



STATE & FEDERAL TAX PRACTICE

**Timothy Eifler**  
Louisville  
502.560.4208  
Timothy.Eifler@skofirm.com

**Erica L. Horn**  
Lexington  
859.231.3037  
Erica.Horn@skofirm.com

**Jennifer S. Smart**  
Lexington  
859.231.3619  
Jennifer.Smart@skofirm.com

**Jackson White**  
Lexington  
859.231.3617  
Jackson.White@skofirm.com

## Kentucky Circuit Court Affirms Limitation of Tax Exemptions Granted to Charitable Institutions

*Erica L. Horn*

The Kentucky Franklin Circuit Court’s holding in *Interstate Gas Supply, Inc. for use and benefit of Tri-State Healthcare Laundry, Inc. v. Department of Revenue*, Civil Action No. 12-CI-00947 (Franklin Cir. Ct. Sept. 13, 2013), further limits the tax exemptions granted by the Kentucky Constitution. Interstate Gas Supply, Inc. (“IGS”), an Ohio natural gas marketer, sought refunds of use tax collected and paid on sales of natural gas by IGS to Tri-State Healthcare Laundry, Inc. (“Tri-State”). Tri-State is a joint-cooperative laundry association owned by several non-profit charitable hospitals in Northern Kentucky. Tri-State provides centralized laundry services to those hospitals, and Tri-State purchases natural gas from IGS for use in its laundry services. IGS collected use tax on its natural gas sales to Tri-State and remitted the tax to Kentucky.

On October 20, 2009, IGS—on behalf of Tri-State—claimed a refund for all use tax paid on Tri-State’s natural gas purchases. IGS claimed that Tri-State is exempt from use tax pursuant to § 170 of the Kentucky Constitution. Section 170 exempts from taxation institutions of purely public charity and states, in relevant part:

There shall be exempt from taxation public property used for public purposes; places of burial not held for private or corporate profit; real property owned and occupied by, and personal property both tangible and intangible owned by, institutions of religion; institutions of purely public charity . . . Ky. Const. § 170.

Tri-State has previously been determined by the Department of Revenue (“DOR”) to be an institution of “purely public charity.” Nevertheless, the DOR denied IGS’s refund request, claiming that § 170 only extends to property taxes and that the use tax is not a property tax. The DOR relied heavily upon *Children’s Psychiatric Hospital of Northern Kentucky v. Revenue Cabinet*, 989 S.W.2d 583 (Ky. 1999) (“*Children’s Psych.*”), as the basis for its decision. In *Children’s Psych.*, the Supreme Court of Kentucky held that the § 170 exemption does not extend to the Kentucky healthcare provider tax. The DOR claimed that the court’s ruling in *Children’s Psych.* limited all exemptions in § 170 to property taxes.

IGS appealed the DOR’s ruling to the Kentucky Board of Tax Appeals (“KBTA”). IGS argued that the § 170 exemption for purely public charities is *not* limited to *ad valorem* property taxes and instead extends to all revenue raising taxes. IGS relied upon a long line of cases dating back to 1896 holding that, unlike the other exemptions in § 170, the charitable exemption exempts the institution as a whole from taxation and is not limited to property taxes. Three cases cited by IGS specifically recognized an exemption from sales and use taxes for purely public charities. IGS further argued that *Children’s Psych.* was limited to the healthcare provider tax.

Finally, IGS claimed that even if § 170 were limited to property taxes, the incidence of the use tax was so similar to a property tax that it was encompassed within the exemption language.

The KBTA found that *Children's Psych.* was not limited to the provider tax and instead applied to all Kentucky taxes, implicitly overruling any precedent to the contrary. The KBTA specifically found that because the use tax is not levied on a percentage or rate of the value of the property on a regular basis, the use tax is not an *ad valorem* property tax and thus is not within the § 170 charitable exemption. Thus, the KBTA found that IGS was not entitled to a refund on behalf of Tri-State.

IGS appealed the decision of the KBTA to the Franklin Circuit Court. The court affirmed, concluding that § 170 of the Kentucky Constitution only exempts institutions of purely public charity from the payment of property taxes. The court relied upon *Children's Psych.* as the basis for its decision, finding it to be the most recent case interpreting the § 170 charitable exemption. The court found that *Children's Psych.* “specifically held that the exemption only extended to property or ad valorem taxes,” and since the use tax is not a property tax, the exemption did not apply. Therefore, the court found that Tri-State was not entitled to a refund on the use tax paid on its purchases of natural gas from IGS.