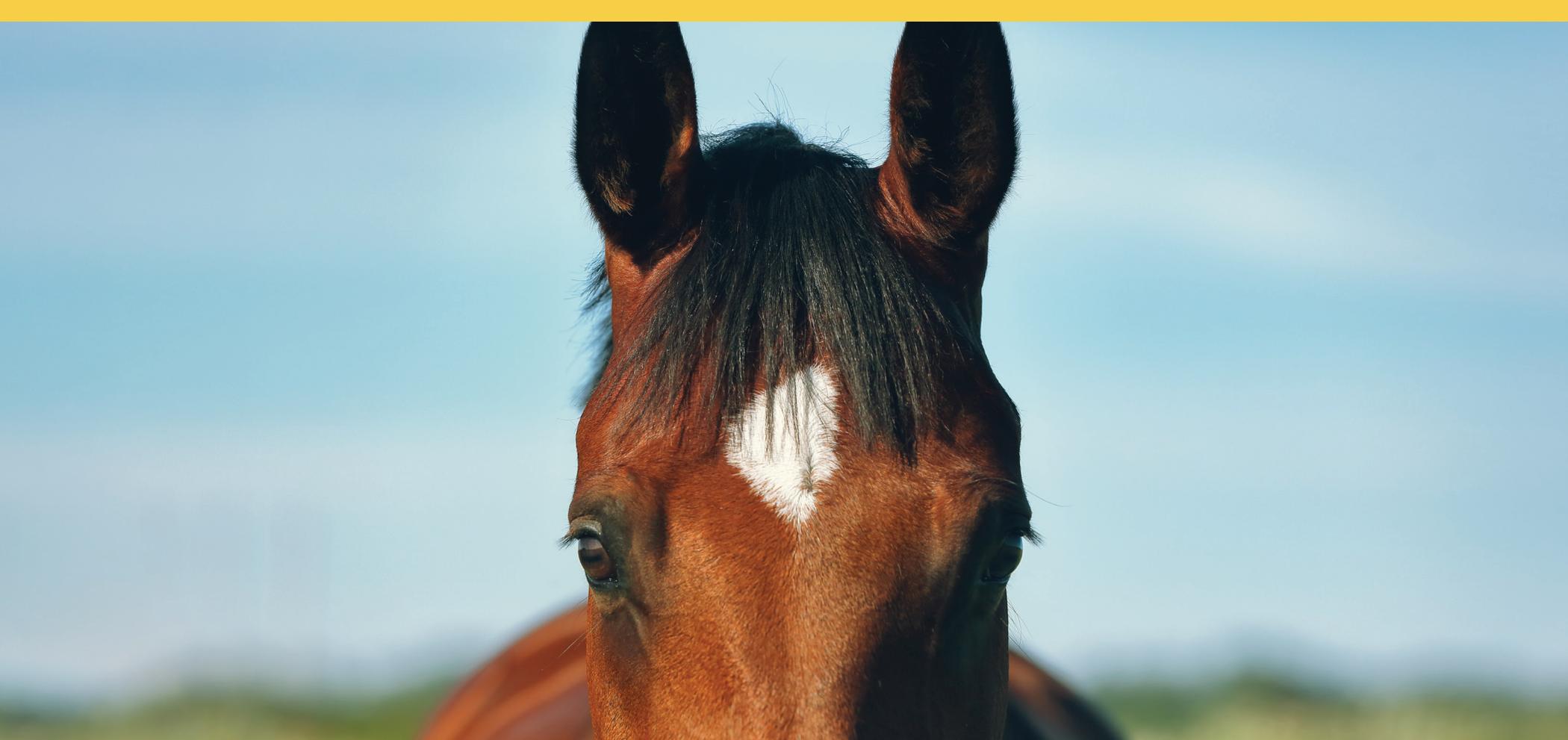


DEANDORTON



Thoroughbred Business Year in Review 2019

THOROUGHBRED BUSINESS YEAR IN REVIEW 2019

Located in Kentucky, known for its world-class horse farms, racing, and sales, our firm of more than 260 team members has provided accounting, tax, and business consulting services to the horse industry for more than 40 years. Our clients cover a broad spectrum of organizations involved in the Thoroughbred and sporthorse industries:

- » from small boarding farms to large multidepartmental farms involved in boarding, breeding, selling, and stallion management;
- » from racing stables and syndicates to racetracks;
- » from bloodstock agents to equine veterinary firms; and
- » from industry associations to equine insurance agencies.

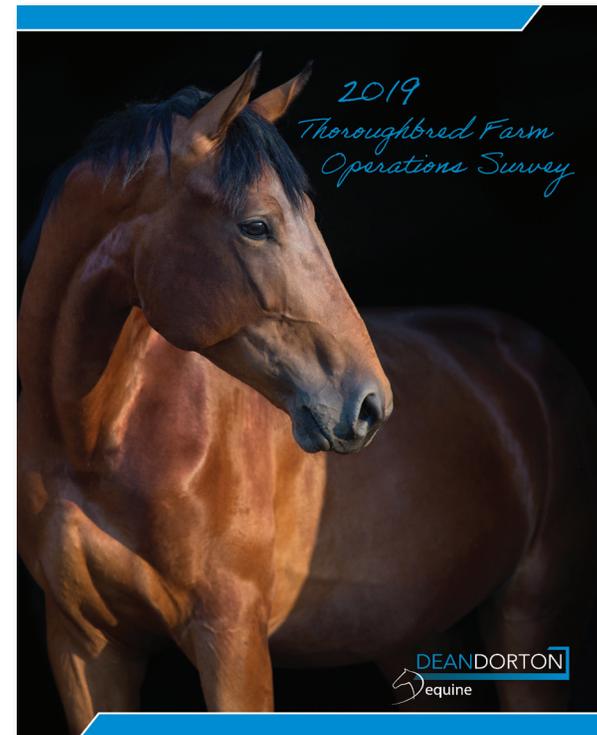
Not all of our clients are based in Kentucky; horse industry clients from across the United States and internationally also gain comfort from having our industry specialists work with them. As a firm, we endeavor to know the business of horses, not just accounting and tax rules relating to the industry. We accomplish this in a number of ways, including, most usefully, by working with our many clients in the industry on their business matters.

We perform a variety of services for our clients involved in the equine industry. And, we welcome inquiries, whether from new participants in the industry who want assistance in properly structuring and administering their stables or farms or from longtime industry participants seeking to improve the performance and administration of their operations.

Members of our Equine Industry Group will be pleased to answer questions you may have regarding this publication. See the Equine Industry Group Leaders page for contact information.

The Thoroughbred Business Year in Review is published by Dean Dorton's Equine Industry Group. We hope you find the information we present regarding the Thoroughbred business to be interesting and helpful.

Dean Dorton also periodically conducts and reports results of surveys of horse farm metrics and practices, mainly centered on pay rates, employee benefits practices, and client billing rates and practices. Our team also co-authors the Equine Sales & Use Tax Review. Please visit deandorton.com/publications to view recent publications, or contact Shannon Abbott at 859-255-2341 or sabbott@deandorton.com if you would like to be placed on our list to receive these publications in the future.



The unique attributes of the equine industry demand services with the depth of experience and expertise that Dean Dorton delivers. When equine industry participants enlist Dean Dorton to provide services, they can be confident they are engaging a firm with in-depth industry experience and know-how. We are interested in our clients' businesses, know the industry, and can provide a wide range of valuable services designed to both optimize savings opportunities and avoid unanticipated problems. Among our team's services are:

Tax Services

- » Developing strategies to use the optimum forms of organization
- » Reducing exposure to the hobby loss rules
- » Structuring transactions to avoid or minimize sales and use taxes
- » Avoiding or managing the potential impact of the passive activity loss rules
- » Using current and deferred trades of real estate, including farms, to avoid or postpone income taxes
- » Using the involuntary conversion tax rules to defer income taxes on insurance recoveries related to horse and farm casualties
- » Estate planning designed to use valuation and family farm conservation easement incentives, family limited partnership strategies, and deferred tax payments
- » Handling multistate tax issues
- » Helping foreign owners and breeders minimize exposure to U.S. taxes and comply with filing requirements
- » Developing tax accounting systems to comply, where required, with rules requiring capitalization of preproductive period costs
- » Taking advantage of unique tax depreciation rules
- » Representing clients with federal and state tax audits

Accounting and Financial Outsourcing

- » Designing and implementing farm accounting and management information systems leveraging cloud-based accounting solutions
- » Working with horse and farm owners to provide full-service backoffice accounting solutions
- » Providing accounting staff at all levels—from CFO to accounts payable clerk—depending on the specific needs of the client
- » Developing key performance indicators to aid horse and farm owners in making business decisions
- » Assessing farm accounting and financial management procedures and practices

Assurance Services

- » Performing audit, review, and compilation services on client financial statements
- » Performing risk assessments and tailored internal audit functions

Business Consulting

- » Developing financial and business plans for farms, breeding operations, and racing stables
- » Litigation support and forensic accounting services
- » Providing a wide range of technology solutions, e.g., complete managed services, network design and support, technology assessments, software consulting, accounting solutions, and business application training
- » Performing comprehensive business valuations/ownership interests in business entities owning equine assets

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Dollars spent at North American Thoroughbred public auctions slightly decreased in 2019 (down 1%) though it continued to surpass the \$1.0 billion mark. The decrease was driven mainly by 4% and 10% decreases in yearling and weanling total sale dollars, respectively. *See pages 2-5.*

Amounts available to Thoroughbred breeders from yearling sales proceeds—after recovering stud fees, sales commissions, and mare and foal board expenses—decreased in 2019 in all stud fee ranges except \$100,000 and over. *See pages 6-8.*

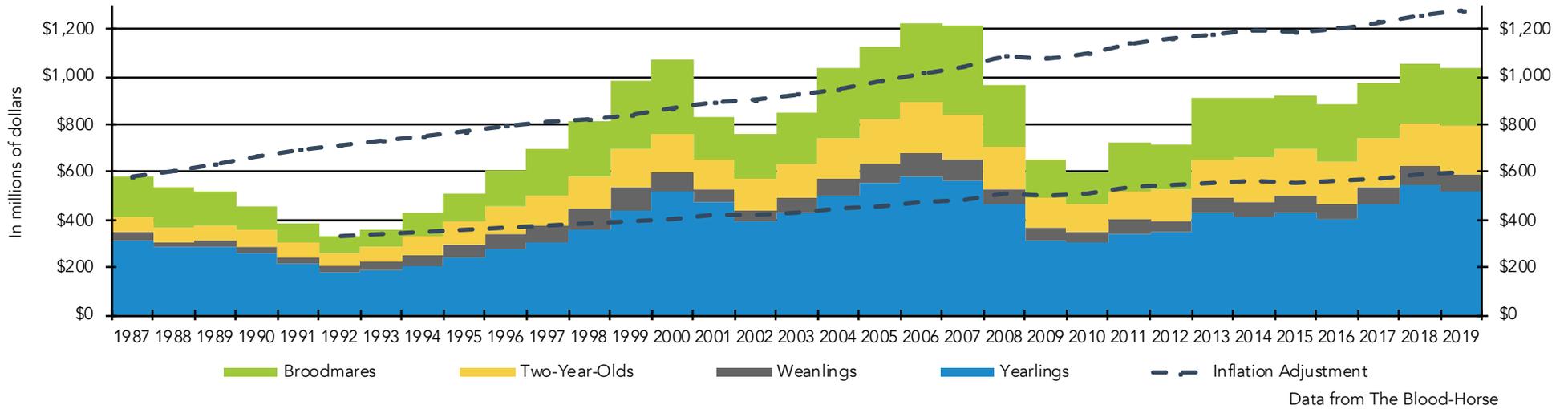
The amounts available from 2019 weanling sales proceeds declined in each stud fee range we analyzed, except for \$100,000 and over and \$20,000 to \$29,999 ranges. On average, owners breeding to stallions with fees in the \$10,000 to \$19,999 range did not cover their expenses whether they sold yearlings or weanlings. *See pages 6-8.*

Depending on the stud fee range, we see a wide variation in the multiple of yearling sales price averages to stud fee averages, from 2.3 to 3.3 in 2019. For each of 2018 and 2019, the highest multiple for yearlings has been in the \$30,000 to \$49,999 range. For weanlings, the range for 2019 sales is narrower, 1.8 to 2.3. *See pages 9-10.*

Gross racing purses continued to rise in 2019 (up 4.4%) after 2018 reflected the first increase since 2012. With still fewer runners in 2019 (a 2.1% drop), average purses per runner increased from \$24,500 to \$26,100. The long decline in starts per runner through the 1990s and first half of the 2000s definitely has stabilized, staying within a 6.1 to 6.3 range over the last 12 years. *See pages 13-14.*

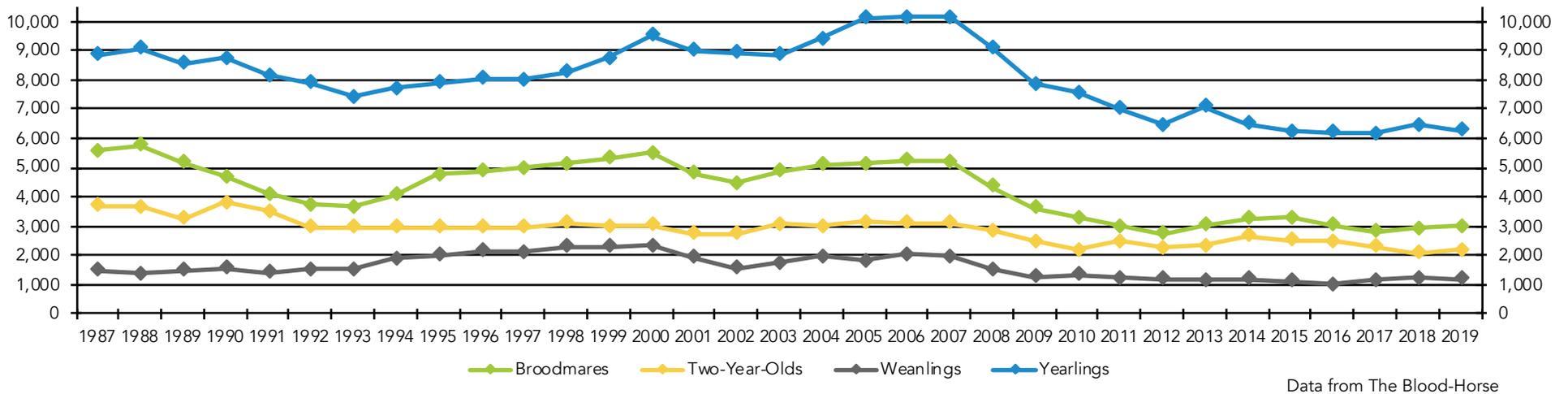
Graph I

Size and Composition of the Public Auction Market in Dollars, 1987 to 2019



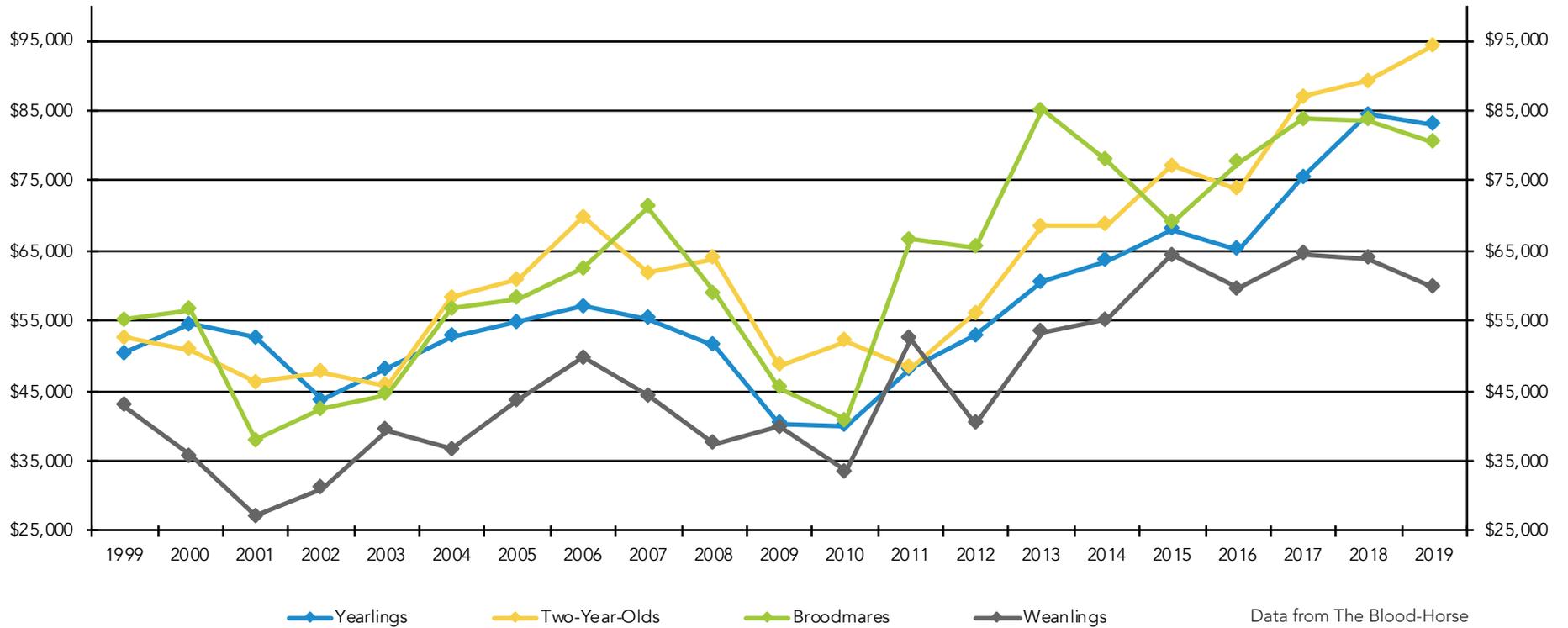
Graph II

Number of Horses Sold at Public Auction by Type of Horse, 1987 to 2019



Graph III

Average Price at Public Auction by Type of Horse, 1999 to 2019



Data from The Blood-Horse

After the precipitous declines in the amounts spent at North American sales in 2008 and 2009 and a less severe decline in 2010, the Thoroughbred horse market recovered some ground in 2011 and 2012, followed by a significant increase in 2013 (27%). The market remained at about the same level in 2013-2016, then increased 10% in 2017, the largest increase since 2013, followed by a 7% increase in 2018. In 2019, the market saw a slight decrease (1%), as shown in Graph I.

For 2019, Graph I shows that while total dollars invested at public auctions decreased 1%, the results in the different categories varied as follows:

Broodmares	-1%
Two-year-olds	+12%
Yearlings	-4%
Weanlings	-10%

From the peak of \$1.226 billion in 2006, to 2019, dollars expended at public auctions dropped by 15%, to \$1.038 billion.

If we observe trends shown in Graph I over the full 33-year period shown, we see that:

- Dollars invested in Thoroughbreds at North American public auctions decreased steadily from 1987 to 1992 (post-1986 federal tax law impacts), then increased steadily and impressively from 1993 to 2000.
- The sharp drops in 2001 and 2002 (post-“dot.com bust” and September 11, 2001 terrorist attacks in the U.S.) were then followed by steady increases from 2003 through 2006.
- This growth leveled off in 2007 (down 1.2%), though dollars invested continued to surpass the \$1.2 billion level.
- The declines of 20% in 2008 and 32% in 2009 (housing bubble burst and ensuing recession) were dramatic; 2010’s decline was 9%.
- The 2011 increase (21%) was the first increase since 2006.
- After pausing at about the same level in 2012, 2013 results were up 27%.
- Public auction dollars then remained steady through 2016, before increasing 10% in 2017 and 7% in 2018.
- In 2019, the growth leveled off (down 1%).

On an inflation-adjusted basis, to be on par with the approximate \$600 million level of public auction dollars in 1987 (the first year of our analysis), auction sales in 2019 would have to have been \$1.278 billion. But, at \$1.038 billion, sales lagged 19% below. After adjusting for inflation, 2019’s auction sales substantially exceeded the low point (1992) of this 33-year period.

Sales by category (in dollars) as a percentage of the total auction market are as follows in the last several years:

	2011	2012	2013	2014	2015	2016	2017	2018	2019
Broodmares	27.6%	26.0%	28.3%	27.8%	24.5%	26.6%	24.1%	22.6%	23.1%
Two-Year-Olds	16.8%	18.4%	17.5%	20.0%	21.3%	20.8%	20.4%	18.0%	19.9%
Yearlings	46.7%	48.7%	47.4%	45.0%	46.3%	45.7%	47.8%	52.0%	50.1%
Weanlings	8.9%	6.9%	6.8%	7.2%	7.9%	6.9%	7.7%	7.4%	6.8%

From its peak in 2006, the number of each type of Thoroughbred sold at public auction has dropped significantly through 2019 (Graph II):

Broodmares	-43%
Two-year-olds	-29%
Yearlings	-38%
Weanlings	-41%

The change in number sold increased from 2018 to 2019 for two-year olds and broodmares while there was a decrease in number sold for yearlings and weanlings. Overall, the number sold decreased 0.3% from 2018 to 2019.

Six percent of the 2019 North American foal crop sold at 2019 public auctions as weanlings, and 30% of the 2018 North American foal crop sold at public auctions in 2019 as yearlings. The following shows the consistency of these numbers over the last nine years:

	2011	2012	2013	2014	2015	2016	2017	2018	2019
Weanlings	5%	5%	5%	5%	5%	5%	5%	6%	6%
Yearlings	26%	25%	32%	28%	28%	28%	27%	29%	30%

From Graph III, we can see substantial increases in average prices for each category in 2013, mixed results in 2014 through 2016, increases in each category in 2017, and mixed results in 2018 and 2019:

	2013	2014	2015	2016	2017	2018	2019
Broodmares	+30%	-9%	-11%	+12%	+8%	-1%	-4%
Two-year-olds	+22%	0%	+12%	-4%	+18%	+3%	+6%
Yearlings	+14%	+5%	+7%	-4%	+16%	+12%	-2%
Weanlings	+32%	+3%	+17%	-7%	+8%	-1%	-7%

We can see from this table that average prices for two-year-olds declined only once—and for yearlings only twice—during the seven years shown, and each such decrease was relatively small.

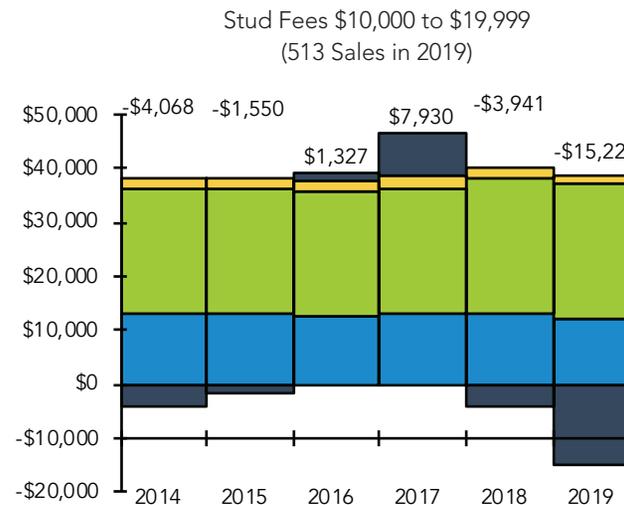
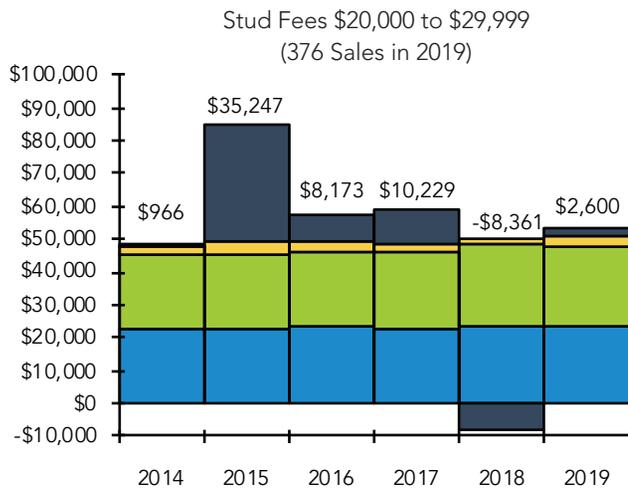
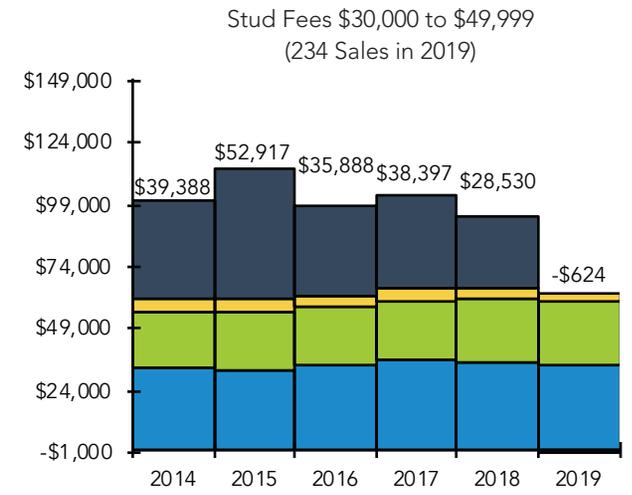
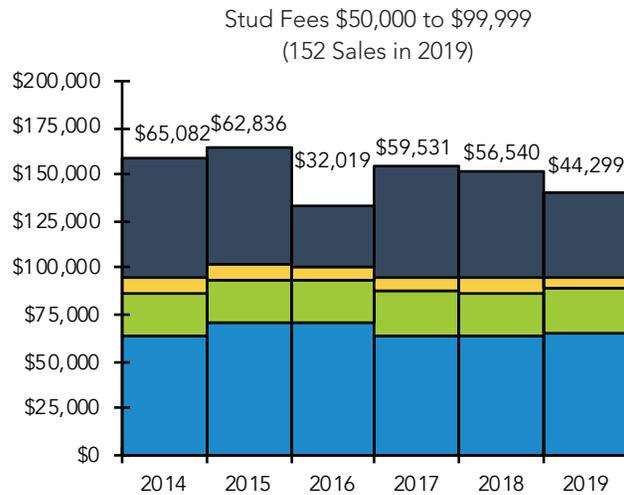
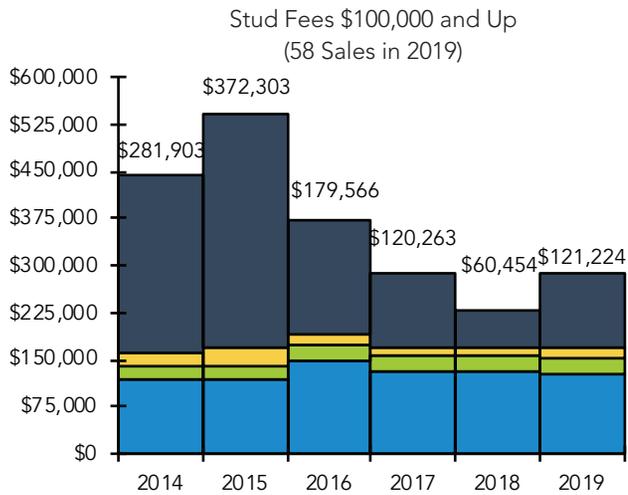
Graph IV

Breakdown of Sale Price of Yearlings into Cost Components (Stud Fees, Sales Commissions, and Mare and Foal Board and Incidental Expenses) Balance Available to Cover Cost of Mare and Profit YEARLINGS — By Stud Fee Range, 2014 to 2019



Graph V

Breakdown of Sale Price of Weanlings into Cost Components
 (Stud Fees, Sales Commissions, and Mare and Foal Board and Incidental Expenses)
 Balance Available to Cover Cost of Mare and Profit
WEANLINGS — By Stud Fee Range, 2014 to 2019



- Balance after other costs to cover cost of mare and profit
- Sales commissions
- Mare and foal board and other incidental expenses
- Stud fees

Note: Dollar figures above bars on bar graphs represent amounts remaining after other costs to cover capital costs associated with mare and profit.

Underlying Data from The Thoroughbred Daily News

We have analyzed data which shows the relationship of North American yearling (Graph IV) and weanling (Graph V) sales results to stud fee costs over 2014 to 2019, segmented by stud fee ranges for the breeding year. These graphs show the portion of average sales price consumed by related stud fees, and add two other significant components of cost: a 5% sales commission and the estimated cost of boarding and caring for the mare for one year and her foal until assumed sale dates (November for weanlings and September for yearlings). For this latter cost, primarily board and veterinary care, we used \$40,000 and \$25,000 for yearlings and weanlings, respectively. We have not included sales tax on stud fees because not all states tax stud fees and because stallion owners who use their own seasons are not subject to this tax. The balance of average sales prices not consumed by the specific costs outlined above is available principally to cover the cost of using the mare for a year to produce the foal and, hopefully, to provide a profit to the breeder. Note that this analysis does not take into account costs associated with barren mares and lost foals. Further note, by using a cutoff of \$10,000 stud fee for this analysis, our analysis does not cover the entire yearling and weanling markets.

For purposes of this analysis, we are treating as weanlings those “short yearlings” that are sold in January and February following their foaling year.

The table below shows the dollar and percentage changes from 2018 to 2019 in the amount of selling price available to cover the cost of using the mare and to produce a profit, broken down by the stud fee ranges shown in the graphs.

Changes from 2018 to 2019 in Selling Price Available for Mare Cost and Profit

Stud Fee Range	Yearlings				Weanlings			
	Increase <Decrease>	% Change	2019	2018	Increase <Decrease>	% Change	2019	2018
\$100,000 and up	\$6,148	4%	\$153,815	\$147,667	\$60,770	100%	\$121,224	\$60,454
\$50,000 to \$99,999	<\$5,110>	-6%	\$84,519	\$89,629	<\$12,241>	-22%	\$44,299	\$56,540
\$30,000 to \$49,999	<\$32,290>	-46%	\$38,451	\$70,741	<\$29,154>	NM	<\$624>	\$28,530
\$20,000 to \$29,999	<\$5,791>	NM	<\$294>	\$5,497	\$10,961	NM	\$2,600	<\$8,361>
\$10,000 to \$19,999	<\$4,460>	NM	<\$14,572>	<\$10,112>	<\$11,280>	NM	<\$15,221>	<\$3,941>

NM = not meaningful

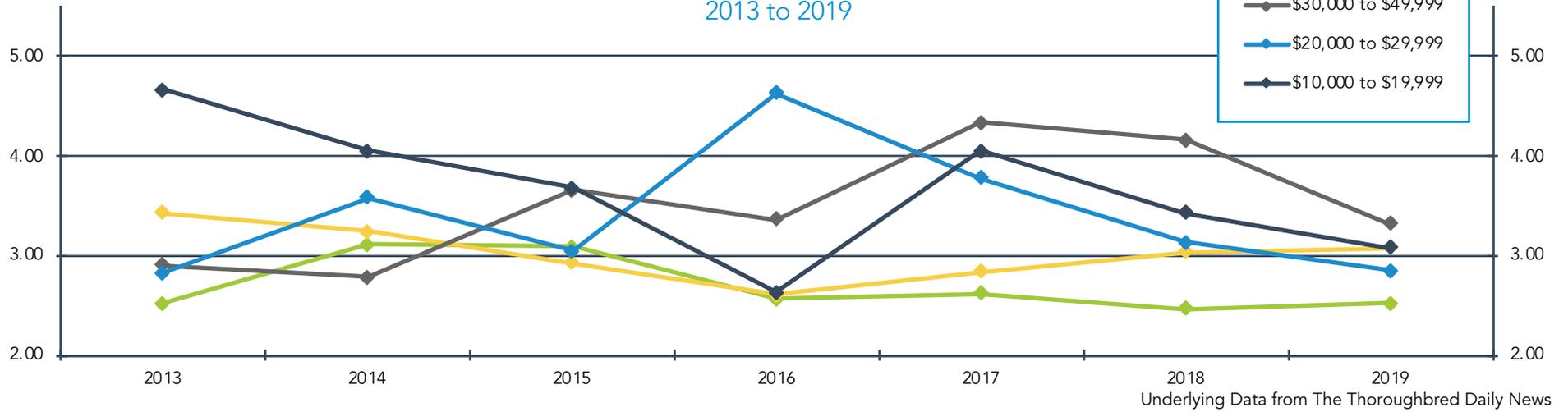
In Graph IV (regarding yearlings), in what we loosely call “profitability,” decreases occurred in each stud fee range in 2019 except over \$100,000.

In Graph V (regarding weanlings), contributions to mare cost recovery and profit margin decreased in 2019 in relation to 2018 in each stud fee range shown, except over \$100,000 and \$20,000 to \$29,999.

Whether for yearlings or weanlings, the averages show significant losses for the sires whose fees were in the \$10,000 to \$19,999 range in the breeding year.

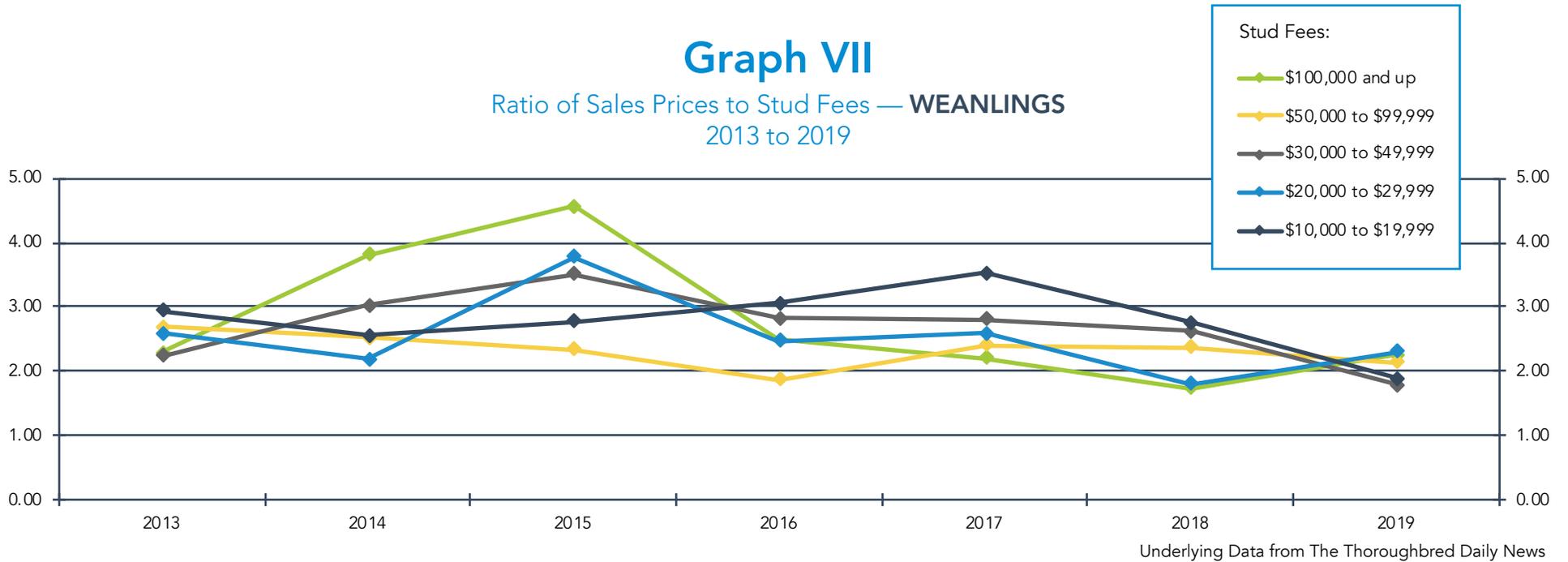
Graph VI

Ratio of Sales Prices to Stud Fees — YEARLINGS
2013 to 2019



Graph VII

Ratio of Sales Prices to Stud Fees — WEANLINGS
2013 to 2019



Considerable published data is available to breeders on stud fee multiples (sales price of yearling or weanling as a ratio of related stud fees) on a stallion-by-stallion basis. We have taken the data that groups stallions by stud fee ranges and looked in Graphs VI and VII at trends over time and relationships among different stud fee ranges. In doing this analysis, the stud fees are from the breeding year, not the sales year. The sales data again includes January and February yearling sales as if these “short yearlings” were weanlings.

The following table shows stud fee multiples for yearlings sold in 2015 through 2019, by stud fee range:

Stud Fee	2015	2016	2017	2018	2019	5-year average
\$100,000 and up	3.1	2.6	2.6	2.5	2.5	2.6
\$50,000 to \$99,999	2.9	2.6	2.8	3.0	3.1	2.9
\$30,000 to \$49,999	3.7	3.4	4.3	4.1	3.3	3.8
\$20,000 to \$29,999	3.0	4.6	3.8	3.1	2.8	3.5
\$10,000 to \$19,999	3.7	2.6	4.0	3.4	3.1	3.4

2019 multiples exceeded the five-year averages only for stud fees in the \$50,000 to \$99,999 range.

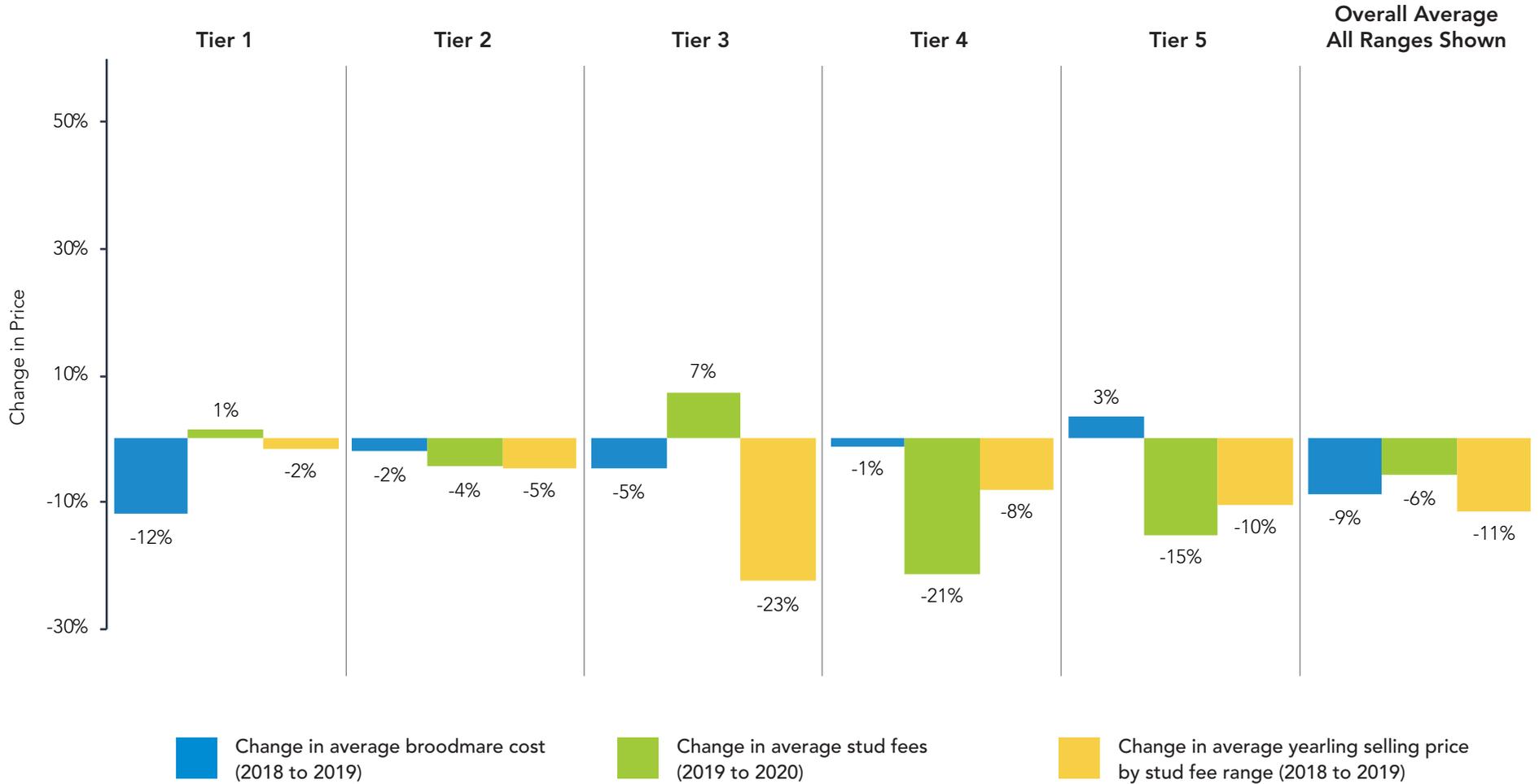
The table below shows stud fee multiples for weanlings sold in 2015 through 2019, by stud fee range:

Stud Fee	2015	2016	2017	2018	2019	5-year average
\$100,000 and up	4.6	2.5	2.2	1.7	2.2	2.6
\$50,000 to \$99,999	2.3	1.9	2.4	2.4	2.1	2.2
\$30,000 to \$49,999	3.5	2.8	2.8	2.6	1.8	2.7
\$20,000 to \$29,999	3.8	2.5	2.6	1.8	2.3	2.6
\$10,000 to \$19,999	2.8	3.1	3.5	2.7	1.9	2.8

The 2019 multiples were below the five-year average multiple for each stud fee range, with the most noticeable sub-averages experienced in ranges from \$30,000 to \$49,999 and \$10,000 to \$19,999.

Graph VIII

Changes in Production Costs and Yearling Selling Prices for Breeders by Stud Fee and Mare Cost Ranges



Data from The Blood-Horse, Keeneland, Fasig-Tipton, and The Thoroughbred Daily News

In Graph VIII, we provide insight into a critical question for breeders:

Are your production costs increasing at a higher or lower rate than the prices you're receiving for your products?

For costs of production, we focus on the two major elements: broodmare costs — based on public auction prices — and stud fees. For sales prices of breeders' products, we examine auction prices of yearlings (excluding January and February sale yearlings, which are more like the prior year November weanling sales than the September yearling sales).

The analysis is based on current production costs and current sales prices and does not attempt to correlate sales prices with the costs of producing these foal crops. In other words, we are focusing on current costs (replacement costs) and current sales prices.

Specifically, we are measuring changes in stud fees by the change in published stud fees by stallion from 2019 to 2020. For broodmares, we are measuring the change in this cost by reference to changes in average auction prices from 2018 to 2019. Similarly, the change in sales price of yearlings is measured by reference to average auction prices from 2018 to 2019.

We recognize that by using published stud fees, we may not be capturing actual fee data as accurately as we would prefer, but we believe that our use of published fees year to year should reasonably capture annual price-level changes.

We segment our analysis into five tiers:

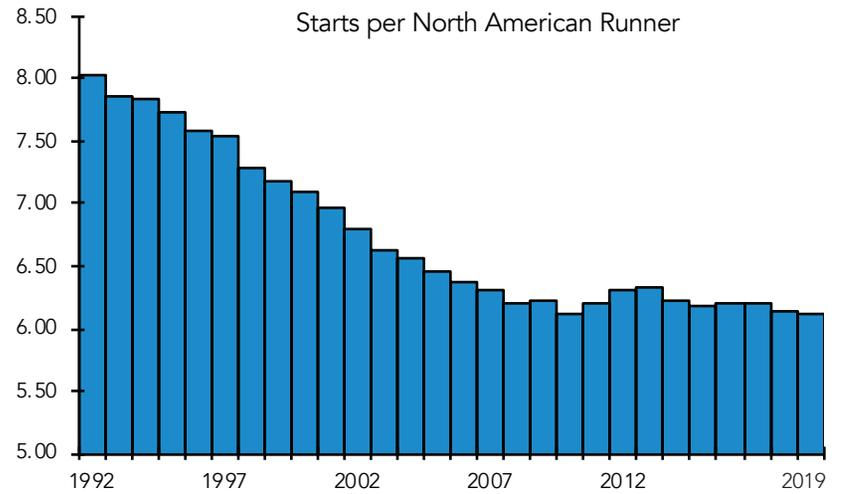
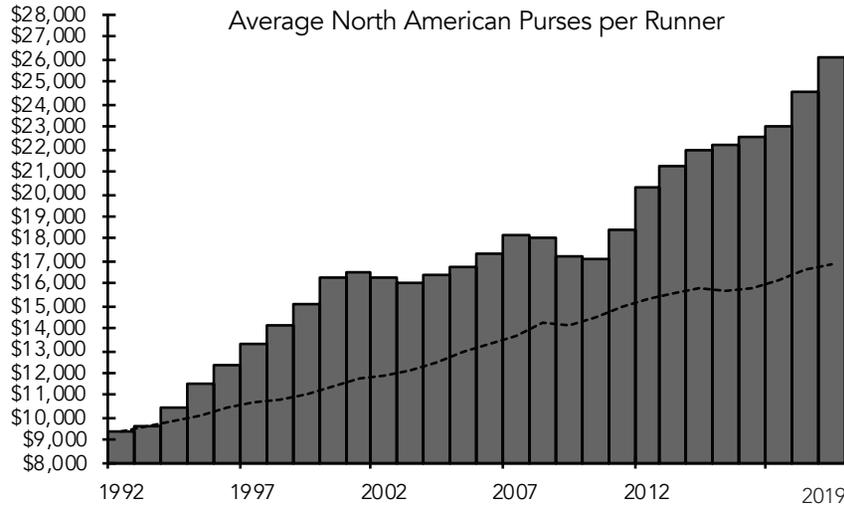
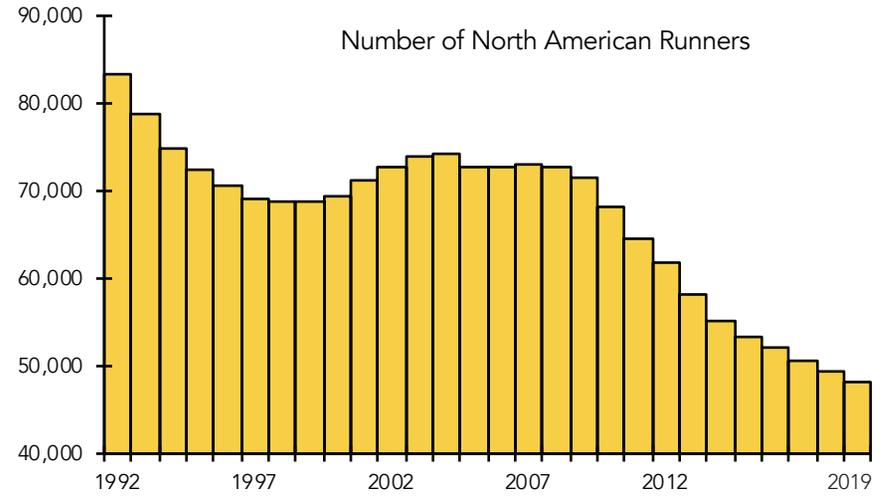
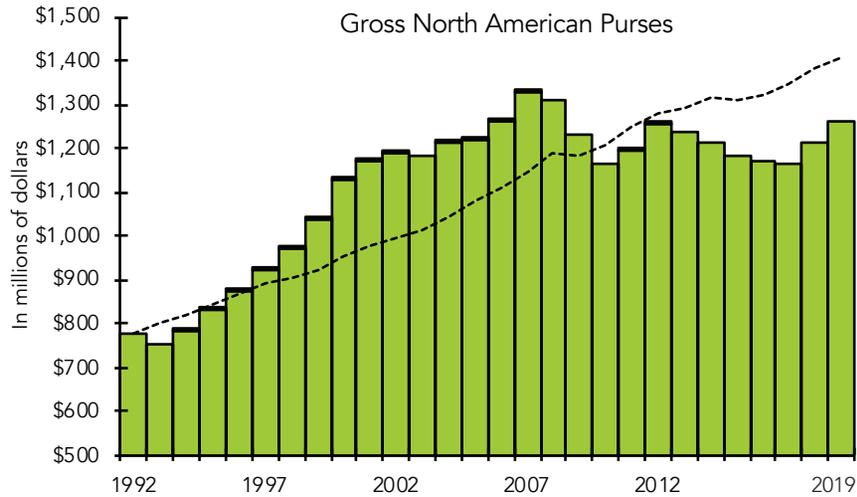
Tier	Stallion cost — stud fees of:	Mare cost — prices for reported 2019 sales at public auction:	Sales prices — yearlings sold at public auction and produced from stallions with these fees (in the breeding year):
1	\$100,000 +	Top decile	\$100,000 +
2	\$50,000-99,999	2nd decile	\$50,000-99,999
3	\$30,000-49,999	3rd decile	\$30,000-49,999
4	\$20,000-29,999	4th decile	\$20,000-29,999
5	\$10,000-19,999	5th decile	\$10,000-19,999

We also show the aggregate changing cost and price levels for all five tiers we analyzed.

Our analysis shows that capital costs associated with buying or retaining broodmares have declined (down 9% overall for the market segments we analyzed), and stud fee costs also have declined (down overall by 6%). Yearling prices declined 11%. Stating the obvious, the reduced average yearling sales prices for all tiers to the extent it exceeds reduced prices for mares and stallion access is financially unhealthy for breeders.

Graph IX

Racing Purses and Number of Horses Racing 1992 to 2019



--- Inflation Adjustment

Data from The Jockey Club Fact Book

After five consecutive years of declines in gross purses, 2018 and 2019 showed increases. Note the generally favorable upward trend from the early 1990s through 2007. None of the post-2007 amounts have reached the 2007 level.

The number of runners (number which started in at least one race in the year) was relatively stable from 2001 through 2008, but has declined steadily from 2009 through 2019, including a 2.1% decline from 2018 to 2019. From 1992 to 2019, the number of runners declined 42% (from 83,433 to 48,330).

From 1992 to 2007, average purses per runner increased 95%, from \$9,300 to \$18,200. But, in 2008 through 2010, the declines in gross purses and the smaller relative declines in number of runners resulted in a decline in average purses per runner of 6% from 2007 to 2010. However, with still fewer runners competing in 2011 and 2012 for more purse money, the 2011 average purse per runner increased to \$18,500, followed by a 2012 increase to \$20,300. Then, although gross purses decreased in 2013 through 2017, the relatively greater decreases in number of runners pushed the 2013 through 2017 average purses per runner to \$21,200, \$21,900, \$22,200, \$22,500, and \$23,000. The trend continued in 2018 and 2019, as average purses per runner increased to \$26,100 and \$24,500, respectively.

Average purses per runner from 1992 to 2019 have increased 180% (the good news for racehorse owners), but much less than the 264% increase in the average cost of purchasing yearlings, the 275% increase in the average cost of purchasing weanlings, and the 396% increase in the cost of purchasing two-year-olds over the same period.

Starts per runner remained stable in 2019. Note the clear decreasing trend from the early 1990s. In 1992, the highest of the 27 years considered, average starts per runner were just over eight; in 2019, the average was 6.1. The number of starts per runner has stabilized over the last 11 years, staying within a range of 6.1 to 6.3.

For gross purses and average purses per runner, we show inflation lines starting with 1992, the earliest year we show. Gross purses for 2019 continue below the inflation-adjusted amount. Average purses per runner have exceeded the inflation-adjusted base throughout the period we show.

Is That Transaction Subject to Sales or Use Tax?

Making sense of complexities while buying and selling horses for racing and breeding

In the United States more than 10,000 state and local jurisdictions impose sales and use taxes. The majority of the taxing jurisdictions are city, county, or other local governments, as only 45 states and the District of Columbia impose the taxes. Alaska, Delaware, Montana, New Hampshire, and Oregon do not impose a sales or use tax, although Alaska permits local jurisdictions to levy the taxes. Based on the number of taxing jurisdictions, sales and use taxes account for approximately 25% of total state and local tax collections.

Every taxing jurisdiction has its own set of laws related to sales and use taxes. When that fact is combined with the number of taxing jurisdictions, it comes as no surprise that sales and use taxes are riddled with complexities. This article focuses on making sense of those complexities in the context of buying and selling horses for racing and breeding, with emphasis on the states of California, Florida, Kentucky, and New York.

IN THE BEGINNING

Understanding sales and use taxation of horse transactions begins with a general understanding of sales and use taxes. These taxes are imposed on a particular "transaction," i.e., a transfer of a taxable product or service for a consideration. In particular, sales taxes apply to retail sales of tangible personal property, digital property, and some specifically enumerated services. Tangible personal property includes property that might be seen, weighed, measured, felt, or touched, or that is in any other manner perceptible to the senses. Because horses fall within this definition, sales of horses are taxable unless the transaction qualifies for a specific statutory exemption.

Jurisdictions that impose a sales tax also impose a complementary use tax, which is imposed on the storage, use, or other consumption of taxable property in a state if no sales tax was paid to that state when the property was purchased. Most states allow a credit against the use tax due for sales tax paid to another state at the time of purchase. Because horses might be purchased in one state and trained, boarded, or raced in other states, use tax is especially relevant in the equine industry. Unlike the sales tax, which the seller generally is required to collect from the purchaser and remit to the taxing authority, the use tax typically is the obligation of the purchaser.

All gross receipts derived from the retail sale of tangible personal property, other than sales for resale, are presumed taxable. However, states and localities often carve out exemptions from tax for certain types of transactions. In most circumstances, the seller must obtain and maintain in its records a properly completed exemption certificate from the purchaser as proof that the sale is exempt from tax. Examples of types of exempt transactions in various states include sales and purchases: (a) in interstate or foreign commerce; (b) of horses for breeding purposes; and (c) of racehorses. The following sections explore how these exemptions apply in California, Florida, Kentucky, and New York.

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INTERSTATE AND FOREIGN COMMERCE

In all four states, sales in interstate and foreign commerce are exempt from tax. For this exemption to apply, the purchaser must take possession of the horse outside the taxing state. Buyers and sellers can take advantage of this exemption by structuring the transaction so that the seller is obligated, as a condition of the sale, to ship the horse by common carrier to the purchaser at a point outside the state. For example, if a seller in Kentucky makes physical delivery of a horse by common carrier to a purchaser in New York, the sale is exempt from Kentucky's sales tax. However, New York's use tax might apply to the transaction.

HORSES PURCHASED FOR BREEDING

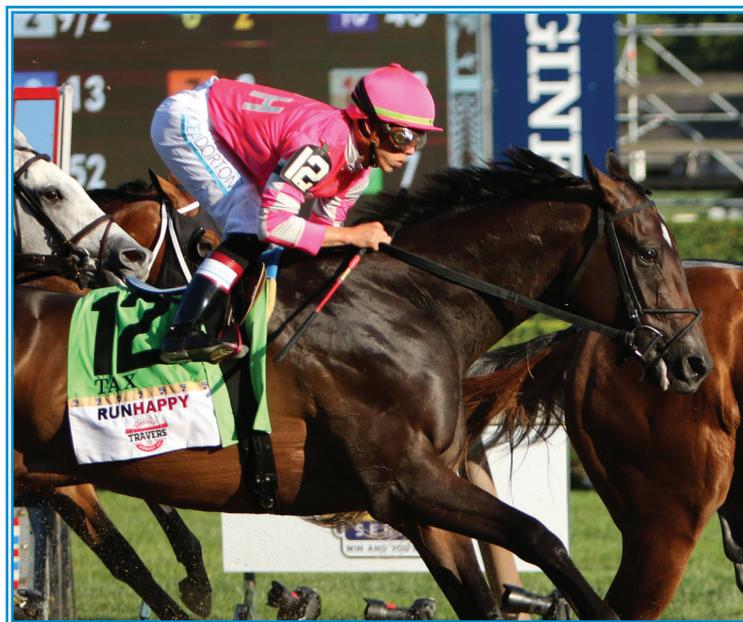
California, Florida, Kentucky, and New York all offer preferential treatment to horses purchased for breeding purposes. The exemptions for sales of horses for breeding purposes are broader in Florida and Kentucky because the exemptions in California and New York are limited to racehorses purchased for the purpose of breeding. Additionally, California's exemption does not apply to local taxes.

In California and Kentucky, the purchaser must intend to use the horse solely for breeding purposes to qualify for the exemption. Guidance issued by New York is conflicting as to whether the purchaser must intend to use the horse exclusively (i.e., 100%) or predominately (i.e., more than 50%) for breeding purposes. Florida law requires only that the horse be purchased for breeding purposes and does not mandate that this be the purchaser's sole intent.

Sales of horses by the breeder also are exempt from tax in Florida. This exemption applies even if a horse is registered with a breeders or registry association prior to the sale and the sale takes place at a show or race meeting, as long as the sale is made within Florida by the original breeder.

RACEHORSES

New York offers the most favorable treatment when it comes to racehorses. In New York the purchase of a Thoroughbred or Standardbred racehorse is exempt from tax if the horse is: (1) registered with The Jockey Club, the United States Trotting Association, or the National Steeplechase and Hunt Association (or is no more than 24 months old and eligible to be registered with one of these associations), and (2) purchased with the intent of entering the horse in a racing event in which pari-mutuel wagering is authorized by law. Sales of racehorses are taxable in California, Florida, and Kentucky. However, Kentucky exempts the sale of horses less than 2 years old at the time of sale, provided the sale is made to a non-resident of Kentucky. A non-resident includes an individual who is not a resident of Kentucky, as well as a business that is not commercially domiciled in the Commonwealth.



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USE TAX CONSIDERATIONS

Finally, because horses often are transported to multiple states for training, racing, or other purposes, special consideration should be paid to the use tax laws of each state. In some states, including California and Florida, property purchased and used outside of the state for a certain length of time might be exempt from use tax if subsequently brought into the state. For example, property used more than 90 days from the date of purchase to the date of entry into California is accepted as proof that the property was not purchased for use in California and, thus, is not subject to use tax in California. Likewise, under Florida law, property used in another state for six months or more before being imported into Florida is presumed not to have been purchased for use in Florida.

Kentucky and New York have equine-specific use tax exemptions. Kentucky exempts from tax the temporary use of horses in the state for purposes of racing, exhibiting, or performing. In New York, no use tax is due if a horse is purchased outside New York and brought into the state for the purpose of entering racing events or preparing for such events if the horse is not entered into racing events on more than five days in any one calendar year.

HOW THIS WORKS IN PRACTICE

The interplay between the sales and use tax laws of various states can be illustrated best by example. Suppose a California resident purchases a Thoroughbred yearling at an auction in Kentucky and takes delivery in Kentucky. Because the horse is less than 2 years old and the purchaser is a non-resident, no Kentucky sales tax is due on the transaction. However, if the horse is transported to Florida for training within six months of its purchase, a Florida use tax liability would arise. The purchaser could avoid Florida use tax by waiting six months or more before transporting the horse to Florida.

What if the California resident also has a farm in Kentucky where she spends more than half the year? Under these circumstances, Kentucky sales tax would apply to the purchase of the yearling because the purchaser does not qualify as a non-resident of Kentucky. If the horse is shipped to Florida for training within six months of purchase, the purchaser also is liable for Florida use tax. However, she can take a credit against the Florida use tax for the sales tax paid to Kentucky. Because Florida and Kentucky both impose tax at the rate of 6%, the credit for sales tax paid to Kentucky would fully offset the purchaser's Florida use tax liability.

These are just a few examples of the impact of sales and use taxes on the equine industry. More complex scenarios arise when multiple parties, several states, and local taxes factor into the equation. Individuals and businesses engaged in the buying and selling of horses should consider sales and use taxes before entering into any transaction to avoid an unpleasant tax surprise down the road.

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