COMMONWEALTH OF KENTUCKY STATE FISCAL NOTE STATEMENT
LEGISLATIVE RESEARCH COMMISSION
2018 REGULAR SESSION

MEASURE

2018 BR NUMBER **1635** **HOUSE** BILL NUMBER **436**

RESOLUTION NUMBER_____ AMENDMENT NUMBER _____

SUBJECT/TITLE An ACT relating to the taxation of rental equipment.

SPONSOR Representative Gibbons Prunty

NOTE SUMMARY

FISCAL ANALYSIS: ☒ IMPACT ☐ NO IMPACT ☐ INDETERMINABLE IMPACT

LEVEL(S) OF IMPACT: ☒ STATE ☒ LOCAL ☐ FEDERAL

BUDGET UNIT(S) IMPACT: _____

FUND(S) IMPACT: ☒ GENERAL ☐ ROAD ☐ FEDERAL ☐ RESTRICTED AGENCY _____ ☒ OTHER

FISCAL SUMMARY

FISCAL ESTIMATES	2017-2018	2018-2019	2019-2020	ANNUAL IMPACT AT FULL IMPLEMENTATION
REVENUES		(Indeterminable)	(Indeterminable)	(Indeterminable)
EXPENDITURES				
NET EFFECT		(Indeterminable)	(Indeterminable)	(Indeterminable)

( ) indicates a decrease/negative

MEASURE'S PURPOSE: HB 436 defines specific equipment held for sale or rental in a retailer's inventory as equipment rental inventory and assigns a state ad valorem tax rate of five cents per one hundred dollars of assessed valuation to that equipment. HB 436 also defines an equipment rental company and allows that company the option to charge a one and one-half percent tangible personal property tax recovery fee on equipment rental inventory. The fee is excluded from the computation of sales and use taxes and is directed to be used for payment of the company's tangible personal property taxes. Any excess funds collected from the fee are to be distributed among the various taxing jurisdictions imposing tangible personal property taxes on the company.

PROVISIONS/MECHANICS: Section 1 of the bill defines equipment rental inventory. Equipment rental inventory is defined as machinery and equipment held in a retailer's inventory for sale or rental without an operator and primarily used for construction, mining, forestry, or industrial purposes; the attachments, ancillary equipment, and tools held in a retailer's inventory for sale or rental and used with the machinery and equipment; and equipment held in a retailer's inventory for sale or rental and used solely to set up or host events or banquets.

Section 2 of the bill adds equipment rental inventory to the list of property that is taxed at a five cents per one hundred dollars of assessed valuation for state ad valorem taxation.

Section 3 of the bill creates a new section in KRS Chapter 134. In this section, equipment rental company is defined as an entity engaged in a line of business described in the NAICS codes 532412 and 532310. It also defines rental agreement to be an agreement under which rental equipment is rented for a period of 365 days or less or under a contract with unlimited terms. Established within this section is an optional tangible property tax recovery fee set at a rate of one and one-half percent of the total amount charged by the equipment rental company for equipment rental inventory rented under a rental agreement. This fee is exclusive of any taxes, fees, charges for delivery or pick up, damage waiver fees, environmental fees, or other separately stated ancillary fees or charges and must be separately stated in the rental agreement or rental invoice. This section allows an exemption of the fee on rental agreements with government, educational, charitable, and religious entities. It also explains the use and payment requirements of the fee. The fee is to be used for payment of the equipment rental company's tangible personal property taxes and any excess funds generated from the fee shall be distributed among the various taxing jurisdictions imposing tangible personal property taxes on the company.

Section 4 of the bill excludes the fee from the gross receipts computation for sales and use tax purposes. This provision exempts the fee from having sales and use tax applied to it.

FISCAL EXPLANATION: Typically, rental equipment as described in the definition of equipment rental inventory is taxed for tangible property tax purposes at a state rate of forty-five cents per one hundred dollars of assessed valuation. HB 436 lowers this tax rate to five cents per one hundred dollars of assessed valuation. The reporting of rental equipment for tangible personal property tax is not a separately stated item on the tax return. Therefore, the Kentucky Department of Revenue does not track the amount of rental equipment in Kentucky or the tax dollars generated from it. The fiscal impact of the lower state tax rate is expected to be negative, but the exact dollar amount is unknown.

The tangible personal property tax recovery fee is an optional fee that a rental company may charge. This fee is to be used to pay the tangible personal property taxes owed by the rental company. If the fee is not sufficient to cover the taxes, the rental company must still pay the remaining taxes owed. In this situation, there would be no fiscal impact to the state. However, if the fee generates more money than what is needed to cover the taxes, the rental company cannot keep the additional money. HB 436 says the rental company shall distribute the additional money to the various taxing jurisdictions imposing tangible personal property tax against the rental company for the equipment rental inventory. In this situation, the rental company would be paying more than what is owed for their tangible personal property taxes resulting in a positive fiscal impact for the state. Since the tangible personal property tax recovery fee is an optional fee and there is no data available to determine if the one and one-half percent fee would result in more funds than the amount needed to cover the rental company's tangible personal property tax owed, the fiscal impact of this provision is unknown.

HB 436 exempts from sales and use tax gross receipts derived from the tangible personal property tax recovery fee. Kentucky is a Streamlined Sales Tax State. It is unclear if the exemption of the tangible personal property tax recovery fee would cause Kentucky to be in violation of the Streamlined Sales Tax Agreement. If challenged and a violation is determined, the state could possibly lose over $30,000,000 of sales and use tax revenue annually.

DATA SOURCE(S): **LRC Staff, Kentucky Department of Revenue**
PREPARER: **Cynthia Brown** **NOTE NUMBER**: **130** **REVIEW**: **JAB** **DATE**: **3/7/2018**

LRC 2018-BR1635-HB436