



Executive Summary: Modernizing Kentucky's Local Tax Filing System

Background

- Kentucky businesses must comply with over 400 local occupational and net profits tax jurisdictions.
- Many file hundreds of returns and write hundreds of checks each year—sometimes for just a few dollars.
- The process is time-consuming, expensive, and confusing, particularly for small businesses.
- Some businesses, frustrated by the burden, choose not to comply and accept penalties as a “cost of doing business.”

What HB 253 Proposed (2025 Session)

- Create a working group of stakeholders: businesses, city governments, and county governments.
- Develop a modernized system that would:
 - Allow businesses to file returns online and make a single ACH transfer.
 - Automatically route payments to the appropriate local jurisdictions.
 - Preserve local control over tax rates and payment schedules.
 - Provide jurisdictions with the same information and records they currently receive.
 - Ensure payments are fast, reliable, and auditable.

What We've Learned Since Adjournment

- Ohio's model (7 years in use) → Higher compliance, easier for businesses.
- Tennessee's system → Highly user-friendly, successful.
- Louisville Metro Government's system → Increased compliance, proven in Kentucky.

Goals for 2026 Regular Session

- Reintroduce legislation to create the framework for this system.
- Build a solution that works just as well for local governments as it does for businesses.
- Avoid new bureaucracy—focus on a system that is a shared asset, not a liability.

- Ensure direct, immediate transfers to local governments—not routed through Frankfort.

Why This Matters

- Easier compliance = higher compliance.
- Local governments receive payments faster and more reliably.
- Businesses save time and money, making Kentucky more competitive.
- Everyone wins: stronger compliance, better records, and a fairer system.

Next Step

- We welcome collaboration with local government leaders and members of the Interim Joint Committee on Local Government to ensure this solution meets the needs of all stakeholders.

Tom Underwood
Chairman Kentucky Small Business Caucus
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The Honorable Members
Interim Joint Committee on Local Government
Kentucky General Assembly
Frankfort, Kentucky

Dear Members of the Committee:

In Kentucky, we ask our businesses to comply with more than 400 different local occupational and net profits tax jurisdictions. For many, this means filing hundreds of separate returns and writing hundreds of checks every year. Some of these checks are for just a few dollars—or even less. For small businesses in particular, the administrative burden is overwhelming.

Most businesses do their very best to comply, but the current system is so cumbersome that some decide to take their chances and accept penalties as a cost of doing business. That is bad for compliance, bad for local revenues, and bad for Kentucky's competitiveness.

HB 253, introduced in the 2025 Session, offered a path forward: bring together business leaders, city officials, and county officials to design a system that makes tax compliance simple and reliable. Imagine if businesses could file all their local tax returns online, submit one secure ACH transfer, and have those funds routed directly—and quickly—to each local jurisdiction. At the same time, local governments would continue to receive the same records and information they do today, with the added benefit of faster, more reliable payments and a stronger audit trail.

We know this can work. Ohio has been doing it for seven years, and compliance has gone up. Tennessee has a user-friendly model that businesses like using. Here in Kentucky, Louisville Metro has already proven that an online system increases compliance and cuts red tape.

As we look ahead to the 2026 Session, our goal is to refile this legislation—not to dictate a one-size-fits-all approach, but to give all stakeholders the time and space to build something that works for everyone. Local control over rates and schedules would remain untouched.

At the end of the day, people are more likely to pay when you make it easy for them to do so. We believe this legislation represents an opportunity to strengthen compliance, improve revenue reliability, and make doing business in Kentucky easier.

We would welcome the chance to work with you and your local governments to get this right—for businesses, for cities, and for counties.

Thank you for your time and thoughtful consideration.

Sincerely,

Tom Underwood

A handwritten signature in black ink, appearing to read "Tom Underwood". The signature is fluid and cursive, with the first name "Tom" being more prominent than the last name "Underwood".

Chairman Kentucky Small Business Caucus

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MODERNIZATION OF LOCAL TAX COLLECTION

WHAT IT DOES:

-  It creates a single online portal to pay local payroll and net profits taxes for all jurisdictions with one transaction.
-  The Ongoing system expenses paid for by businesses using the portal.
-  It creates ease of filing and payment, which will likely increase compliance and provide more funds to local governments
-  It requires that remitted funds be deposited to local government accounts within one day.
-  It Places the State Treasurer in charge of the system, as they already handle remittances and fund transfers.
-  It requires the appointment of a steering committee, made up of stakeholders, to develop system design for bidding to third-party programmers.
-  Businesses are not required to use the new system but all local jurisdictions are.
-  It creates a reporting system for local jurisdictions for audit and compliance.
-  It dramatically reduces paperwork and administrative costs for a vast number of Kentucky small businesses.

WHAT IT DOES NOT DO:

-  It does not interfere with home rule. Local governments will still have their abilities to set rates, etc.
-  It does not cost local jurisdictions anything nor is it an unfunded mandate. Fees will be paid by businesses to support the system. Local jurisdictions will receive 100% of the taxes they are due.
-  It does not allow the holding of the local funds by the state. Under the supervision of the State Treasurer, it requires that collections be deposited in the local jurisdictions' accounts the same day as it is received by the system.
-  It does not discourage economic development. In fact, the ease of reporting and transfer will likely encourage compliance and removes a disincentive for new businesses.
-  It does not create a new state bureaucracy. The system is basically a merchant account like most online retailers. There may need to be one or two staffers added to State Treasurer's office for maintenance and oversight.
-  It does not require every business to participate. Local businesses can continue with the current system, should they choose.
-  It does not rush implementation. The bill calls for a steering committee be appointed, made up of stakeholders to work through 2025 to create a basis for an RFI for system development. It then allows all of 2026 for build out and testing until it goes online January 1, 2027.

MODERNIZATION OF LOCAL TAX COLLECTION

The Kentucky CPA Journal, Issue 5, December 20, 2024

"Tax in the Bluegrass: One-Stop Local Occupational License Tax Filing?"

By Mark A. Loyd, JD, CPA

Hundreds of local tax districts in Kentucky impose occupational license taxes on wages and net profits, including counties, cities and school districts. These taxes are widespread across the Commonwealth. For example, approximately three-quarters of Kentucky's 120 counties impose occupational license taxes.

The burden of complying with Kentucky occupational license taxes can be crushing on businesses, especially for small ones. Imagine having to prepare (or pay your CPA to prepare) and file occupational license tax returns in dozens or hundreds of tax districts, instead of just one return. The General Assembly can address this heavy and unnecessary burden on Kentucky businesses.

Multitudes of multijurisdictional occupational license tax filings

Occupational license taxes generally take two forms: taxes on wages and taxes on net profits. The former are imposed on employees, and the latter on businesses. Businesses bear the compliance burdens of both.

Occupational license taxes on wages are imposed on salaries, wages, commissions, and other compensation earned by persons within the local tax district for work done and services performed or rendered in the district, regardless of whether an employee is a resident or nonresident of the district. Employers are required to deduct and withhold occupational license tax from their employees' wages. Employers often have employees in multiple tax districts, even in the same county, for example when the county imposes an occupational license tax and cities within the county impose their own occupational license tax.

Businesses are subject to occupational license taxes imposed on their net profits from activities conducted in the tax district. Businesses operating in multiple districts determine the portion of their net profits to be apportioned to each district using a statutory formula.

Each business must file tax returns in each tax district for withholding and net profits taxes. In limited circumstances, multiple tax districts are centrally administered, typically by a county. However, most of the hundreds of local tax districts require businesses to file tax returns with their district.

The result is that businesses throughout the Commonwealth seeking to be compliant may find themselves filing dozens and sometimes hundreds of tax returns for occupational license tax withholding on their employees' wages and on their business's net profits.

WHAT IT DOES:

- ✓ It creates a single online portal to pay local payroll and net profits taxes for all jurisdictions with one transaction.
- ✓ The Ongoing system expenses paid for by businesses using the portal.
- ✓ It creates ease of filing and payment, which will likely increase compliance and provide more funds to local governments
- ✓ It requires that remitted funds be deposited to local government accounts within one day.
- ✓ It Places the State Treasurer in charge of the system, as they already handle remittances and fund transfers.
- ✓ It requires the appointment of a steering committee, made up of stakeholders, to develop system design for bidding to third-party programmers.
- ✓ Businesses are not required to use the new system but all local jurisdictions are.
- ✓ It creates a reporting system for local jurisdictions for audit and compliance.
- ✓ It dramatically reduces paperwork and administrative costs for a vast number of Kentucky small businesses.

Local occupational license taxes require General Assembly authorization

In Kentucky, for a local tax district to impose an occupational license tax, the General Assembly must first authorize it. State legislative authorization is a prerequisite, required by Section 181 of the Kentucky Constitution.

Over the years, the General Assembly has authorized counties and localities to enact ordinances imposing occupational license taxes on wages and net profits by enacting state statutes like KRS 68.180, KRS 68.197, KRS 68.198, KRS 91.200 and KRS 92.281. School boards may also impose occupational license taxes. KRS 160.605.

The General Assembly can and has imposed conditions and limitations on tax districts' imposition of occupational license taxes. For example, enabling statutes may include limitations on the rate of tax, generally in the form of a "not to exceed" provision.

Uniformity guardrails for occupational license taxes

The General Assembly has also enacted statutes providing uniformity guardrails for occupational license taxes. These may be found in KRS 67.750 to 67.795.

For example, net profits are determined by reference to taxable income under the federal Internal Revenue Code. KRS 67.750(7)&(8). And, "For purposes of KRS 67.750 to 67.790, computations of gross income and deductions therefrom, gross receipts or sales, and deductions therefrom, accounting methods, and accounting procedures shall be as nearly as practicable identical with those required for federal income tax purposes." KRS 67.760(1).

Another example of statutorily required uniformity is the standard apportionment formula mandated by KRS 67.753. Businesses with payroll and sales in more than one tax district generally apportion their net profits by applying an apportionment percentage comprised of an equally weighted payroll factor (with a numerator of payroll in the district and a denominator of payroll everywhere) and a sales factor (with a numerator of sales in the district and a denominator of sales everywhere). KRS 67.753.

If the standard apportionment percentage does not fairly represent the extent of the business entity's activity in the tax district, the business entity may petition the tax district or the tax district may require alternative apportionment. KRS 67.753.

Interestingly, the tax base, apportionment formula, and return filing methodology for occupational license taxes are different from those for Kentucky income tax. For example, the Internal Revenue Code reference in KRS 67.750 is December 31, 2008, and the reference in KRS 141.010 for Kentucky income taxes is January 1, 2024.

WHAT IT DOES NOT DO:

-  It does not interfere with home rule. Local governments will still have their abilities to set rates, etc.
-  It does not cost local jurisdictions anything nor is it an unfunded mandate. Fees will be paid by businesses to support the system. Local jurisdictions will receive 100% of the taxes they are due.
-  It does not allow the holding of the local funds by the state. Under the supervision of the State Treasurer, it requires that collections be deposited in the local jurisdictions' accounts the same day as it is received by the system.
-  It does not discourage economic development. In fact, the ease of reporting and transfer will likely encourage compliance and removes a disincentive for new businesses.
-  It does not create a new state bureaucracy. The system is basically a merchant account like most online retailers. There may need to be one or two staffers added to State Treasurer's office for maintenance and oversight.
-  It does not require every business to participate. Local businesses can continue with the current system, should they choose.
-  It does not rush implementation. The bill calls for a steering committee be appointed, made up of stakeholders to work through 2025 to create a basis for an RFI for system development. It then allows all of 2026 for build out and testing until it goes online January 1, 2027.

Another difference is that occupational license tax is apportioned using a two-factor apportionment formula and Kentucky income tax is apportioned using a single sales factor apportionment percentage using market-based sourcing. Compare KRS 67.753, with KRS 141.120. Kentucky has also adopted unitary filing for state income tax but occupational license tax net profits tax returns are filed on a separate entity basis.

Moving toward statewide one-stop filing

The uniformity guardrails went into effect in 2008. KRS 67.795. They were first introduced in 2003. Ky. Acts, 2003 c 117, § 24. This was a significant step forward.

Since 2012, tax districts have been mandated by KRS 67.766 to provide a copy of tax return forms and ordinances to the Kentucky Secretary of State. These are available at <https://web.sos.ky.gov/occupationaltax/>. The Secretary of State's website also has available a Form OL-3 Kentucky Standard Local Occupational License Fee Return.

Prior to the development of the Secretary of State's return and ordinance repository, there was no official one-stop place to obtain local occupational license tax return forms or ordinances. But, now the building blocks are in place for one-stop filing.

The streamlined approach

Centralized filing is the norm in the 21st century for sales taxes; states like Indiana and Ohio require centralized filing of local income taxes, according to the Tax Foundation, The Efficiency of State Administration of Local Taxes (Dec. 13, 2022).

As to sales taxes, according to the Streamlined Sales Tax Governing Board, Inc., "The purpose of the SSUTA [Streamlined Sales and Use Tax Agreement] is to provide a road map for states who want to simplify and modernize sales and use tax administration in their states to substantially reduce the burden of tax compliance." About Streamlined FAQs (available at www.streamlinedsalestax.org).

The first thing on the list for simplifying and modernizing tax administration to substantially reduce the burden of tax compliance is - state-level administration.

The General Assembly has taken steps over the years in the direction of streamlining occupational license taxes. For example, the General Assembly enacted uniformity provisions for the tax base and definitions in KRS Chapter 67. They enacted a central repository of tax return forms and ordinances. They have also enacted tax rate limitations. The next logical step is a one-stop filing solution.

Local "income" taxes, not an afterthought

Local occupational taxes, especially on wages, have become even more significant, especially as the Kentucky individual income tax rate is now 4 percent and potentially headed toward 3.5 percent, 3 percent and perhaps lower. For example, in Jefferson County with a combined county rate of 2.2 percent, the rate can be 3.2 percent in some cities that impose their own 1 percent tax.

Businesses, their owners, officers, and employees have always found Kentucky's local occupational taxes to be a constraint on growth and expansion. When they make decisions about where they locate, they can do simple math. And, when the complexity and cost of compliance are factored in, Kentucky localities must streamline compliance with local occupational license taxes with a one-stop filing solution.

"Rebellions are built on hope." Jyn Erso in Rogue One: A Star Wars Story (2016).

The General Assembly has the power to streamline local occupational license tax compliance in Kentucky by requiring a one-stop filing solution. Without the General Assembly's authorization, local tax districts cannot impose occupational license taxes. Limits on rates, uniformity guardrails and a one-stop repository of returns and ordinances are all steps on the path to finally streamlining a burden that Kentucky businesses have faced long enough. Is not now the time for Kentucky local occupational tax compliance to come into the 21st century?

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