

INSTRUCTIONS—SCHEDULE P

New in 2001—The pension exclusion is 100 percent or \$37,500, whichever is less. Retirees of previously exempt retirement systems of the federal government, Commonwealth of Kentucky, or any Kentucky local government must compute the amount of pension income attributable to service credit earned after December 31, 1997. This amount will be included with other nonexempt pension sources in Part II.

Types of Income Subject to Exclusion—All pension and retirement income paid under a written retirement plan is eligible for exclusion. This includes pensions, annuities, IRA accounts, 401(k) and similar deferred compensation plans, death benefits, and other similar accounts or plans. As a general rule, if the income is reported on the federal income tax return, Form 1040, line 15(b) or 16(b); Form 1040A, line 11(b) or 12(b); Form 4972; or is a disability retirement benefit or deferred compensation distribution reported on Form 1040, line 7 or 1040A, line 7, then it qualifies for the exclusion.

Roth IRA—Income from converting an IRA to a Roth IRA is eligible for the exclusion. If in 1998 you converted a regular IRA to a Roth IRA, and elected to report the income over four years, the income that you must report in 2001 is eligible for the pension exclusion. Report this income on line 2.

Form 740-NP filers report only pension income received while a resident of Kentucky.

LINE-BY-LINE INSTRUCTIONS

Column A, Column B—This exclusion is for each taxpayer. A husband and wife must compute and claim their own exclusion, regardless of filing status.

PART I—Exempt Retirement Income—Enter the federally taxable portion of pension income paid by the federal government, by the Commonwealth of Kentucky, or by any Kentucky local government. Also include supplemental U.S. Railroad Retirement Board benefits reported on Form 1040, line 16(b) (Form 1040A, line 12(b)) and federal or Kentucky disability retirement income included on federal Form 1040, line 7

(Form 1040A, line 7). Do not include income from deferred compensation plans in Part I.

Use Line 1(a) if retired before January 1, 1998, to report fully exempt pension benefits.

Use Line 1(b) if retired after December 31, 1997, to compute the amount of pension income attributable to service credits earned before January 1, 1998. **Use the worksheet below to compute the exempt percentage.** Multiply the taxable pension by the exempt percentage, enter the result (exempt amount) in Column A or Column B.

Note: Subtract the exempt amount from the taxable pension amount and include the difference with other retirement income in Part II.

PART II—Other Retirement Income, Line 2—Enter the amount reported on federal Form 1040 or 1040A of non-lump-sum pension and retirement income not reported on line 1(c). Also include amounts from Schedule M, line 4 (Form 740-NP, line 45) that reflect pension and IRA bases differences.

PART III—Total to Be Excluded This Year, Line 3—Enter the lesser of the amount on line 2 or \$37,500.

Line 4—Enter the total of lines 1(c) and 3. This is your pension income exclusion. Enter on line 4 and as follows: Schedule M, line 8; Form 740-NP, line 42(b); or Form 741, page 1, line 11.

DEFINITIONS—For use with Schedule P and the worksheet below.

Service Credit—Number of months (years) used by your retirement system to determine retirement benefits.

Purchased Service Credit—Voluntary purchases of service credit as allowed by your retirement system (i.e., military service or prior service with the same or similar system). **Note:** Purchased time is credited based on the dates of service.

Purchased Service Credit Under Internal Revenue Code 415(n)—Internal Revenue Code 415(n) allows for the purchase of up to five years of service credit not otherwise purchasable under the plan.



Worksheet for Federal, Kentucky State and Kentucky Local Government Retirees Who Retired After 12/31/97

Complete this worksheet to determine what percentage of your pension is exempt. If your retirement system has computed the exempt amount (earned before January 1, 1998), enter the amount on page 1, line 1(b), column A or B. If your retirement system has computed the exempt percentage, **enter the exempt percentage on page 1, line 1(b) in the exempt percentage column.** Use a separate worksheet for each governmental pension. Retain this worksheet with your tax records. **Use the percentage on line 4 to compute the exempt portion of your pension in subsequent years.**

1. Enter total months of service credit including purchased service _____
2. Enter months of service credit earned after 12/31/97. Include sick leave credited at date of retirement, and service credit from purchase of military and other service earned after 12/31/97. Do not include purchased service credit under IRC 415(n) _____
3. Subtract line 2 from line 1. Total months of service before January 1, 1998 _____
4. Divide line 3 by line 1. Enter here and on page 1, line 1(b), in the exempt percentage column _____
Use this percentage to determine the amount of pension attributable to service earned before 1/1/98.