INSTRUCTIONS—FORM 741
KENTUCKY FIDUCIARY INCOME TAX RETURN

WHO MUST FILE

Every fiduciary must file a return for the following even though all income may be distributed or distributable: (1) every estate with gross income for the taxable year of $1,200 or over; (2) every trust with gross income for the taxable year of $100 or over.

WHEN AND WHERE TO FILE

Taxpayers must file within three months and 15 days after the close of their taxable year. Mail the return to:

Refunds:	Kentucky Department of Revenue Frankfort, KY 40618-0006
Pay Returns:	Kentucky Department of Revenue Frankfort, KY 40619-0008

FIDUCIARY INCOME

Kentucky income tax law is based on the federal income tax law in effect on December 31, 2006. The Department of Revenue generally follows the administrative regulations and rulings of the Internal Revenue Service in those areas where no specific Kentucky law exists. Kentucky law requires taxpayers to report income on the same calendar or fiscal year and to use the same methods of accounting as required for federal income tax purposes. Effective for taxable years ending after September 10, 2001, a fiduciary that for federal income tax purposes elects to use the 30 percent or the 50 percent special depreciation allowance will have a depreciation difference for Kentucky purposes. See Form 740 and Schedule M instructions or contact the Department of Revenue for more information.

ADMINISTRATION EXPENSES (KRS 140.090(h))

In the case of a decedent's estate, if the election was made not to deduct costs of administration, including attorney's fees actually allowed and paid, on a Kentucky inheritance tax return, these expenses may be deducted on Form 741. A statement waiving the right to deduct these expenses for inheritance tax purposes must also be filed with Form 741.

If the same administration expenses that were claimed on the Kentucky Inheritance Tax Return, Form 92A200 or Form 92A205, are also claimed on the federal fiduciary income tax return, Form 1041, an adjustment must be made to add these expenses to the Kentucky adjusted total income on the Kentucky Form 741, Schedule M, Line 3.

LINE-BY-LINE INSTRUCTIONS

Line 1—Enter the amount shown as federal adjusted total income from federal Form 1041, Line 17. **Attach a complete copy of the federal return.**

Line 3—Enter the portion of deductions that are allocated to the additional Kentucky income reported on Line 2. These deductions are in addition to the deductions claimed on your federal Form 1041.

Line 7—Enter the portion of deductions on federal Form 1041 allocable to Kentucky tax-exempt income reported on Line 6. To compute unallowable deductions, divide the Kentucky tax exempt income by the entire income of the fiduciary. Multiply total deductions by this percentage. Report the amount of unallowable deductions on Line 7.

Line 10, Beneficiaries' Shares of Income and Deductions—Income distribution deduction. Enter amount.

Each beneficiary's share of income, deductions, credits, etc., must be reported on a separate Schedule K-1 and filed with Form 741. A copy must be given to the beneficiary and a copy retained by the fiduciary.

The income distributed or distributable to beneficiaries is the amount on page 1, Line 10. Each beneficiary is required to include the distributed or distributable share of income, as shown on Schedule K-1, on the individual income tax return. The name and identification number of each beneficiary should be entered as it appears on the individual return.

Generally, federal rules and regulations apply but amounts reported may be different due to differences in Kentucky and federal laws, e.g., statutorily exempt income, U.S. government bonds, municipal interest, etc.

Line 11—Enter excludable amount of retirement income. Attach Schedule P if the pension income is more than $41,110 and is from a retirement system of the federal government, Commonwealth of Kentucky or a Kentucky local government. The fiduciary may claim a deduction for retirement income not distributed on Form 741, Line 10. Each beneficiary is entitled to combine the retirement income distributed on Line 10 with other pension income received and claim the pension income exclusion on his or her individual income tax return.

Line 12, Federal Estate Tax Deduction—Enter amount.

Refer to federal Form 1041 instructions for the definition of the federal estate tax deduction.

The federal estate tax deduction does not include fiduciary income tax paid on federal Form 1041. A copy of the computation for the deduction must be attached to Form 741.

Line 15, Nontaxable Income Attributable to Nonresident Beneficiaries—Enter the amount of intangible income included in Line 14 that is attributable to the nonresident beneficiaries and was not deducted on Line 10 as an income distribution deduction.

Attach federal Schedules K-1 or a schedule that lists the name, address, Social Security number and the amount of income of each beneficiary.

Line 17(a), Tax Computation—Compute your tax using the following tax rate schedule.

If taxable income is:	*Tax before credit is:*
$ 0 — $3,000	2% of taxable income
$3,001 — $4,000	3% of taxable income minus $30
$4,001 — $5,000	4% of taxable income minus $70
$5,001 — $8,000	5% of taxable income minus $120
$8,001 — $75,000	5.8% of taxable income minus $184
$75,001 and up	6% of taxable income minus $334

Example: (Taxable income) $8,500 x 5.8% − $184 = $309

Line 17(b), Lump-sum Distribution—Special 10–Year Averaging—Kentucky allows a special 10-year averaging method for determining tax on lump-sum distributions received from certain retirement plans that qualify for federal 10-year averaging. If this special method is used for federal purposes, Form 4972-K, Kentucky Tax on Lump-Sum Distributions, and Schedule P, Pension Income Exclusion, must be filed with Form 741. Enter tax from Form 4972-K.

Line 17(c), Recycling Composting Recapture—Enter amount from Schedule RC-R.

Line 17(d)—Add the amounts from Lines 17(a), (b) and (c), and enter total on Line 17(d).

Line 18—Nonrefundable Credits

To claim credits for any of the following **business incentive and other credits**, enter the amount on Line 18, identify and attach any applicable schedule(s) or certification(s) to substantiate the credit(s) claimed. If more than one credit is claimed, attach a list of credits claimed and enter the total.

- nonrefundable Kentucky corporation tax credit (KRS 141.420(3))
- limited liability entity tax credit (KRS 141.0401(2))
- skills training investment tax credit
- historic preservation restoration tax credit
- credit for tax paid to another state
- employer's unemployment tax credit
- recycling and/or composting tax credit
- Kentucky Investment Fund tax credit
- coal incentive tax credit
- qualified research facility tax credit
- employer GED incentive tax credit
- voluntary environmental remediation credit (Brownfield)
- biodiesel credit
- environmental stewardship credit
- clean coal incentive credit

To claim credit(s) for tax paid to another state, enter the amount on Line 18 and identify as "credit for tax paid to another state." A copy of the return filed with any state for which credit is being claimed must be attached to Form 741.

Nonrefundable Kentucky Corporation Tax Credit—Partners, members and shareholders of pass-through entities (PTEs), such as, limited liability companies (LLCs), partnerships with limited liability, and S corporations taxed as corporations, are entitled to a nonrefundable credit under KRS 141.420(3) for the tax paid by the PTE under KRS 141.040. The credit is limited to the tax savings if the income taxed on the corporation's return is omitted on the individual's return, or the proportionate share of tax paid by the entity less the required minimum tax of $175, whichever is less. The limitation is calculated separately for each PTE. If the PTE passes through a loss, the individual tax limitation is zero.

Estates or trusts that are owners of disregarded single member LLCs (SMLLCs) that report income on Schedules C, E, or F for federal income tax shall file Form 725, Kentucky Single Member LLC Corporation Income Tax Return, to compute and pay the corporation income tax. The member shall report income or loss from the entity and determine credit in the same manner as other individual PTE owners.

For PTEs including SMLLCs that are doing business both within and without Kentucky, the income that is omitted to determine the amount of allowable credit is that portion of the income subject to the corporation income tax.

Nonrefundable Kentucky corporation tax credit (KRS 141.420(3))—The credit amount is shown on Kentucky Schedule(s) K-1 from pass-through entities (PTEs) or Form(s) 725 for single member limited liability companies. Copies of Kentucky Schedule(s) K-1 or Form(s) 725 must be attached to your return.

Kentucky Corporation Tax Credit Worksheet

Complete a separate worksheet for each PTE. Retain for your records.

Name ______________________________

Address ______________________________

FEIN ______________________________

Percentage of Ownership .... ________ %

1. Enter Kentucky taxable income from Form 741, Line 16 .... ________
2. Enter income included in Line 1 and taxed under KRS 141.040 **(from Kentucky Schedule K-1 or Form 725)** .... ________
3. Subtract Line 2 from Line 1 and enter total here .... ________
4. Enter Kentucky tax on income amount on Line 1 .... ________
5. Enter Kentucky tax on income amount on Line 3 .... ________
6. Subtract Line 5 from Line 4. If Line 5 is larger than Line 4, enter zero. This is your tax savings if income is ignored .... ________
7. Enter nonrefundable corporation tax credit **(from Kentucky Schedule K-1 or Form 725)** .... ________
8. Enter the lesser of Line 6 or Line 7. This is your credit. Enter here and on Form 741, Line 18 .... ________

Limited Liability Entity Tax Credit (KRS 141.0401(2))—An individual that is a partner, member or shareholder of a limited liability pass-through entity is allowed a limited liability entity tax (LLET) credit against the income tax imposed by KRS 141.020 equal to the individual's proportionate share of LLET computed on the gross receipts or gross profits of the limited liability pass-through entity as provided by KRS 141.0401(2), after the LLET is reduced by the minimum tax of $175 and by other tax credits for which the limited liability pass-through entity may be allowed. The credit allowed an individual that is a partner, member, or shareholder of a limited liability pass-through entity against income tax shall be applied only to income tax assessed on the individual's proportionate share of distributive income from the limited liability pass-through entity as provided by KRS 141.0401(3)(b). Any remaining LLET credit shall be disallowed and shall not be carried forward to the next year.

Nonrefundable Kentucky limited liability entity tax credit (KRS 141.0401(2))—The credit amount is shown on Kentucky Schedule(s) K-1 from pass-through entities (PTEs) or Form(s) 725 for single member limited liability companies. **Copies of Kentucky Schedule(s) K-1 or Form(s) 725 must be attached to your return.**

Kentucky Limited Liability Entity Tax Credit Worksheet

Complete a separate worksheet for each LLE. Retain for your records.

Name ____

Address ____

FEIN ____

Percentage of Ownership .... ____________%

1. Enter Kentucky taxable income from Form 741, Line 16 .... ______________
2. Enter LLE income **as shown on Kentucky Schedule K-1 or Form 725)** .... ______________
3. Subtract Line 2 from Line 1 and enter total here .... ______________
4. Enter Kentucky tax on income amount on Line 1 .... ______________
5. Enter Kentucky tax on income amount on Line 3 .... ______________
6. Subtract Line 5 from Line 4. If Line 5 is larger than Line 4, enter zero. This is your tax savings if income is ignored .... ______________
7. Enter nonrefundable limited liability entity tax credit **(from Kentucky Schedule K-1 or Form 725)** .... ______________
8. Enter the lesser of Line 6 or Line 7. This is your credit. Enter here and on Form 741, Line 18 .... ______________

Line 21(a)—Enter on Line 21(a) all estimated tax payments, credit from the previous year's return and/or extension payments.

Line 21(b)—If Kentucky income tax was erroneously withheld on income in respect of a decedent, attach a copy of the wage and tax statement of the deceased to Form 741. Enter on Line 21(b) the amount of withholding.

Line 21(c)—Refundable Kentucky Corporation Tax Credit (KRS 141.420(3)(c))

This amount is shown on Kentucky Schedule(s) K-1 from pass-through entities (PTEs) or Form(s) 725 for single member LLCs. Copies of Kentucky Schedule(s) K-1 or Form(s) 725 should be attached to your return.

For taxable years beginning after December 31, 2004, and before January 1, 2007, the portion of credit that represents 1 percent of the entity's taxable income in excess of $216,600 shall be refundable. The PTE shall compute and report the amount of nonrefundable and refundable credit available to the partners, members or shareholders.

Line 21(d)—Add the amounts from 21(a), (b) and (c), and enter the total on 21(d).

Line 22—Subtract Line 21(d) from Line 20.

Any tax due must be paid in full at time of filing. Attach check payable to the **Kentucky State Treasurer**.

PENALTY AND INTEREST

Late Filing Penalty—If a return is not filed by the due date or the extended due date, a penalty of 2 percent of the total tax due for each 30 days or fraction thereof that a return is not filed may be assessed, not to exceed 20 percent. The minimum penalty is $10.

Late Payment Penalty—If the amount of tax due as shown on Line 21 is not paid by the original due date of the return, a penalty of 2 percent of the tax computed due may be assessed for each 30 days or fraction thereof that the tax is past due, not to exceed 20 percent. The minimum penalty is $10. However, if the amount timely paid is 75 percent of the tax determined due by the Department of Revenue, no late payment penalty will be assessed.

Interest—Interest will be assessed at the "tax interest rate" from the original due date of the return until the date of payment.

Note: Penalties but not interest may be reduced or waived if reasonable cause for reduction or waiver can be shown.

SIGNATURE

To be valid, this return must be signed by the fiduciary or agent. If prepared by a person other than fiduciary or agent, type or print name of person preparing the return.

SCHEDULE M (FORM 741) INSTRUCTIONS

Part I—Additions to Federal Adjusted Total Income

Line 1—Enter interest income from bonds issued by other states.

Line 2—Enter additions from Kentucky Schedule(s) K-1 received from partnerships, fiduciaries and S corporations.

Line 3—Enter other additions to income. Other additions may include:

- interest deducted by an electing small business trust (ESBT) on the federal Form 1041 for money borrowed to acquire S corporation stock;
- state income taxes deducted on federal Form 1041;
- the portion of a lump-sum distribution on which you have elected the 20 percent capital gains rate for federal income tax purposes (Schedule P and Form 4972-K required);
- the federal net operating loss deduction;
- the passive activity loss adjustment (see Form 8582-K and instructions);
- differences in pension (3-year recovery rule) and IRA bases;
- differences in gains (losses) from the sale of intangible assets amortized under the provisions of the Revenue Reconciliation Act of 1993;
- federal depreciation if you have elected to take the 30 percent or the 50 percent special depreciation allowance for property placed in service after September 10, 2001.

Line 4, Total Additions—Add Lines 1 through 3. Enter on Schedule M, Line 4 and on page 1, Line 2.

Part II—Subtractions from Federal Adjusted Total Income

Line 5—Enter interest from U.S. government bonds and securities (attach schedule).

Line 6—Enter subtractions from Kentucky Schedule(s) K-1 received from partnerships, fiduciaries and S corporations.

Line 7—Enter other subtractions from income. Other subtractions may include:

- Kentucky net operating loss deduction;
- passive activity loss adjustment (see Form 8582-K and instructions);
- differences in the gains (losses) from the sale of intangible assets amortized under the provisions of the Revenue Reconciliation Act of 1993;
- Nonresident trust or nonresident estate—Subtract the amount of income reported on Form 741, Line 1 that is not taxable to Kentucky. **Note:** Deductions must also be adjusted to claim only that portion of deductions allocable to the Kentucky income;
- Kentucky depreciation computed in accordance with the Internal Revenue Code in effect on December 31, 2001, if you have elected to take the 30 percent or the 50 percent special depreciation allowance for property placed in service after September 10, 2001;
- income of military personnel killed in the line of duty.

Note: All income earned by soldiers killed in the line of duty is exempt from Kentucky tax for the year during which the death occurred and the year preceding the death. Federal and state death benefits payable to the estate or any beneficiaries may also be excluded. Additional information may be found in the General Information section of the instructions for Form 740 or Form 740-NP.

Line 8, Total Subtractions—Add Lines 5 through 7. Enter on Schedule M, Line 8 and on page 1, Line 6.

SCHEDULE K-1 INSTRUCTIONS

A Kentucky Schedule K-1 is required if you claim an income distribution deduction on Schedule B and have differences in income reported on Schedule M. Attach copies of federal Schedule(s) K-1 if there are no differences.

Schedule K-1 is used to report the portion of income distributed to beneficiaries that is subject to tax. All items of income subject to tax and all deductions are listed on Schedule K-1.

- Enter in column (b) amounts from federal Form 1041, Schedule K-1;
- enter in column (c) any difference between Kentucky and federal amounts (Schedule M); and
- enter in column (d) the Kentucky income and deduction amounts.

Line 11, Resident Beneficiary Adjustment—Complete Line 11 to determine the net difference between the federal Schedule K-1 and the Kentucky Schedule K-1. Combine from column (c), Lines 1 through 6, and portions of Lines 9 and 10. Do not include amounts from Lines 7, 8, 9(a), or other deductions that qualify as itemized deductions. These amounts are entered on the beneficiaries' Form 740, Schedule A, Itemized Deductions Schedule.

Nonresident Beneficiaries (Form 740-NP Filers)—Complete Schedule K-1 for nonresident beneficiaries. This Schedule K-1 should reflect all income that has been claimed as part of the income distribution deduction. However, nonresident beneficiaries are only subject to tax on the following types of income:

- from Kentucky sources;
- from activities carried on in Kentucky;
- from the performance of services in Kentucky;
- from real or tangible property located in Kentucky; and
- from a partnership or S corporation doing business in Kentucky.

Lines 12a, b and c—If an income distribution includes net distributable share income from a pass-through entity subject to tax under KRS 141.040, complete Lines 12a, b and c.

Line 12d—If an income distribution includes net distributable share income from a limited liability entity subject to tax under KRS 141.0401(2), complete Line 12d.

ADDITIONAL INFORMATION

If you need further assistance, contact a local Kentucky Taxpayer Service Center or the Department of Revenue, Frankfort, KY 40620, (502) 564-4581.