

Kentucky Imposes Sales and Use Tax on 35 New Services



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Did you say 35 new services will be subject to sales and use tax? Yes. Additionally, an exemption from sales tax was expanded, a *de minimis* threshold was enacted for the new services, and there is a new reporting requirement for organizers of festivals.

Expand the base, expand the base, expand the base!

Numerous tax reform commissions and paid tax consultants have advised the General Assembly for decades to “modernize” Kentucky’s sales tax statutes by “expanding the tax base.” “Expanding the base” can be done in different ways, such as by repealing exemptions from sales and use tax or by imposing tax on products or services not subject to tax. The Legislature started down the path of expanding the base in 2018 by adding ten services to the tax base and increasing the types of admissions subject to tax.

Effective January 1, 2023, 35 more services will be subject to sales and use tax. Here’s the list:

- Photography and photo finishing services
- Marketing services
- Telemarketing services
- Public opinion and research polling services
- Lobbying services
- Executive employee recruitment services
- Web site design and development services
- Web site hosting services
- Facsimile transmission services
- Private mailroom services, including presorting mail and packages by postal code; address barcoding; tracking; delivery to postal service; and private mailbox rentals
- Bodyguard services
- Residential and nonresidential security system monitoring services
- Private investigation services
- Process server services
- Repossession of tangible personal property services
- Personal background check services
- Parking services, including valet services and the use of parking lots and parking structures, but excluding any parking services at an educational institution
- Road and travel services provided by automobile clubs
- Condominium time-share exchange services
- Rental of space for meetings, conventions, short-term business uses, entertainment events, weddings, banquets, parties, and other short-term social events

- Social event planning and coordination services
- Leisure, recreational, and athletic instructional services
- Recreational camp tuition and fees
- Personal fitness training services
- Massage services, except when medically necessary
- Cosmetic surgery services
- Body modification services including tattooing, piercing, scarification, branding, tongue splitting, transdermal and subdermal implants, ear pointing, teeth pointing, and any other modifications that are not necessary for medical or dental health
- Testing services, except testing for medical, educational, or veterinary reasons
- Interior decorating and design services
- Household moving services
- Specialized design services including the design of clothing, costumes, fashion, furs, jewelry, shoes, textiles, and lighting
- Lapidary services, including cutting, polishing, and engraving precious stones
- Labor and services to repair or maintain commercial refrigeration equipment and systems when no tangible personal property is sold in that transaction including service calls and trip charges
- Labor to repair or alter apparel, footwear, watches, or jewelry when no tangible personal property is sold in that transaction
- Prewritten computer software access services

While examples of the types of things to be taxed is included as part of the language of a few of the services, such as body modification and specialized design services, only five of the 35 are defined:

- Cosmetic surgery services
 - Modifications to all areas of the head, neck, and body to enhance appearance through surgical and medical techniques, *excluding* reconstruction of facial and body defects due to birth disorders, trauma, burns, or disease;
- Photography and photo finishing services
 - (1) The taking, developing, or printing of an original photograph, or (2) Image editing including shadow removal, tone adjustments, vertical and horizontal alignment and cropping, composite image creation, formatting, watermarking printing, and delivery of an original photograph in the form of tangible personal property, digital property, or other media, *excluding* photography services necessary for medical or dental health;
- Marketing services
 - Developing marketing objectives and policies, sales forecasting, new product developing and pricing, licensing, and franchise planning;
- Telemarketing services
 - Services provided via telephone, facsimile, electronic mail, or other modes of communications to another person, which are unsolicited by that person, for the purposes of: (a)(1) promoting products or services; (2) taking orders; or (3) providing information or assistance regarding the products or services; or (b) soliciting contributions; and
- Prewritten computer software access services
 - The right of access to prewritten computer software where the object of the transaction is to use the prewritten computer software while possession of the prewritten computer software is maintained by the seller or a third party, wherever located, regardless of whether the charge for the access or use is on a per use, per user, per license, subscription, or some other basis.

The Department of Revenue is working to develop guidance for taxpayers as to the meaning and breadth of many of the new services. Two other changes were made to expand the reach of sales and use taxes.

Broaden the definition of “extended warranties”

First, the definition of “extended warranties” is amended to impose tax on extended warranties on **real property**. The phrase “extended warranties” is a bit of a misnomer. The phrase includes an agreement such as an extended warranty

on your car, but it also includes what are commonly referred to as maintenance or service contracts. Thus, maintenance or service contracts for real property, such as parking lot cleaning, exterior maintenance of apartment buildings, and heating and air conditioning maintenance, will be subject to sales tax. (Snow removal is already taxable as a “landscaping” service.)

Limit the exemption for residential utilities

Second, the exemption from sales tax on residential utilities, such as sewer services, water, electricity, and natural gas, will be limited to services “purchased and declared by the resident as used in his or her place of domicile.” “Place of domicile” is defined as “the place where an individual has his or her legal, true, fixed, and permanent home and principal establishment, and to which, whenever the individual is absent, the individual has the intention of returning.” Many questions are popping up around this change, including: How does a resident “declare” their place of domicile? Will there be a form? Will there be a different form for every type of utility – water, gas, electric, etc.? What if you own rental property and you pay the utilities? The rental property is not *your* place of domicile, but it is *someone’s* place of domicile.

Add exemptions?

What is the opposite of “expanding the base?” The tax base is narrowed or constricted when existing exemptions are broadened or new exemptions are added. The General Assembly significantly expanded the current exemption for prescription drugs, which has applied only to drugs to treat humans. Effective January 1, 2023, both prescription and over the counter drugs used in the farming and treatment of cattle, sheep, goats, swine, poultry, ratite birds, llamas, alpacas, buffalo, aquatic organisms, or cervids also will be exempt from sales and use tax. (Note that the exemption does not extend to horses.)

Two other exemptions added by the General Assembly are specifically related to the new services subject to sales and use tax. The first provides that the provision of services related to lump sum, fixed-price, or similar contracts executed on or before February 25, 2022 are to be exempt from the additional taxable services imposed. (February 25, 2022 is the date on which House Bill 8 was introduced in the General Assembly.) That date now having passed, any businesses entering multi-year fixed price or lump sum contracts need to factor in the additional taxable services when quoting or bidding on jobs.

Second, there is a partial exemption for the newly taxed services if the gross receipts from the provision of the services were less than \$6,000 during calendar year 2021. However, once gross receipts exceed \$6,000 in 2022 or a subsequent year, all additional receipts are subject to tax. If a business that will provide one of the new taxable services has no doubt but that it will exceed the \$6,000 *de minimis* threshold, we recommend collecting the tax beginning on January 1, 2023 on *all* receipts to eliminate the administrative burdens associated with keeping track of when \$6,000 is reached and rushed actions to register for sales tax and revised accounting and other activities the day after the \$6,000 is met.

Miscellaneous

The final sales tax change of note is aimed at increasing compliance in the state by vendors at events. Beginning July 14, 2022, coordinators of festivals or similar events must provide the Department of Revenue a list of vendors selling at the event. While a precise definition of “festivals or similar events” has not yet been provided, it is possible the reporting requirement could apply to everything from a city or county’s annual spring, summer, or fall festival to large events such as The Kentucky Derby and The Breeder’s Cup.