50,000
49. **Aquaculture**  
*Kentucky Revised Statute 139.480, effective 1998*

Aquatic organisms sold directly to or raised by a person regularly engaged in the business of producing products of aquaculture for sale and items necessary for the production of aquatic organisms are exempt.

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$100,000</td>
</tr>
<tr>
<td>FY2005</td>
<td>$105,000</td>
</tr>
<tr>
<td>FY2006</td>
<td>$110,000</td>
</tr>
</tbody>
</table>

50. **Twine and Wire**  
*Kentucky Revised Statute 139.480, effective 1998*

Baling twine and baling wire used for the purpose of baling hay and straw are exempt.

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$30,000</td>
</tr>
<tr>
<td>FY2005</td>
<td>$30,000</td>
</tr>
<tr>
<td>FY2006</td>
<td>$30,000</td>
</tr>
</tbody>
</table>

51. **Horses Less Than Two Years of Age**  
*Kentucky Revised Statute 139.531(2)c, effective 1976*

Sales of horses less than two years of age at the time of sale, provided the sale is made to a nonresident of Kentucky, and the horse is transported out of state, either immediately following the sale or immediately following training within the state are exempt.

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$17.2 million</td>
</tr>
<tr>
<td>FY2005</td>
<td>$17.8 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$18.6 million</td>
</tr>
</tbody>
</table>
52. Farm Chemicals

*Kentucky Revised Statute 139.480(8),(24) and (26), effective 1992, revised 1994, 1996*

Insecticides, fungicides, herbicides, rodenticides, and other farm chemicals used in the production of crops as a business, or in the raising and feeding of ratite birds, llamas and alpacas, or livestock and poultry, the products of which ordinarily constitute food for human consumption are exempt.

FY2004 ....................................$7.3 million
FY2005 ....................................$7.5 million
FY2006 ....................................$7.7 million

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>$144.1 million</td>
</tr>
<tr>
<td>2005</td>
<td>$148.3 million</td>
</tr>
<tr>
<td>2006</td>
<td>$152.7 million</td>
</tr>
</tbody>
</table>

**Table 16. Subtotal for Farming Tax Expenditures**

Exclusion of Services

*Kentucky Revised Statute 139.100 and 139.160, effective 1960*

Services are excluded from the sales and use tax by the definition of “retail sale” or “sale at retail” as a sale of tangible personal property.

(a) Personal services.

FY2004 ....................................$59.3 million
FY2005 ....................................$63.0 million
FY2006 ....................................$67.0 million
(b) Business services.

FY2004 .................................... $168.6 million
FY2005 .................................... $179.1 million
FY2006 .................................... $190.3 million

(c) Health services.

FY2004 .................................... $421.3 million
FY2005 .................................... $447.6 million
FY2006 .................................... $475.5 million

(d) Legal services.

FY2004 .................................... $74.5 million
FY2005 .................................... $79.2 million
FY2006 .................................... $84.1 million

(e) Educational services.

FY2004 .................................... $5.0 million
FY2005 .................................... $5.3 million
FY2006 .................................... $5.6 million

(f) Social services.

FY2004 .................................... $13.6 million
FY2005 .................................... $14.5 million
FY2006 .................................... $15.4 million

(g) Engineering, accounting, research, management.

FY2004 .................................... $ 99.8 million
FY2005 .................................... $106.0 million
FY2006 .................................... $112.6 million
(h) Automotive and miscellaneous repair services.

FY2004 ................................... $110.8 million
FY2005 ................................... $117.7 million
FY2006 ................................... $125.0 million

(i) Amusement and recreational services.  
(Taxable amusement and recreational services such as video tape rentals and commercial sports events are not included in this estimate.)

FY2004 .................................... $13.4 million
FY2005 .................................... $14.3 million
FY2006 .................................... $15.1 million

(j) Other Services.

FY2004 .................................... $5.1 million
FY2005 .................................... $5.4 million
FY2006 .................................... $5.7 million

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>$ 971.4 million</td>
</tr>
<tr>
<td>2005</td>
<td>$ 1,032.1 million</td>
</tr>
<tr>
<td>2006</td>
<td>$ 1,096.3 million</td>
</tr>
</tbody>
</table>

Table 17. Total for Excluded Services
Background

The term “special fuels” is defined to include all combustible gases and liquids capable of being used in motor vehicles, except gasoline, as defined in KRS 138.210, and liquefied petroleum gas, as defined in KRS 234.100. A tax on special fuels was first enacted in 1952. When the base was changed for gasoline in 1980 to the average per gallon wholesale price, the special fuels tax base was changed accordingly. This provided that the special fuels rate would be a function of the wholesale price of gasoline, and as the price of gasoline rose, the rate on special fuels would rise proportionately. The “supplemental highway user tax” became effective July 1, 1986.

In 1988, the General Assembly made a major change in the special fuels law. The new law requires that the tax be levied on the dealer at the point of receipt of the fuels (as is the case for gasoline) instead of the point of sale by the dealer. Generally, special fuels used for off-highway purposes are subject to a refund of the tax, provided proper applications are filed and other procedures are followed.

The tax is imposed for the privilege of using the highways of the state, therefore, the receipts are deposited in the Road Fund. For FY03, the special fuels tax collections were $104.5 million, which was 9.3 percent of total Road Fund tax receipts.

Current Tax Rate

The current tax rate is a minimum of 10 cents per gallon. As the price of the fuel increases above $1.11 per gallon, the tax increases accordingly. The current rate for the supplemental highway tax is 2 cents per gallon thereby increasing the total minimum rate on special fuels to 12 cents per gallon.

Tax Base

The tax is based on the average wholesale price per gallon of special fuel with a minimum wholesale price of $1.11 per gallon. The tax becomes a liability of the dealer when the special fuel is received or enters the dealer’s storage facility. The dealer is allowed a deduction of 2.25 percent to cover evaporation, shrinkage, unaccountable losses, collection costs, bad debts, and handling and reporting the tax.
Taxable Unit

The unit for levying the special fuels tax is a “per gallon” basis.

Tax Due

Returns and payments of the tax are due monthly. The tax must be remitted to the Revenue Cabinet on or before the twenty-fifth day of the month.

Table 18. Total Special Fuels Tax Expenditures

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Tax Expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>$49.1 million</td>
</tr>
<tr>
<td>2005</td>
<td>$50.6 million</td>
</tr>
<tr>
<td>2006</td>
<td>$52.0 million</td>
</tr>
</tbody>
</table>

Tax Expenditures

1. Non-highway Use

*Kentucky Revised Statute 138.344(1), effective 1988, revised 2000*

Special fuels used exclusively for non-highway use by qualified purchasers are exempt sales.

FY2004 .................................... $27.0 million
FY2005 .................................... $28.0 million
FY2006 .................................... $29.0 million
2. Railroad Companies

*Kentucky Revised Statute 138.240(2)(f), effective 1988*

Railroad companies principally engaged in the business of transporting property for others as a common carrier or in the conveyance of persons are exempt.

- FY2004 .................... $12.2 million
- FY2005 .................... $12.5 million
- FY2006 .................... $12.7 million

3. Agricultural Use

*Kentucky Revised Statute 138.358(2), effective 1988*

A credit is allowed for special fuels used for non-highway agricultural purposes.

- FY2004 .................... $3.5 million
- FY2005 .................... $3.6 million
- FY2006 .................... $3.7 million

4. Dealer’s Monthly Reporting Allowance

*Kentucky revised Statute 138.270(1)(b), effective 1958*

An allowance of 2.25 percent of the net tax due is allowed a dealer on a timely filed and paid monthly return. This allowance is given to offset the costs of evaporation, shrinkage, unaccountable losses, collection costs, bad debts and handling and reporting the tax.

- FY2004 .................... $2.3 million
- FY2005 .................... $2.3 million
- FY2006 .................... $2.3 million
5. **Residential Heating**  
*Kentucky Revised Statute 138.358(1), effective 1988*

An exemption is allowed for special fuels used exclusively for heating personal residences.

- FY2004 .................................... $1.4 million
- FY2005 .................................... $1.4 million
- FY2006 .................................... $1.4 million

6. **Bus, Taxicab and Certain Senior Citizen’s Programs Refunds**  
*Kentucky Revised Statute 138.446, effective 1978*

Seven-ninths of the tax paid is refunded if the special fuels are used in regularly scheduled operations of the city and suburban buses, taxicabs, senior citizen transportation and non-profit buses.

- FY2004 .................................... $310,000
- FY2005 .................................... $315,000
- FY2006 .................................... $320,000

7. **State and Local Government Use**  
*Kentucky Revised Statute 138.358(3), effective 1988*

An exemption is allowed for sales to qualifying state and local government agencies for non-highway use.

- FY2004 .................................... $200,000
- FY2005 .................................... $200,000
- FY2006 .................................... $200,000
8. Religious, Charitable or Educational Use

_Kentucky Revised Statute 138.358(3), effective 1988_

An exemption is allowed for sales to qualifying non-profit religious, charitable or educational organizations for non-highway use.

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$200,000</td>
</tr>
<tr>
<td>FY2005</td>
<td>$200,000</td>
</tr>
<tr>
<td>FY2006</td>
<td>$200,000</td>
</tr>
</tbody>
</table>

9. Watercraft

_Kentucky Revised Statute 138.455, effective 1960_

One hundred percent of the tax paid on special fuels to operate or propel watercraft is refunded to qualified boat dock operators.

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$30,000</td>
</tr>
<tr>
<td>FY2005</td>
<td>$30,000</td>
</tr>
<tr>
<td>FY2006</td>
<td>$30,000</td>
</tr>
</tbody>
</table>

10. U.S. Government Exemption

_Kentucky Revised Statute 138.240(2), effective 7/1/88_

Special fuels sold to the U.S. Government are exempt.

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$2.0 million</td>
</tr>
<tr>
<td>FY2005</td>
<td>$2.0 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$2.0 million</td>
</tr>
</tbody>
</table>
EARMARKED FUNDS

Earmarked funds are reserved to be spent only on a particular program. The taxpayer is still liable for the tax, and the state is still collecting these revenues. The fact that the revenues are earmarked for special purposes does not qualify them as tax expenditures.

Earmarked funds are included for informational purposes in this report because they do have an impact on the amount of usable funds collected by the General Fund and the Road Fund.

Table 19. Total Earmarked Funds

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>$20.9 million</td>
</tr>
<tr>
<td>2005</td>
<td>$22.7 million</td>
</tr>
<tr>
<td>2006</td>
<td>$23.2 million</td>
</tr>
</tbody>
</table>

Earmarked Funds

1. Thoroughbred Development Fund - Pari-Mutuel Tax

\[ \text{Kentucky Revised Statute 138.510, effective 1990} \]

Three-quarters of one percent (0.75%) of all pari-mutuel wagering at thoroughbred horse tracks under the jurisdiction of the Kentucky Racing Commission and 2 percent of wagering at receiving tracks in intertrack wagering, as well as telephone account wagering is deducted from the pari-mutuel tax and deposited in this fund.

FY2004 ..............................................$8.2 million
FY2005 ..............................................$8.3 million
FY2006 ..............................................$8.3 million
2. **Equine Industry Program Trust and Revolving Fund - Pari-Mutuel Tax**  
*Kentucky Revised Statute 138.510(3), effective 1990*

One-fifth of one percent (0.2%) of the total amount wagered on live racing in Kentucky and .05 percent of the total amount wagered on intertrack wagering is deducted from the pari-mutuel tax and deposited in this fund. The fund is used for the equine industry program at the University of Louisville.

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$525,000</td>
</tr>
<tr>
<td>FY2005</td>
<td>$525,000</td>
</tr>
<tr>
<td>FY2006</td>
<td>$525,000</td>
</tr>
</tbody>
</table>

3. **Higher Education Equine Trust and Revolving Fund - Pari-Mutuel Tax**  
*Kentucky Revised Statute 138.510(4), effective 1992*

One-tenth of one percent (0.1%) of the total amount wagered in Kentucky is deducted from the pari-mutuel tax to be deposited in this fund. The fund is used for construction, expansion or renovation of facilities or the purchase of equipment for equine programs at state universities.

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$550,000</td>
</tr>
<tr>
<td>FY2005</td>
<td>$550,000</td>
</tr>
<tr>
<td>FY2006</td>
<td>$550,000</td>
</tr>
</tbody>
</table>

4. **Standardbred Development Fund - Pari-Mutuel Tax**  
*Kentucky Revised Statute 230.265(3), effective 1990*

One percent of all pari-mutuel wagering at harness host tracks under the jurisdiction of the Kentucky Racing Commission and 2 percent of wagering at receiving tracks in intertrack wagering, as well as telephone account wagering is deducted from the tax and deposited in this fund.

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$430,000</td>
</tr>
<tr>
<td>FY2005</td>
<td>$430,000</td>
</tr>
<tr>
<td>FY2006</td>
<td>$430,000</td>
</tr>
</tbody>
</table>
5. Tobacco Enforcement Program - Cigarette Tax  
*Kentucky Revised Statute 438.335 and 438.337, effective 1996*

One-twentieth of one cent of the three-cent per pack revenue collected from the state excise tax on cigarettes is earmarked for the Department of Agriculture to enforce the laws aimed at the prevention of sales of tobacco products to minors.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$530,000</td>
</tr>
<tr>
<td>FY2005</td>
<td>$535,000</td>
</tr>
<tr>
<td>FY2006</td>
<td>$540,000</td>
</tr>
</tbody>
</table>

6. Kentucky Transportation Center - Motor Fuels Tax  
*Kentucky Revised Statute 177.320(4), effective 1986*

The Kentucky Transportation Center receives 0.1 percent of all revenues arising from the imposition of taxes on gasoline, special fuels and liquefied petroleum gas. The receipts are limited to $190,000 in any fiscal year.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$190,000</td>
</tr>
<tr>
<td>FY2005</td>
<td>$190,000</td>
</tr>
<tr>
<td>FY2006</td>
<td>$190,000</td>
</tr>
</tbody>
</table>

7. Tobacco Research Trust Fund - Cigarette Tax  
*Kentucky Revised Statute 248.540, effective 1970*

One-sixth of the tax collected is earmarked for the Tobacco Research Trust Fund.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY2004</td>
<td>$3.3 million</td>
</tr>
<tr>
<td>FY2005</td>
<td>$3.4 million</td>
</tr>
<tr>
<td>FY2006</td>
<td>$3.5 million</td>
</tr>
</tbody>
</table>
8. Agricultural Diversification and Development Fund - Cigarette Tax  
   *Kentucky Revised Statute 248.652*, effective 1998

Any additional increases in the cigarette tax are earmarked for the Agricultural Diversification and Development Council to be distributed to various diversification and health-related programs.

   - FY2004: $0
   - FY2005: $0
   - FY2006: $0

9. Equine Drug Research - Pari-Mutuel Tax  
   *Kentucky Revised Statute 230.265(3)*, effective 1982

An amount equal to 0.1 percent of the total amount wagered in Kentucky is deducted from the pari-mutuel tax to be used in financing drug research and testing.

   - FY2004: $600,000
   - FY2005: $600,000
   - FY2006: $600,000
10. Kentucky Aviation Economic Development Fund - Sales Tax
   Kentucky Revised Statute 183.525, effective July 1, 2000

   All sales and use tax collected on the sale of aircraft fuel is deposited in this fund.

   FY2004 .................................... $5.6 million
   FY2005 .................................... $5.7 million
   FY2006 .................................... $5.8 million

11. Tax Increment Financing - Various Taxes
   Kentucky Revised Statute 65.495, effective July 14, 2000 and
   Kentucky Revised Statute 65.703, effective June 21, 2001

   A locality may create a development area and, with state approval, receive payment of part of the increase in tax revenues within the development area to help offset the cost of development. Potentially all taxes could be involved, although it is expected that sales, property and income taxes would be most utilized because of the dollar volume.

   FY2004 ........................................ $1.0 million
   FY2005 ........................................ $2.5 million
   FY2006 ........................................ $2.8 million