

Guidelines:

Kentucky Small Business Tax Credit (KSBTC)

July 2018

The Kentucky Small Business Tax Credit (KSBTC) Program, authorized under Kentucky Revised Statute (KRS) [154.60](#), allows eligible small businesses paying taxes imposed by KRS [141.020](#) (income tax on individuals), [141.040](#) (corporation income tax), or [141.0401](#) (limited liability entity tax) to apply for a Kentucky state income tax credit. Subject to a statutory limit of \$3,000,000 per state fiscal year, this program provides a non-refundable state income tax credit between \$3,500 - \$25,000 for small businesses that create and fill one or more Eligible Positions and invest \$5,000 or more in qualifying equipment or technology. Qualified applicants are eligible to receive a tax credit in an amount not to exceed the lesser of: 1) \$3,500 per Eligible Position; or 2) the rounded eligible dollar amount invested in qualifying equipment or technology. Applicants are also subject to a \$25,000 maximum tax credit cap per applicant for each calendar year.

Eligible Applicants

Any for-profit small business including sole proprietorships, partnerships, limited partnerships, corporations, limited liability companies, joint ventures, associations, or cooperatives that has fifty (50) or fewer full-time employees at the time of application and approved by the Office of Entrepreneurship, with the exception of ineligible business types listed below, is eligible to apply.

The following business types are ineligible for this program:

- Businesses engaged in any type of illegal activity;
- Businesses in default on any federal, state, or local taxes; not in good standing with the Kentucky Secretary of State's office (if required to be registered with that office); or that do not hold all current licenses, permits, and registrations necessary to legally operate a business in Kentucky;
- Businesses presenting live performances of a prurient sexual nature or deriving more than five percent of annual gross revenue through the sale or rental of products or services, or the depiction of any displays, of a prurient sexual nature;
- Businesses principally engaged in overt religious indoctrination; and
- Businesses deriving more than 50 percent of annual gross revenues from lobbying activities.

Businesses that receive Kentucky Economic Development Finance Authority (KEDFA) approved loans, grants, or tax incentives based on job creation and/or equipment purchases cannot apply for a tax credit through this program if the Eligible Position and/or qualifying equipment included in this application was used as the basis to obtain a tax credit, grant or loan funds under another KEDFA program.

Program Requirements

Small businesses may apply for a tax credit after the following two criteria have been met: 1) at least one Eligible Position has been created and filled for twelve consecutive months; and 2) at least \$5,000 of qualifying equipment or technology has been purchased. Applications must be submitted within the twenty-four month period after the first program requirement occurs (e.g., hire date of initial Eligible Position or purchase of initial qualifying equipment or technology).

Eligible Position

An Eligible Position must meet ALL of the following criteria:

- be filled by an employee subject to the Kentucky income tax imposed by KRS [141.020](#);
- be filled by an employee working an average of thirty-five or more hours per week for a period of twelve consecutive months within the twenty-four month period immediately preceding submission of a KSBTC application;
- pay an average hourly wage of \$10.88 or more per hour; and
- increase the base employment of the small business.

All paid hours (work hours and paid leave hours) should be included when calculating the average hours worked per week to determine if an employee meets the 35-hour minimum requirement to qualify as full-time. If an employee hired in an Eligible Position ceases for any reason to be employed by the small business during the twelve-month employment period, the position may still be eligible for tax credit consideration if another eligible full-time employee is hired to fill the position within forty-five days of the last work day of the first employee.

An employee's average hourly wage includes wages, tips, overtime, bonuses, and commissions as reflected on the employee's federal form W-2 wage and tax statement. Employee benefits should not be included when calculating average hourly wage.

Base Employment

An accurate calculation of the applicant's number of full-time employees on the base employment date is required before determining if a position increases the base employment of the small business. For an initial application, the base employment date is the day prior to the hire date of the employee filling the earliest Eligible Position identified on the company's KSBTC application. "Hire date" is the first day that an eligible employee starts working for the company in an eligible position. For companies that have previously been approved for tax credits through the KSBTC program, base employment is calculated as: 1) the base employment number on the company's first approved KSBTC application; plus 2) the total number of tax-credit Eligible Positions on all approved KSBTC applications.

Base Employment Calculation Example: ABC Company has 10 employees on the payroll as of June 30. One of the employees works part-time. Two other employees live outside of Kentucky and are not subject to Kentucky income tax. On July 1, ABC Company hires a new, full-time employee who is subject to Kentucky income tax. On July 15, another new, full-time employee subject to Kentucky income tax starts working for ABC Company. Both new employees earn more than \$10.88 per hour. If ABC Company submits a first-time KSBTC application for both new positions, its base employment date is June 30 (the day before the earliest eligible new hire start date) and the base employment number on that date is calculated as follows:

10	Total employees on the payroll as of June 30
(1)	Minus one part-time employee (must be full-time to be counted in base employment)
(2)	Minus two full-time employees not subject to Kentucky income tax
= 7	Base full-time employment number

When calculating base employment, only full-time employees subject to Kentucky income tax are to be included in employment counts. Tax credits are potentially available for net increases in eligible employees above the base employment number. It is important to note that a small business may not be able to claim a tax credit for all new employees hired. If employees counted in the base employment calculation leave the small business and are not replaced prior to submitting a KSBTC application, the net employment increase will be reduced, impacting the number of new positions qualifying for a tax credit.

Example: Continuing the example above, assume ABC Company’s two new, full-time employees have been employed for twelve or more consecutive months, so ABC Company is ready to submit a tax credit application. ABC Company’s base employment number, as calculated above, is seven employees. Since the base employment date, ABC Company has added two new, full-time employees, but one of the full-time employees included in the base employment figure has since stopped working at the company and the position has not been backfilled. At the time the KSBTC application is submitted, ABC Company has eight full-time employees calculated as follows:

7	Full-time employees as of the base employment date
2	Plus two eligible, new, full-time employees who started working after the base employment date and have continued working for 12 consecutive months
(1)	Minus one full-time employee included in the base employment calculation who left and has not been replaced
= 8	Full-time employment number as of the KSBTC application date

Although ABC Company created and filled two new positions, only one of the positions is eligible for tax credit consideration because ABC Company’s net eligible employment increase is one (eight full-time employees minus seven base employees). If ABC Company replaces the full-time employee in the base employment prior to the submission of a KSBTC application, its employment as of the application date would be nine and two positions would be eligible for tax credit consideration since the net employment increase above base employment is two (nine full-time employees minus seven base employees).

Qualifying Equipment or Technology

Qualifying equipment or technology must meet ALL of the following criteria:

- tangible property purchased by the applicant small business for use in the business in Kentucky (not for resale or personal use);
- tangible property with an expected useful life of one year or more;
- tangible property purchased within the twenty-four month period immediately preceding the submission of a KSBTC application; and
- tangible property approved by the Office of Entrepreneurship

If it meets all of the above criteria, examples of qualifying equipment or technology include, but are not limited to: computers, equipment, furniture, fixtures, furnishings (excluding artwork), and vehicles titled in the legal name of the small business. Rebates, refunds, tax, labor, installation, delivery and similar charges must be subtracted from the total cost to obtain the eligible cost of qualifying equipment or technology. Real property, buildings, and consumable supplies are excluded from the list of qualifying equipment and technology. The applicant small business must certify that it still owns the qualifying equipment and technology at the time a KSBTC application is submitted.

Invoices and proof of payment must be submitted with the application to verify equipment or technology purchases. Examples of acceptable proof of payment include:

- front and back of the cancelled check used for payment;
- statement from vendor showing payment in full for item; or
- copy of electronic funds transfer statement with sufficient detail to verify payment.

Application Process

Once a small business creates and maintains an Eligible Position for twelve months and invests a minimum of \$5,000 in qualifying equipment or technology, it may apply for a small business tax credit. The small business may choose to submit several qualifying positions on one application as long as all positions and equipment meet eligibility criteria, including the requirement that all qualifying activity occur within the twenty-four months immediately preceding the application submission date.

- Applicant completes the minimum program requirements and submits a KSBTC application and required attachments to the Cabinet for Economic Development's Office of Entrepreneurship (OOE). Applicants are encouraged to work with OOE staff to ensure application completeness and accuracy. Email cedsbsd@ky.gov or call (800) 626-2930 for assistance with the KSBTC application.
- OOE personnel will review the KSBTC application and attachments. If the application is incomplete or requires clarification, OOE staff will contact the applicant for further discussion. Applications meeting or exceeding the minimum program criteria will move to the next step unless one of the program caps has been reached.
- OOE will notify the applicant of preliminary selection for submission to the Kentucky Economic Development Finance Authority (KEDFA) and will confirm the tax credit amount. Applicants are eligible to receive a tax credit not to exceed the lesser of: 1) \$3,500 per Eligible Position; or 2) the total eligible dollar amount invested in qualifying equipment or technology, rounded down to the nearest \$100. An application fee of one percent (1%) of the eligible tax credit amount will be due if the application is selected for submission to KEDFA. Applications will not be submitted to KEDFA until the application fee has been paid.
- If KEDFA approves the recommended small business tax credit, notification will be sent to the applicant and the Kentucky Department of Revenue. Tax credits approved through the KSBTC program must be claimed on the tax return for the taxable year during which the credit was approved. Unused credits may be carried forward up to five years. Small businesses with specific questions regarding applying the tax credits approved through this program and/or what impact the tax credits may have on the company's taxes should contact the [Kentucky Department of Revenue](#) or the company's tax preparer.

Applications will be accepted and processed each fiscal year until the yearly statutory cap of \$3,000,000 in small business tax credits has been awarded.

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