

<b>Finance and Administration Cabinet STANDARD PROCEDURE</b>		<b>ISSUED BY:</b> Department of Revenue; Tax Administration
<b>PROCEDURE # 6.11.11</b>	<b>SUBJECT:</b> Annual Adjustment of Tax Interest Rate	
<b>EFFECTIVE DATE:</b> 9/16/11		
<b>CONTACT:</b> Division of Registration & Data Integrity		<b>LOCATION:</b> 501 High St., Station, 20A <b>PHONE:</b> (502) 564-7490

## STATEMENT OF AUTHORITY

1. The Finance and Administration Cabinet's Standard Procedures Manual establishes standard mandatory internal procedures cabinet-wide. These procedures are established in accordance with the Secretary's statutory authority under KRS 42.014 and KRS 12.270 to establish the internal organization and functions of the Cabinet as necessary to perform the duties effectively.
2. The Standard Procedures Manual may only be revised in accordance with the process outlined in Standard Procedure #1.1 entitled: "Finance Standard Procedures and Manual".

### I. PURPOSE

To outline the process, approval and implementation of the annual adjustment of the tax interest rate for the Department of Revenue (DOR).

### II. POLICY

[KRS 131.183\(1\)](#) provides, in part, that "The commissioner of revenue shall adjust the tax interest rate not later than November 15 of each year if the adjusted prime rate charged by banks during October of that year, rounded to the nearest full percent, is at least one (1) percentage point more or less than the tax interest rate which is then in effect." In compliance with this provision, the Division of Registration and Data Integrity will conduct an annual survey of selected banks in Kentucky, which charge a prime rate to their preferred customers and advise the Commissioner of Revenue of the findings.

The prime rate represents the base, which banks use to establish interest rates. Loans that are below the prime rate are generally secured by sound collateral, which present little or no risk, such as real estate, both commercial and residential. Working capital loans made to large corporate customers commonly receive rates at prime or percentage points above the prime, based on nationally published prime rates, such as The Wall Street Journal Prime Rate.

### III. DEFINITIONS

- A. The term "tax interest rate" is defined in [KRS 131.010\(6\)](#) as "the interest rate determined under [KRS 131.183](#)" and, more specifically, subsection (1).

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- B. The term “adjusted prime rate charged by banks” is defined in [KRS 131.010\(5\)](#) as the “average predominant prime rate quoted by commercial banks to large businesses, as determined by the board of governors of the Federal Reserve System”.
- C. The DOR interprets the term “average predominant prime rate”, as defined in [KRS 131.010\(5\)](#), to mean the average of the prevailing rate that a bank charges to its most credit-worthy customers, generally corporations. It further is interpreted to mean the “average” of the averages, as revealed in the survey of banks conducted by DOR.
- D. The DOR interprets the term “commercial banks”, as defined in [KRS 131.010\(5\)](#), to mean a federally insured bank, which is chartered by either the approved Federal official or the state banking authority.

#### IV. PROCEDURE

##### A. Process

1. During November, the Division of Registration and Data Integrity shall conduct a survey of nine (9) banks located across the state.
2. The “average predominant prime rate” charged by each bank, during the previous month of October to its most credit-worthy customers, generally corporations, shall be recorded and totaled.
  - a. If a bank has charged two different prime rates during October, the rate shall be calculated from weighted averages based on the number of days charged at each rate.
  - b. An average rate charged by the banks shall be obtained by dividing the total by nine (9). The average shall be rounded to the nearest percent.
  - c. If this rate is at least one percentage point above or below the current tax interest rate, the tax interest rate charged by the DOR for the following calendar year must be adjusted to reflect the new rate.
  - d. The interest rate applicable to refunds must also reflect the new rate.
3. A memorandum shall be sent to the Commissioner of the DOR from the Executive Director of the Office of Processing and Enforcement.
  - a. This memorandum shall explain the process for obtaining the information on which to base the tax interest rate and the results of the bank survey.

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- b. It shall also state what the tax interest rate will be for the next calendar year for bills and refunds.

### **B. Approval**

1. Upon agreement, the Commissioner of Revenue shall approve the tax interest rate for the new calendar year.
2. After approval, the Commissioner shall return a copy of the memorandum to the Executive Director of the Office of Processing and Enforcement, indicating approval of the tax interest rate for the new calendar year.
3. Upon receipt of this approval, the Executive Director of the Office of Processing and Enforcement shall forward a copy of the memorandum to the Director of the Division of Registration and Data Integrity.
4. The original copy of the memorandum shall be archived in the Office of Processing and Enforcement.

### **C. Implementation**

The Director of the Division of Registration and Data Integrity shall coordinate implementation of the necessary changes as follows:

1. Prepare a request to the Commonwealth Office of Technology to effect the programming changes to all affected systems, including a mandated completion date.
2. Submit the approved memorandum to the webmaster to post to the Kentucky Revenue Employee Website (KREW).
3. The Commissioner's office shall also notify DOR Staff of the adjustment by email.