

INSTRUCTIONS



2007 KENTUCKY S CORPORATION INCOME TAX AND LIMITED LIABILITY ENTITY TAX (LLET) RETURN

The Department of Revenue will not be printing S corporation packets and labels in 2007.

PURPOSE OF THE INSTRUCTIONS

These instructions have been designed for S corporations, both domestic and foreign, which are required by law to file a Kentucky S corporation income tax return.

Refer to the chart on page 4 to determine what corporation income tax form your business needs to file. Form 720S and related schedules are available from the Department of Revenue or Kentucky Taxpayer Service Centers (see page 18).

HOW TO OBTAIN ADDITIONAL FORMS

Forms and instructions are available at all Kentucky Taxpayer Service Centers (see page 18). They may also be obtained by writing FORMS, Department of Revenue, 501 High Street, Frankfort, KY 40601, or by calling (502) 564-3658. Forms can be downloaded from www.revenue.ky.gov.

KENTUCKY TAX LAW CHANGES

2005 Kentucky General Assembly

Top Corporation Income Tax Rate Reduction—For tax years beginning on or after January 1, 2007, the top corporation income tax rate drops from 7 percent to 6 percent.

2006 Special Session Kentucky General Assembly

On June 28, 2006, the Kentucky General Assembly enacted House Bill 1 (HB 1) during an unprecedented five-day Special Session. The bill was signed into law by Gov. Fletcher the same day. The following is a summary of the main provisions of HB 1:

HB 1—Provisions effective for tax years beginning on or after January 1, 2007

Restoration of Federal Pass-through Entity Treatment—All pass-through entities will be treated the same for Kentucky income tax purposes as they are treated for federal income tax purposes, except for differences between Kentucky law and federal law. LLCs, S corporations, limited liability partnerships and limited partnerships will no longer be subject to the corporation income tax. The income will be passed through and taxed at the ownership level.

HB 1 requires withholding of the income tax due from nonresident individual owners of pass-through entities and from corporate owners of pass-through entities if the corporate owner's only business connection to Kentucky is the ownership interest in a pass-through entity doing business here.

New Limited Liability Entity Tax Replaces AMC—A limited liability entity tax (LLET) is imposed on every corporation and limited liability pass-through entity doing business in Kentucky. A minimum of \$175 will be due from those entities subject to this new tax.

Except for the \$175 minimum, the LLET will not apply if the entities' gross receipts or gross profits from all sources are \$3 million or less.

Except for the \$175 minimum, the LLET will be partially reduced for taxpayers with gross receipts or gross profits from all sources in excess of \$3 million, but less than \$6 million.

Entities exempted, pursuant to KRS 141.0401(6), from the LLET are:

1. Financial institutions, as defined in KRS 136.500, except banker's banks organized under KRS 287.135 or 286.3-135;
2. Savings and loan associations organized under the laws of this state and under the laws of the U.S. and making loans to members only;
3. Banks for cooperatives;
4. Production credit associations;
5. Insurance companies, including farmers' or other mutual hail, cyclone, windstorm or fire insurance companies, insurers and reciprocal underwriters;
6. Corporations or other entities exempt under Section 501 of the Internal Revenue Code (IRC);
7. Religious, educational, charitable or like corporations not organized or conducted for pecuniary profit;
8. Corporations whose only owned or leased property located in this state is located at the premises of a printer with which it has contracted for printing, provided that: (a) the property consists of the final printed product, or copy from which the printed product is produced; and (b) the corporation has no individuals receiving compensation in this state as provided in KRS 141.120(8)(b);
9. Public service corporations subject to tax under KRS 136.120;
10. Open-end registered investment companies organized under the laws of this state and registered under the Investment Company Act of 1940;

11. Any property or facility that has been certified as a fluidized bed energy production facility as defined in KRS 211.390;
12. An alcohol production facility as defined in KRS 247.910;
13. Real estate investment trusts as defined in Section 856 of the IRC;
14. Regulated investment companies as defined in Section 851 of the IRC;
15. Real estate mortgage investment conduits as defined in Section 860D of the IRC;
16. Personal service corporations as defined in Section 269A(b)(1) of the IRC;
17. Cooperatives described in Sections 521 and 1381 of the IRC, including farmers' agricultural and other cooperatives organized or recognized under KRS Chapter 272, advertising cooperatives, purchasing cooperatives, homeowners associations including those described in Section 528 of the IRC, political organizations as defined in Section 527 of the IRC, and rural electric and rural telephone cooperatives; or,
18. Publicly traded partnerships as defined by Section 7704(b) of the IRC that are treated as partnerships for federal tax purposes under Section 7704(c) of the IRC or their publicly traded partnership affiliates. "Publicly traded partnership affiliates" shall include any LLC or limited partnership for which at least 80 percent of the LLC member interests or limited partner interests are owned directly or indirectly by the publicly traded partnership.

New Limited Liability Entity Tax Credit Against Income Tax— A corporation is allowed an LLET credit against the income tax imposed by KRS 141.040 equal to the LLET computed on its gross receipts or gross profits as provided by KRS 141.0401(2)(c), after the LLET is reduced by the minimum tax of \$175 and by any other credits for which the corporation may be allowed.

A corporation that is a partner or member of a limited liability pass-through entity is allowed an LLET credit against the income tax imposed by KRS 141.040 equal to the corporation'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)(c), 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 a corporation that is a partner or member of a limited liability pass-through entity against income tax shall be applied only to income tax assessed on the corporation'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.

An individual that is a partner, member, or shareholder of a limited liability pass-through entity is allowed an 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.

Other Credits Against the LLET—The nonrefundable credits, e.g., economic development, recycling, biodiesel, etc. are applied against the LLET to arrive at the LLET liability. **KRS 141.0205(5)**

Apportionment—A multistate pass-through entity that is doing business within and without Kentucky will pass through its proportionate share of its receipts, property and payroll to its corporation ownership to be included in the corporation's apportionment factor. A general partnership formed after January 1, 2006 that is doing business within and without Kentucky will pass through its proportionate share of receipts, property and payroll to its corporation ownership to be included in the corporation's apportionment factor.

Homeowners Associations—Any homeowners association that is required to file a federal income tax return on Form 1120H is required to file a Kentucky corporation income tax return on Form 720. That statement does not reflect a law change, but rather a continuation of the Department of Revenue's (DOR) long-standing interpretation of Kentucky's corporation income tax law. KRS 141.010(14)(c) defines taxable net income in the case of a homeowners association. If no income is taxable on the federal Form 1120H, no income is taxable on the Kentucky return.

Homeowners associations will be exempt from the LLET, including the \$175 minimum tax for taxable years beginning on or after January 1, 2007.

2007 Kentucky General Assembly

Business Entities (Effective June 26, 2007)—Amends and defines business entities and updates KRS Chapter 271B to reflect the provisions of the Model Business Corporation Act. The provisions will provide for more consistency among business corporations, nonprofit corporations, cooperatives, associations, partnerships, limited partnerships, limited liability companies and business trusts. **(HB 334)**

Electronic Levy of Delinquent Taxes (Effective June 26, 2007)—Requires that the financial institution match system implemented by the DOR for the seizing of financial assets of delinquent taxpayers and debtors not be implemented unless and until the department is prepared to implement the system in 90 percent of all financial institutions within a period of no longer than 18 months from the effective date of this act.

The bill also provides that financial institutions may implement a data match sooner. The bill amends KRS 131.990 to apply fines for failure to comply within 90 days of notification by the DOR and to require the financial institution to forfeit its license to do business in the commonwealth for failure or refusal to comply within 120 days of notification by the DOR. The bill also amends KRS 205.990 to apply fines for failure to comply with KRS 205.772 and applicable administrative regulations if the financial institution has not complied within 90 days of the notification by the Cabinet for Families and Children. **(HB 443)**

Internal Revenue Code Reference Date (Effective for Tax Years Beginning on or After January 1, 2007)—Amends KRS 141.010(3) to update the Internal Revenue Code (IRC) reference date for individual and corporation income tax purposes to December 31, 2006. The depreciation and section 179 expense deductions for properties placed in service after September 10, 2001 will still be computed under the IRC in effect on December 31, 2001.

The bill also amends KRS 67.750 to update the reference date for the IRC for local governments to December 31, 2006.

In addition, the bill amends KRS 141.010(13) to disallow any dividend-paid deduction of a captive real estate investment trust when computing the taxable net income of a corporation. **(HB 258)**

Withdrawal of Commonwealth's Consent to Suits (Effective March 19, 2007)—Withdraws the commonwealth's consent to suits attempting to recover alleged tax overpayments generated by the use of *unitary* corporate income tax returns. The bill also prohibits withdrawals from the State Treasury to pay these claims. The purpose of the legislation is to end litigation and the commonwealth's exposure resulting from a 1994 court decision which created a tax loophole for certain corporations. (HB 316)

Economic Development Incentive Programs

Economic Development Project (Effective June 26, 2007)—Amends KRS 154.22-010(10) and KRS 154.28-010(11) to expand and define economic development project to include certain leased facilities. Such economic development projects utilizing leased facilities will be eligible only for the aggregate assessments pursuant to KRS 154.22-070 or KRS 154.28-110 withheld by the approved company each year and will not be eligible for credit against Kentucky income tax and LLET. (HB 462)

Economic Development Project Adjoining Regional Postsecondary Education Center (Effective March 16, 2007)—Expands the Kentucky Jobs Development Act by amending KRS 154.24-090(4) to provide that if an eligible company receives approval from the Kentucky Economic Development Finance Authority before July 1, 2008, and locates an economic development project on property that adjoins one of the five regional postsecondary education centers operated and occupied in cooperation with the Kentucky Community and Technical College System, the eligible company may alternatively satisfy the wage requirements. Ninety percent of the company's employees must receive base hourly wages and benefits equal to or greater than 200 percent of the federal minimum wage and the company must seek to provide meaningful employment opportunities for nontraditional students enrolled at a regional postsecondary education center. (HB 468)

Economic Development Incentive Program-Cities of the First Class (Effective March 23, 2007)—Creates new KRS Chapter 154.25 to establish an economic development incentive program which would provide tax credits and wage assessment fees to eligible companies. An eligible company means any corporation, limited liability company, partnership, limited partnership, sole proprietorship, business trust or any other entity designated by the United States Department of Commerce, United States Census Bureau North American Industry Classification System code 336211, 336111, 336112 or 336120 that is within the jurisdiction of a consolidated local government containing a city of the first class, employs a minimum of 1,000 full-time persons engaged in manufacturing, has been operating within the commonwealth on a continuous basis for at least five years preceding the request for approval

by the Kentucky Economic Development Finance Authority of the project which meets the standards set forth in the act, and that has been previously approved for economic development incentives from the commonwealth related to one or more of its facilities. (HB 536)

Tax Increment Financing and Urban Redevelopment (Effective March 23, 2007)—Provides that any city or county government may establish a local development area to encourage reinvestment in and development and reuse of areas of the city or county as provided in the act. Any taxing authority may, in addition to any other pledge permitted by law to secure its obligations, pledge up to 100 percent of the incremental local tax revenues (real property and occupational taxes) generated in the development area or local development area or from a project within the development area or local development area. In addition, any city, county or agency with bonding authority may issue increment bonds and may pledge incremental revenues to the payment of the incremental bonds. Certain projects within the development areas shall be eligible for participation by the commonwealth, if such projects meet the requirements for commonwealth participation. The measure also creates a State Tax Increment Financing Commission which offers three tax increment participation programs: (1) Participation Program for Real Property Ad Valorem Tax Revenues, (2) Signature Project Program and (3) Mixed Use Redevelopment in Blighted Urban Areas. State tax revenues received from (a) real property taxes, (b) individual income taxes, (c) corporate income taxes, (d) limited liability entity taxes or (e) sales taxes may be used as funding sources for the designated and approved projects provided such taxes were not previously committed to another development project within the same development area. The state tax revenues that can be committed are further limited by the requirements of the tax increment participation programs. The bill establishes the Division of Tax Increment Financing within the DOR to analyze and assist in implementing proposed state tax increment financing projects and serve as the record keeping unit for all state tax increment financing projects. (HB 549)

Economic Revitalization Project (Effective March 23, 2007)—Amends KRS 154.26-010 and KRS 154.26-080 to include in the definition of an economic revitalization project a closed facility that resumes operations. Also amends the definition of eligible company to reduce the requirement on the number of tons of coal mined from an economic revitalization project facility from four million to three million tons. (HB 69)

2007 Second Extraordinary Session

KRS 141.422 was amended to permit producers of renewable diesel to be entitled to the nonrefundable biodiesel tax credit and subject to the same requirements provided in KRS 141.423. (HB 1)

FILING FORM GUIDE

Ownership	Kentucky Form and Tax		
	Form Required	Corporation Income Tax	LLET
1. C corporation	720	Yes	Yes
2. C corporation (consolidated group as provided by KRS 141.200(4))	720	Yes	Yes
3. C corporation (nexus consolidated group as provided by KRS 141.200 (9) to (14))	720	Yes	Yes
4. Publicly traded partnership (taxed as a corporation for federal income tax purposes)	720	Yes	Yes
5. S corporation	720S	Yes *	Yes
6. Single member limited liability company whose single member is an individual	725	No	Yes
7. Limited liability company (two or more members)	765	No	Yes
8. Limited partnership	765	No	Yes
9. Limited liability partnership	765	No	Yes
10. General partnership	765-GP	No	No
11. Publicly traded partnership (taxed as a partnership for federal income tax purposes)	765-GP	No	No

* If the S corporation has built-in gains, passive investment income or installments of tax on the recapture of LIFO benefits as provided by KRS 141.040(14).

IMPORTANT

Corporations must create a Kentucky Form 4562 and Schedule D by converting federal forms.

Depreciation, Section 179 Deduction and Gains/Losses From Disposition of Assets—For taxable years beginning before January 1, 2002, Kentucky depreciation and Section 179 deduction are determined in accordance with the Internal Revenue Code (IRC) in effect on December 31, 1999, and for taxable years beginning after December 31, 2001, Kentucky depreciation and Section 179 deduction are determined in accordance with the IRC in effect on December 31, 2001. For calendar year 2007 returns and fiscal year returns that begin in 2007, any corporation income taxpayer that elects any of the following will have a different depreciation or Section 179 expense deduction for Kentucky purposes than for federal purposes:

- 30 percent bonus depreciation allowance;
- 50 percent bonus depreciation allowance;
- additional Section 179 deduction for New York Liberty Zone Property;
- additional depreciation and Section 179 deduction for Gulf Opportunity Zone Property; or,
- increased Section 179 deduction from \$25,000 to \$125,000.

If any of the above federal/Kentucky differences exist, the differences will continue through the life of the assets. There will be recapture and basis differences for Kentucky and federal income tax purposes until the assets are sold or fully depreciated.

Important: If the corporation has not taken the 30 percent special depreciation allowance, the 50 percent special depreciation allowance, the additional Section 179 deduction for New York Liberty Zone Property, or the increased Section 179 deduction for federal income tax purposes on any assets for which a depreciation deduction is being claimed for the taxable year, then no adjustment will be needed for Kentucky income tax purposes. **If federal Form 4562 is required to be filed for federal income tax purposes, a copy must be submitted with Form 720S to verify that no adjustments are required.**

Determining and Reporting Depreciation and Section 179 Deduction Differences—Federal/Kentucky depreciation or Section 179 deduction differences shall be reported as follows:

1. The amount from Line 14 and depreciation claimed on federal Schedule A or elsewhere except for the Section 179 deduction on the federal Form 1120S must be included on page 1, Part I—Ordinary Income (Loss) Computation, Line 3, Form 720S. **If federal Form 4562 is required to be filed for federal income tax purposes, a copy must be attached to Form 720S.**
2. Convert federal Form 4562 to a Kentucky form by entering **Kentucky** at the top center of the form above Depreciation and Amortization. Compute Kentucky depreciation and Section 179 deduction in accordance with the IRC in effect on December 31, 2001, by ignoring the lines and instructions regarding the special depreciation allowance and the additional Section 179 deduction. **NOTE:** For Kentucky purposes, the maximum Section 179 deduction amount on Line 1 is \$25,000 and the threshold cost of Section 179 property on Line 3 is \$200,000. The \$25,000 maximum

allowable Section 179 deduction for Kentucky purposes is reduced dollar-for-dollar by the amount by which the cost of qualifying Section 179 property placed in service during the year exceeds \$200,000. In determining the Section 179 deduction for Kentucky, the income limitation on Line 11 should be determined by using Kentucky net income before the Section 179 deduction instead of federal taxable income.

3. The corporation **must attach the Kentucky converted Form 4562** to Form 720S, and the amount from Line 22 less the amount on Line 12 of the Kentucky converted Form 4562, must be included on page 1, Part I—Ordinary Income (Loss) Computation, Line 8, Form 720S and the amount from Line 12 of the Kentucky converted Form 4562 must be included on Schedule K, Section I, Line 8. A Kentucky converted Form 4562 must be filed for each year even though a federal Form 4562 may not be required.

Determining and Reporting Differences in Gain or Loss From Disposition of Assets—If during the year the corporation disposes of assets on which it has taken the special depreciation allowance or the additional Section 179 deduction for federal income tax purposes, the corporation will need to determine and report the difference in the amount of gain or loss on such assets as follows:

1. Convert **federal Schedule D (Form 1120S)** and other applicable federal forms to Kentucky forms by entering **Kentucky** at the top center of the form, and compute the Kentucky capital gain net income from the disposed assets using Kentucky basis. Include the amount from Line 6 of the Kentucky converted Schedule D (Form 1120S) on Line 4(d) or 6, Section I of Schedule K, Form 720S. Include the amount from Line 13 of the Kentucky converted Schedule D (Form 1120S) on Line 4(e) or 6, Section I of Schedule K, Form 720S. **Federal Schedule D (Form 1120S) filed with the federal return and the Kentucky converted Schedule D must be attached to Form 720S.**
2. If the amount reported on Line 4 of federal Form 1120S, Net Gain or (Loss) Form 4797, is a gain, include this amount on page 1, Part I—Ordinary Income (Loss) Computation, Line 9, Form 720S. If the amount reported on Line 4 of federal Form 1120S, Net Gain or (Loss) Form 4797, is a loss, include this amount on page 1, Part I—Ordinary Income (Loss) Computation, Line 5, Form 720S. Convert **federal Form 4797** and other applicable federal forms to Kentucky forms by entering **Kentucky** at the top center of the form, and compute the Kentucky gain or (loss) from the sale of business property using Kentucky basis. If the amount on Line 17 of Kentucky converted Form 4797 is a gain, include this amount on page 1, Part I—Ordinary Income (Loss) Computation, Line 5, Form 720S. If the amount on Line 17 of Kentucky converted Form 4797 is a loss, include this amount on page 1, Part I—Ordinary Income (Loss) Computation, Line 9, Form 720S. **Federal Form 4797 filed with the federal return and the Kentucky converted Form 4797 must be attached to Form 720S.**

Tax Treatment of S Corporation and Shareholder(s)

A corporation which elects S corporation treatment for federal income tax purposes in accordance with Sections 1361(a) and 1361(b) of the IRC must file as an S corporation for Kentucky income tax purposes. For taxable years beginning on or after January 1, 2007, an S corporation is classified as limited liability pass-through entity as provided by KRS 141.010(28). For taxable years beginning on or after January 1, 2007, an annual limited liability entity tax (LLET) shall be paid by every corporation and every limited liability pass-through entity doing business in Kentucky on all Kentucky gross receipts or Kentucky gross profits as provided by KRS 141.0401(2), unless specifically excluded. See LLET Nonfiling Status Codes on page 9 of these instructions.

Also, an S Corporation for tax years beginning on or after January 1, 2007: (1) is required to submit installments of tax on the recapture of LIFO reserves as provided by Section 1363(d) of the Internal Revenue Code; (2) pay tax on built-in gains as provided by Section 1374 of the Internal Revenue Code; and (3) pay tax on passive investment income as provided by Section 1375 of the Internal Revenue Code. The tax rate imposed on the LIFO recapture, built-in gains, and passive investment income shall be at the highest rate of tax for the taxable year, which is currently six percent (6%). **KRS 141.040(14)**

In determining tax as provided by KRS Chapter 141, a resident individual, estate, or trust that is a shareholder of an S corporation shall take into account the shareholder's total distributive share of the S corporation's items of income, loss, and deduction. In determining tax as provided by KRS Chapter 141, a nonresident individual, estate, or trust that is a shareholder of an S corporation shall take into account the shareholder's total distributive share of the S corporation's items of income, loss, and deduction multiplied by the apportionment fraction if applicable in KRS 141.206(9). **KRS 141.206(5)(6)**

Resident and nonresident individual shareholders shall be entitled to a nonrefundable LLET credit against tax imposed under KRS 141.020 (Kentucky individual income tax). The nonrefundable LLET credit allowed shareholders shall be the shareholders' proportionate share of the LLET for the current year after the subtraction of any credits identified in KRS 141.0205 and reduced by \$175. The credit allowed shareholders shall be applied to the income tax assessed on income from the S corporation. Any remaining credit from the S corporation shall be disallowed. **KRS 141.0401(3)**

For taxable years beginning on or after January 1, 2007, an S corporation required to file a tax return pursuant to KRS 141.206(2) shall withhold income tax at the maximum tax rate as provided in KRS 141.020 on the net distributive share income, whether distributed or undistributed, of each nonresident individual shareholder. Withholding shall not be required if: (1) the S corporation demonstrates to the Kentucky Department of Revenue that a shareholder has filed an appropriate tax return for the prior year with the department, by attaching to the Kentucky Form 740NP-WH that the shareholder is exempt from withholding as provided by KRS 141.206(4)(b)2 and providing the shareholder's name, address, social security number, and net distributive share income; or (2) the S corporation is a qualified investment pass-through entity as provided by KRS 141.206(12). See instructions on page 14 for nonresident withholding.

Reporting of a nonresident individual's net distributive share income on Form 740NP-WH and withholding at the maximum rate, currently six percent (6%), by an S corporation shall satisfy the filing requirement of KRS 141.180 for a nonresident individual shareholder whose only Kentucky source income is net distributive share income from the S corporation.

Banks and Savings and Loan Associations—KRS 141.040(1)

excludes financial institutions (banks and savings and loan associations) as defined in KRS 136.500 from tax on taxable net income and KRS 141.0401(6)(a) and (b) excludes financial institutions from the LLET.

KRS 141.010(10)(j) excludes from the Kentucky adjusted gross income of the shareholders the distributive share of net income from an S corporation subject to tax under KRS 136.505, the bank franchise tax, or KRS 136.300, the savings and loan association capital stock tax. KRS 141.010(10)(j) also excludes from the Kentucky adjusted gross income of the shareholders the portion of the distributive share of net income from an S corporation related to a qualified S subsidiary subject to tax under KRS 136.505 or KRS 136.300.

An S corporation subject to tax under KRS 136.505 or KRS 136.300 should enter zero on Lines 1 through 10 of Form 720S, Schedule K. An S corporation related to a qualified S subsidiary subject to tax under KRS 136.505 or KRS 136.300 should exclude from the amounts entered on Lines 1 through 10 of Form 720S, Schedule K the portion of these items related to the subsidiary. The net amount of the items of income and deductions excluded from Lines 1 through 10 of Form 720S, Schedule K should be entered on Line 26 of Form 720S, Schedule K. A statement should be attached to each shareholder's Form 720S, Schedule K-1 advising the shareholder that this income is excluded for Kentucky income tax purposes because the S corporation is subject to tax under either KRS 136.505 or KRS 136.300.

GENERAL INFORMATION

Internal Revenue Code Reference Date—Effective for taxable years beginning after December 31, 2006, Kentucky Revised Statute (KRS) 141.010(3) was amended to define "Internal Revenue Code" (IRC) for Kentucky income tax purposes to mean the IRC in effect on December 31, 2006, exclusive of any amendments made subsequent to that date, other than amendments that extend provisions in effect on December 31, 2006, that would otherwise terminate and as modified by KRS 141.0101, except that for property placed in service after September 10, 2001, only the depreciation and expense deductions allowed under Sections 168 and 179 of the Internal Revenue Code in effect on December 31, 2001, exclusive of any amendments made subsequent to that date. **KRS 141.010(3)**

Kentucky Tax Registration Application—Prior to doing business in Kentucky, each corporation should complete a Kentucky Tax Registration Application, Revenue Form 10A100 to register for a Kentucky Corporation/LLET account number. This account number will be used for remitting the corporation income tax as required per KRS 141.040 and the LLET as required per KRS 141.0401. The application is available at Kentucky Taxpayer Service Centers (see page 18) or from the Department of Revenue, Taxpayer Registration Section, Frankfort, KY 40620 or at www.revenue.ky.gov (click on Business). The application may be faxed to (502) 227-0772.

Who Must File—**NOTE:** The limitations imposed and protections provided by the United States Constitution or Pub. L. No. 86-272 do not apply to the limited liability entity tax imposed by KRS 141.0401. A Kentucky S Corporation Income Tax and LLET Return, Form 720S, must be filed by every S corporation: (a) being organized under the laws of this state; (b) having a commercial domicile in this state; (c) owning or leasing property in this state; (d) having one or more individuals performing services in this state; (e) maintaining an interest in a pass-through entity doing business in this state; (f) deriving income from or attributable to sources within this state, including deriving income directly or indirectly from a trust doing business in this state, or deriving income directly or indirectly from a single member limited liability company that is doing business in this state and is disregarded as an entity separate from its single member for federal income tax purposes; or (g) directing activities at Kentucky customers for the purpose of selling them goods or services. **KRS 141.010(25), KRS 141.040, KRS 141.0401 and KRS 141.206**

Disregarded Entities—A Qualified Sub Chapter S Subsidiary (QSSS) and a single member limited liability company (LLC) are treated for Kentucky income tax purposes in the same manner as they are treated for federal income tax purposes. Therefore, a QSSS or a single member LLC that is disregarded for federal income tax purposes shall be included in the return filed by its single member (parent entity). A single member filing Form 1120S for federal purposes must file Form 720S. **KRS 141.010(25), KRS 141.200(10) and Regulation 103 KAR 16:300**

Pass-through Entities—An S corporation doing business in Kentucky solely as a partner or member in a pass-through entity will file Form 720S pursuant to the provisions of KRS 141.010, 141.120 and 141.206. (See Schedule A—Apportionment and Allocation Instructions and Schedule A-C Apportionment and Allocation Continuation Sheet.)

S Corporations Not Required to File—S corporations which are exempt by law from Kentucky income tax include financial institutions as defined in KRS 136.500, insurance companies, savings and loan associations, corporations exempted by IRC Section 501 and religious, educational, charitable and like corporations not conducted for profit. **KRS 141.040**

Nonresident Withholding (Form 740NP-WH)

Withholding

KRS 141.206(4)(b) provides that for taxable years beginning on or after January 1, 2007, every pass-through entity required to file a return under KRS 141.206(2), except publicly traded partnerships as defined in KRS 141.0401(6)(r), shall withhold Kentucky income tax on the distributive share, whether distributed or undistributed, of each nonresident individual partner, member or shareholder, or each corporate partner or member that is doing business in Kentucky only through its ownership interest in a pass-through entity. Withholding shall be at the maximum rate as provided in KRS 141.020 or KRS 141.040.

Withholding shall not be required if: (a) the pass-through entity demonstrates to the department that a partner, member or shareholder has filed an appropriate tax return for the prior year with the department, by attaching to the Kentucky Form 40A201, "740NP-WH, Kentucky Nonresident Income Tax Withholding on Net Distributive Share Income Transmittal Report", a statement that the partner, member or shareholder is exempt from withholding as provided by KRS 141.206(4)(b)2, and providing each partner's, member's or shareholder's name, address, federal identification number, Kentucky corporation/ LLET account number, if applicable, and net distributive income; (b) the nonresident partner or member is exempt from Kentucky income tax as provided by KRS 141.040(1); (c) the partner, member or shareholder is a nonresident individual and the pass-through entity is a qualified investment pass-through entity as provided by KRS 141.206(12)(a); or (d) the partner or member is a pass-through entity as provided by KRS 141.010(26).

The reporting of a nonresident individual's net distributive share income and withholding on Form 740NP-WH at the maximum rate of six (6) percent shall satisfy the filing requirements of KRS 141.180 for a nonresident individual partner, member or shareholder whose only Kentucky source income is net distributive share income. The nonresident individual partner, member or shareholder may file a Kentucky Individual Income Tax Return Nonresident or Part-Year Resident (Form 740-NP) to take advantage of the graduated tax rates, credits and deductions.

A pass-through entity shall complete Form 740NP-WH and Form PTE-WH for each individual nonresident partner, member or shareholder and each corporate partner or member and mail Form 740NP-WH and Copy A of Form PTE-WH to the Kentucky

Department of Revenue with payment by the 15th day of the fourth month following the close of the pass-through entity's taxable year. Also, Copy B and C of Form PTE-WH shall be provided to the partners, members or shareholders. Form 740NP-WH and Form PTE-WH are available at www.revenue.ky.gov.

Composite Return

For taxable years beginning on or after January 1, 2007, the Department of Revenue will permit the filing of a "composite return" as provided by KRS 141.206(13) on behalf of electing nonresident individual partners, members or shareholders of a pass-through entity as defined in KRS 141.010(26). Income tax will be computed at the highest marginal rate provided in KRS 141.020 on the partner's, member's or shareholder's pro rata share of the distributive share income from a pass-through entity doing business in, or deriving income from sources within Kentucky. The partners', members' or shareholders' distributive share of income shall include all items of income or deduction used to compute adjusted gross income on the Kentucky return that is passed through to the partner, member or shareholder by the pass-through entity, including but not limited to interest, dividend, capital gains or losses, guaranteed payments and rents (KRS 141.206(13)).

The composite return of a pass-through entity shall be filed with the Department of Revenue, on Form 740-NP, Kentucky Individual Income Tax Return Nonresident or Part-Year Resident. The composite return box on the front of the Form 740-NP return shall be checked to indicate that this is a composite return, and a schedule shall be attached reporting each of the electing nonresident individual partner's, member's or shareholder's name, address, social security number, net distributive share income and tax due. The tax due for all electing partners, members or shareholders shall be remitted with the composite return. A pass-through entity filing a composite return shall make estimated tax payments if required by the provisions of KRS 141.300.

Required Forms and Information—Each S corporation must enter all applicable information on Form 720S, attach a schedule for each line item or line item instruction which states "attach schedule," and the following forms or schedules, if applicable.

Substitute Forms—Any form to be used in lieu of an official Department of Revenue form must be submitted to the department for prior approval.

Kentucky Forms and Schedules

1. S Corporation Income Tax Return (Form 720S)
2. Kentucky Shareholder's Share of Income, Credits, Deductions, Etc.—Schedule K-1 (Form 720S)
3. Apportionment and Allocation (Schedule A)
4. Apportionment and Allocation—Continuation Sheet (Schedule A-C)
5. Limited Liability Entity Tax (Schedule LLET)
6. Limited Liability Entity Tax—Continuation Sheet (Schedule LLET-C)
7. Application for Filing Extension (Form 41A720SL)
8. Tax Credit Summary Schedule (Schedule TCS)

Required Federal Forms and Schedules

All S corporations **must** provide a copy of the following federal forms submitted to the Internal Revenue Service:

1. Form 1120S, Pages 1 through 4
2. Form 4797—Sales of Business Property
3. Schedule D—Capital Gains and Losses
4. Form 5884—Work Opportunity Credit
5. Schedules for items on Form 1120S, Schedule L, which state, "attach schedule."

6. Form 4562—Depreciation and Amortization
7. Form 8825—Rental Real Estate Income and Expenses of a Partnership or an S Corporation

Electronic Funds Transfer (EFT)—LLET estimated tax payments are not permitted by EFT. The Department of Revenue is accepting electronically filed Corporation/LLET income tax estimated tax voucher payments **only** for corporation income tax. Before filing by EFT, the corporation must have a valid Kentucky Corporation/LLET account number which is a six-digit number and have registered with the Department of Revenue to file EFT. Using an incorrect account number such as withholding or sales and use tax will result in the payment being credited to another corporation's account. For more information contact the Department of Revenue at 1-800-839-4137 or (502) 564-6020. The EFT registration form is available at www.revenue.ky.gov. See E-Filing and Payment Options (click on KY E-Tax) located in the upper right-hand corner. The direct link is www.revenue.ky.gov/etax.htm.

EFT is not available for a corporation's LLET estimated tax payments, return payment or extension payment.

Accounting Procedures—Kentucky income tax law requires an S corporation to report income on the same calendar or fiscal year and to use the same methods of accounting required for federal income tax purposes. Any federally approved change in accounting periods or methods must be reported to the Department of Revenue. Attach a copy of the federal approval to the return when filed. **KRS 141.140**

Mailing/Payment—If including payments for other taxes in addition to corporation income tax or LLET, **send a separate check or money order for each type of tax.** Mail the Kentucky S Corporation Income Tax and LLET Return to the **Kentucky Department of Revenue, Frankfort, KY 40620.** Make the check(s) payable to the **Kentucky State Treasurer.**

Filing/Payment Date—An S corporation return must be filed and payment must be made on or before the 15th day of the fourth month following the close of the taxable year.

If the filing/payment date falls on a Saturday, Sunday or a legal holiday, the filing/payment date is deemed to be on the next business day. **KRS 446.030(1)(a)**

Extensions—An extension of time to file an S Corporation Income Tax and LLET Return may be obtained by either making a specific request to the Department of Revenue or attaching a copy of the federal extension to the return when filed. **A copy of the federal extension submitted after the return is filed does not constitute a valid extension, and late filing penalties will be assessed.** If an S corporation is making a payment with its extension, Kentucky Form 41A720SL must be used. For further information, see the instructions for Form 41A720SL. **Regulation 103 KAR 15:050**

NOTE: An extension of time to file a return does not extend the date for payment of tax.

Corporation Estimated Taxes

The Corporation/Limited Liability Entity Estimated Tax Voucher, Form 720ES, is used to submit estimated tax payments for corporation income and LLET. See **Electronic Funds Transfer (EFT)** on this page. If the corporation is required to make estimated tax payments but did not receive Form 720ES, contact the Department of Revenue at (502) 564-3658 or visit the Web site at www.revenue.ky.gov.

NOTE: See www.revenue.ky.gov for information on the 2008 estimated tax payments.

Corporation Estimated Tax Payments—Estimated tax payments must be made by each S corporation whose income tax and LLET liability for the taxable year can reasonably be expected to exceed \$5,000. The first estimated tax payment must be made by the 15th day of the 6th month of the taxable year. To determine the amount of the first payment, subtract \$5,000 from the estimated full-year tax liability, and divide the result by two. The remaining one-half is due in equal installments on the 15th day of the 9th and 12th month, respectively.

Failure to pay estimated tax installments equal to the amount determined by first subtracting \$5,000 from 70 percent of the total tax due under KRS 141.040 and computed by the taxpayer on the return filed for the tax year will result in the assessment of an underpayment penalty. The amount of the penalty is 10 percent of the amount of the underpayment, but not less than \$25. Form 2220-K, Underpayment of Estimated Income Tax by Corporations, must be attached. **KRS 131.180(3), KRS 141.990(3) and Regulation 103 KAR 15:050**

Corporation Estimated Tax—Safe Harbor—Every corporation subject to taxation under KRS 141.040 and/or KRS 141.0401 shall make a declaration of estimated tax and must pay installments if the taxes imposed by KRS 141.040 and/or KRS 141.0401 for the taxable year can reasonably be expected to exceed \$5,000. A corporation that has a prior year income tax liability less than or equal to \$25,000 and fails to make estimated payments equal to its prior year tax liability **or** has a prior year income tax liability greater than \$25,000 and fails to pay at least 70 percent of the income tax liability less \$5,000 will be subject to a penalty of 10 percent of any underpayment of any installment. **KRS 141.042, KRS 141.044(1) and KRS 141.990**

Other Information

Amended Return—To correct Form 720S as originally filed, file an amended Form 720S and check the appropriate box on page 1. If the amended return results in a change in income or a change in the distribution of any income or other information provided to shareholders, an amended Schedule K-1 (Form 720S) must also be filed with the amended Form 720S and given to each shareholder. Check Item E(2) on each Schedule K-1 to indicate that it is an amended Schedule K-1.

Records Retention—The Department of Revenue deems acceptable virtually any records retention system which results in an essentially unalterable method of records storage and retrieval, provided: (a) authorized Department of Revenue personnel are granted access, including any specialized equipment; (b) taxpayer maintains adequate back-up; and (c) taxpayer maintains documentation to verify the retention system is accurate and complete.

Internal Revenue Service Audit Adjustments—An S corporation which has received final adjustments resulting from Internal Revenue Service audits must submit a copy of the "final determination of the federal audit" within 30 days of the conclusion of the federal audit. Use Form 720S for reporting federal audit adjustments and check the Amended Return box.

Interest—Interest at the tax interest rate is applied to corporation income tax and LLET liabilities not paid by the date prescribed by law for filing the return (determined without regard to extensions thereof). The tax interest rate for 2008 is available online at www.revenue.ky.gov, or you may contact the Department of Revenue at (502) 564-8139.

Penalties

Failure to file a Kentucky S Corporation Income Tax and LLET Return by the filing date including extensions—2 percent of the tax due for each 30 days or fraction thereof that the return is late (maximum 20 percent). The minimum penalty is \$10 for each tax. **KRS 131.180(1)**

Jeopardy Fee—A \$100 minimum penalty on all nonfiled returns, when the taxpayer fails to file a return or provide information after being requested to do so by the Department of Revenue. **KRS 131.150(2)**

Failure to pay income tax and/or LLET by the payment date— 2 percent of the tax due for each 30 days or fraction thereof that the payment is overdue (maximum 20 percent). The minimum penalty is \$10 for each tax. **KRS 131.180(2)**

Late payment or underpayment of estimated tax— 10 percent of the late payment or underpayment. The minimum penalty is \$25. **KRS 131.180(3)**

Failure or refusal to file a Kentucky S Corporation Income Tax and LLET Return or furnish information requested in writing— 5 percent of the tax assessed for each 30 days or fraction thereof that the return is not filed or the information is not submitted (maximum 50 percent). The minimum penalty is \$100. **KRS 131.180(4)**

Negligence— 10 percent of the tax assessed. **KRS 131.180(7)**

Fraud—50 percent of the tax assessed. **KRS 131.180(8)**

Cost of Collection Fees

- (a) 25 percent on all taxes which become due and owing for any reporting period, regardless of when due. These collection fees are in addition to all other penalties provided by law. **KRS 131.440(1)(a)**
- (b) 25 percent on all taxes assessed and collected by the Department of Revenue for taxable periods ending before December 1, 2001. **KRS 131.440(1)(b)**
- (c) 50 percent of any tax deficiency assessed after the amnesty period for nonfiled returns eligible for amnesty. **KRS 131.440(1)(c)**

FORM 720S—SPECIFIC INSTRUCTIONS

Period Covered—File the 2007 return for calendar year 2007 and fiscal years that begin in 2007. For a fiscal year, fill in the taxable period beginning and ending at the top of Form 720S.

All S corporations must enter Taxable Year Ending at the top right of Form 720S and supporting forms and schedules to indicate the ending month and year for which the return is filed.

- A calendar year is a period from January 1 through December 31 each year. This would be entered as:

1 2 / 0 7
Mo. Yr.

- A fiscal year is 12 consecutive months ending on the last day of any month except December. A fiscal year ending January 31, 2008, would be entered as:

0 1 / 0 8
Mo. Yr.

- A 52/53-week year is a fiscal year that varies between 52 and 53 weeks. Example: A 52/53-week year ending the first week of January 2008, would be entered as:

1 2 / 0 7
Mo. Yr.

Failure to properly reflect the **Taxable Year Ending** may result in delinquency notices or billings for failure to file.

Item A—Enter the six-digit Kentucky corporation/LLET account number on the applicable line at the top of each form and schedule and on all checks and correspondence. This number was included in correspondence received from the Department of Revenue at the time of registration.

If the account number is not known, telephone (502) 564-8139.

Item B—Check the box indicating the method used in determining the amount of LLET due on the Schedule LLET, Section D, line 1.

LLET Nonfiling Status Code—Return Not Required

If the S corporation is not required to file an LLET return, enter one of the following two-digit codes in the space provided.

REASON CODE	Reason
10	A public service corporation subject to tax under KRS 136.120.
11	An open-end registered investment company organized under the laws of this state and registered under the Investment Company Act of 1940.
12	A property or facility which has been certified as a fluidized bed energy production facility as defined in KRS 211.390.
13	An alcohol production facility as defined in KRS 247.910.
14	A real estate investment trust as defined in Section 856 of the Internal Revenue Code.
15	A captive real estate investment trust as defined in KRS 141.010(29).
16	A regulated investment company as defined in Section 851 of the Internal Revenue Code.
17	A real estate mortgage investment conduit as defined in Section 860D of the Internal Revenue Code.
18	A personal service corporation as defined in Section 269A(b)(1) of the Internal Revenue Code.
19	A cooperative described in Sections 521 and 1381 of the Internal Revenue Code, including farmers' agricultural and other cooperatives organized or recognized under KRS Chapter 272, advertising cooperatives, purchasing cooperatives, homeowners associations including those described in Section 528 of the Internal Revenue Code, political organizations as defined in Section 527 of the Internal Revenue Code and rural electric and rural telephone cooperatives.

Item C—Income Tax Nonfiling Status Code—Return Not Required

If the S corporation is not required to file an income tax return, enter the following two-digit code in the space provided.

REASON CODE	Reason
21	This return contains only the LLET as the corporation is exempt from income tax as provided by Public Law 86-272.

Item D—Enter the S corporation's federal identification number. See federal Publication 583 if the corporation has not obtained this number.

Name and Address—Print or type the corporation's name as set forth in the charter. For the address, include the suite, room or other unit number after the street address. If the U.S. Postal Service does not deliver mail to the street address and the corporation has a P.O. Box, show the box number instead of the street address (check the box if a change in name or address has occurred).

Telephone Number—Enter the business telephone number of the principal officer or chief accounting officer signing this return.

State and Date of Incorporation—Enter the state and date of incorporation of the corporation filing this return.

Principal Business Activity in Kentucky—Enter the principal business activity of the corporation filing this return.

North American Industrial Classification System (NAICS)—Enter your six-digit NAICS code. To view a complete listing of NAICS codes, visit the United States Census Bureau at www.census.gov.

Item E—Check the applicable boxes:

- (a) *Qualified Investment Pass-through Entity*—Check the box to indicate the S corporation is a qualified investment pass-through entity as provided by KRS 141.206(12)(a).
- (b) *LLC*—Check this box if S corporation is organized as a limited liability company (LLC).
- (c) *Initial Return*—Check this box if this is the corporation's first time filing an S corporation income tax return in Kentucky. Complete questions 1, 2 and 3 on Form 720S, page 2, Schedule Q, Kentucky Corporation Questionnaire.
- (d) *Final Return*—Check this box if this is the S corporation's final return. The S corporation has dissolved or withdrawn. Submit an explanation.
- (e) *Short-period Return*—Check this box and submit an explanation for a short-period return that is not an initial return.
- (f) *Amended Return*—Check this box if this is an amended return. Attach statement giving explanation of changes to net income, apportionment factor and/or taxes.

Item F—Enter the number of shareholders on the first line, and enter the number of QSSSs included on this return on the second line.

PART I—ORDINARY INCOME (LOSS) COMPUTATION

Line 1—Enter the amount from federal Form 1120S, Line 21, ordinary income (loss) from trade or business activities. **Attach**

Form 1120S, pages 1, 2, 3 and 4.

Additions to Federal Ordinary Income—Lines 2, 3, 4 and 5 itemize items of additional income or unallowed deductions which are differences between federal ordinary income and Kentucky ordinary income.

Line 2—Enter state taxes measured in whole or in part by gross or net income. "State" means any state of the United States, the District of Columbia, the commonwealth of Puerto Rico, any territory or possession of the United States or any foreign country or political subdivision thereof. Attach a schedule reflecting the total taxes deducted on federal Form 1120S. **KRS 141.010(13)(a)**

Line 3—Enter federal depreciation (do not include Section 179 deduction). See instructions on page 5 regarding depreciation and Section 179 deduction. If a federal Form 4562 is required to be filed for federal income tax purposes, a copy must be attached.

Line 4—Enter related party and intangible expenses prohibited by KRS 141.205.

Line 5—Enter other differences which result in additions to federal ordinary income in computing Kentucky ordinary income:

- (a) See instructions on page 5 regarding **differences in gain or loss from disposition of assets**. If applicable, include the amount of loss reported on Line 4 of federal Form 1120S and the amount of gain from Line 17 of Kentucky converted Form 4797. **Federal Form 4797 filed with the federal return and the Kentucky converted Form 4797 must be attached.**
- (b) To determine the allowable depletion deduction for Kentucky purposes, the percentage limitations provided by the IRC must be applied to Kentucky gross/net income rather than federal gross/net income. **KRS 141.050**
- (c) Any difference in the gain (loss) upon disposition of intangible assets resulting from a difference between the accumulated federal amortization deduction and the accumulated Kentucky amortization deduction. **Regulation 103 KAR 15:090**

Line 6—Enter the total of Lines 1, 2, 3, 4 and 5.

Subtractions from Federal Ordinary Income—Lines 7 through 9 itemize items of additional deductions allowed which are differences between federal ordinary income and Kentucky ordinary income.

Line 7—Enter the amount of the work opportunity credit reflected on federal Form 5884. For Kentucky purposes, the S corporation may deduct the total amount of salaries and wages paid or incurred for the taxable year. **This adjustment does not apply for other federal tax credits.**

Line 8—Enter Kentucky depreciation (do not include Section 179 deduction). See instructions on page 5 regarding depreciation and Section 179 deduction differences, and if applicable, Kentucky converted Form 4562 must be attached.

Line 9—Enter other differences which result in subtractions to federal ordinary income in computing Kentucky ordinary income:

- (a) See instructions on page 5 regarding **differences in gain or loss from disposition of assets**. If applicable, include the amount of gain reported on Line 4 of federal Form 1120S and the amount of loss from Line 17 of Kentucky converted Form 4797. **Federal Form 4797 filed with the federal return and the Kentucky converted Form 4797 must be attached.**

- (b) To determine the allowable depletion deduction for Kentucky purposes, the percentage limitations provided by the IRC must be applied to Kentucky gross/net income rather than federal gross/net income. **KRS 141.050**
- (c) Any difference in the gain (loss) upon disposition of intangible assets resulting from a difference between the accumulated federal amortization deduction and the accumulated Kentucky amortization deduction. **Regulation 103 KAR 15:090**

Line 10—Subtract Lines 7, 8 and 9 from Line 6.

PART II – LLET COMPUTATION

Line 1—Enter the amount from Schedule LLET, Section D, Line 1. An S corporation must use Schedule LLET(K), Limited Liability Entity Tax for Pass-through Entities with Economic Development Project(s), if the S corporation has one or more projects under the Kentucky Rural Economic Development Act (KREDA), Kentucky Industrial Development Act (KIDA), Kentucky Job Development Act (KJDA), Kentucky Economic Opportunity Zone (KEOZ) or Kentucky Industrial Revitalization Act (KIRA).

Line 2—**This line is not used for 2007.** There is no recapture of the recycling/composting equipment credit for LLET purposes as the credit was not taken against the LLET in a prior year.

Line 3—Enter the total of Lines 1 and 2.

Line 4—Enter the nonrefundable LLET credit from Kentucky Schedule(s) K-1 of which the S corporation is a partner or member. **Copies of Kentucky Schedule(s) K-1 must be attached to the S corporation return in order to claim the credit.**

Line 5—Enter the total tax credits from Schedule TCS, Part III, Column E.

Line 6—Enter the greater of Line 3 less Lines 4 and 5, or \$175.

Line 7—Enter the total LLET estimated tax payments made for the taxable year. Do not include the amount credited from prior year.

Line 8—Enter the amount of LLET paid with Form 41A720SL, Application for Six-Month Extension of Time to File Kentucky Corporation Income Tax Return.

Line 9—Enter the amount credited to 2007 LLET from Part III, Line 11, of the 2006 return.

Line 10—Enter the 2007 income tax overpayment credited to the 2007 LLET from Part III, Line 10.

Line 11—If Line 6 is greater than the total of Lines 7 through 10, enter the difference on this line and enter the amount in the Tax Payment Summary.

Line 12—If Line 6 is less than the total of Lines 7 through 10, enter the difference on this line.

Line 13—Enter the portion of Line 12 to be credited to the 2007 income tax, enter the amount on this line and Part III, Line 7.

Line 14—Enter the portion of Line 12 to be credited to 2008 LLET.

Line 15—Enter the portion of Line 12 to be refunded (Line 12 less Lines 13 and 14).

PART III – INCOME TAX COMPUTATION

Line 1—Enter tax from the Excess Net Passive Income Tax Worksheet, Line 13. (See instructions and worksheet on page 15.)

If the corporation has accumulated earnings and profits (AE&P) at the close of its tax year, has passive investment income for the tax year that is in excess of 25% of gross receipts, and has taxable income at year-end, the corporation must pay a tax on the excess net passive income as provided by KRS 141.040(14)(c). Complete Lines 1 through 3 and Line 9 of the worksheet on page 15 to make this determination. If Line 2 is greater than Line 3 and the corporation has taxable income (see instructions for Line 9 of worksheet), it must pay the tax. **Attach completed worksheet to the return.**

Line 2—Enter the built-in gains tax from the Built-In Gains Tax Worksheet, Line 8. **Attach completed worksheet to the return.** (See instructions and worksheet on page 15.)

Section 1374(d)(3) of the Internal Revenue Code defines a recognized built-in gain as any gain recognized during the recognition period (the 10-year period beginning on the first day of the first year for which the corporation is an S corporation, or beginning the date the asset was acquired by the S corporation, for an asset with a basis determined by reference to its basis (or basis of any other property) in the hands of a C corporation) on the sale or distribution (disposition) of any asset, except to the extent the corporation establishes that: (1) the asset was not held by the corporation as of the beginning of the first tax year the corporation was an S corporation (except this does not apply to an asset acquired by the S corporation with a basis determined by reference to its basis (or the basis of any property) in the hands of the C corporation), or (2) the gain exceeds the excess of the fair market value of the asset as of the start of the first tax year (or as of the date the asset was acquired by the S corporation, for an asset with a basis determined by reference to its basis (or the basis of any other property) in the hands of the C corporation) over the adjusted basis of the asset at that time. Certain transactions involving the disposal of timber, coal, or domestic iron ore under section 631 are not subject to the built-in gains tax. See Rev. Rul. 2001-50, 2001-43 I.R.B. 343.

Section 1374(d)(4) of the Internal Revenue Code defines a recognized built-in loss as any loss recognized during the recognition period (defined above) on the disposition of any asset to the extent the corporation establishes that: (1) the asset was held by the corporation as of the beginning of the first tax year the corporation was an S corporation (except that this does not apply to an asset acquired by the S corporation with a basis determined by reference to its basis (or the basis of any property) in the hands of a C corporation), and (2) the loss does not exceed the excess of the adjusted basis of the asset as of the beginning of the first tax year (or as of the date the asset was acquired by the S corporation, for an asset with a basis determined by reference to its basis (or the basis of any other property) in the hands of a C corporation), over the fair market value of the asset as of that time.

Line 3—**This line is not applicable to 2007** as the first installment is paid on the C Corporation's final return.

Line 4—Enter the total of Lines 1, 2, and 3.

Line 5—Enter the total of the income tax estimated tax payments made for the taxable year. Do not include the amount credited from prior year. Check the box if Form 2220-K is attached.

Line 6—Enter the amount of income tax paid with Form 41A720SL, Application for Six-Month Extension of Time to File Kentucky Corporation Income Tax Return.

Line 7—Enter the 2007 LLET overpayment credited to the 2007 income tax from Part II, Line 13.

Line 8—If Line 4 is greater than the total of Lines 5 through 7, enter the difference on this line and enter the amount in the Tax Payment Summary.

Line 9—If Line 4 is less than the total of Lines 5 through 7, enter the difference on this line.

Line 10—Enter the portion of Line 9 to be credited to the 2007 LLET, enter the amount on this line and Part II, Line 10.

Line 11—Enter the portion of Line 9 to be credited to 2008 income tax.

Line 12—Enter the portion of Line 9 to be refunded (Line 9 less Lines 10 and 11).

SCHEDULE K (FORM 720S)

General Instructions—Complete all applicable lines entering the total pro rata share amount for each item listed. Federal instructions for Form 1120S and federal Schedule K provide additional information which will assist the S corporation in completing Schedule K, Form 720S.

An S corporation must use Form 41A720S(K), Schedule K, for S corporations with Economic Development Project(s), if the S corporation has one or more projects under the Kentucky Rural Economic Development Act (KREDA), Kentucky Industrial Development Act (KIDA), Kentucky Jobs Development Act (KJDA), Kentucky Economic Opportunity Zone (KEOZ) or Kentucky Industrial Revitalization Act (KIRA).

NOTE: Banks and savings and loan associations see special instructions under Tax Treatment of S Corporation and Shareholder(s) on page 6 of these instructions.

Section I—Income (Loss) and Deductions

Line 1—Enter Kentucky ordinary income (loss) from Form 720S, Part I, Line 10.

Line 2—Enter net income (loss) from rental real estate activities reported on federal Schedule K, Form 1120S, adjusted to reflect any differences in Kentucky and federal income tax laws.

Line 3(a)—Enter the gross income from other rental activities reported on federal Schedule K, Form 1120S.

Line 3(b)—Enter the expenses from other rental activities reported on federal Schedule K, Form 1120S, adjusted to reflect any differences in Kentucky and federal income tax laws.

Line 3(c)—Enter the difference of Line 3(a) and Line 3(b).

Line 4(a)—Enter interest income from federal Schedule K, Form 1120S, adjusted to exclude tax-exempt U.S. government interest, if any, and to include interest income from obligations of states other than Kentucky and their political subdivisions.

Lines 4(b) and 4(c)—Enter the amount of dividend and royalty income reported on federal Schedule K, Form 1120S.

Line 4(d)—See page 5 of the 2007 Form 720S instructions regarding **differences in gain or loss from disposition of assets**, and if applicable, enter the amount from Line 6 of the Kentucky converted Schedule D that is portfolio income. Report any gain or loss that is not portfolio income on Line 6, Schedule K, Form 720S. **Kentucky converted Schedule D must be attached to Form 720S.** Otherwise, enter the amount from Line 6 of the federal

Schedule D (Form 1120S) that is portfolio income.

Line 4(e)—See page 5 of the 2007 Form 720S instructions regarding **differences in gain or loss from disposition of assets**, and if applicable, enter the amount from Line 13 of the Kentucky converted Schedule D that is portfolio income. Report any gain or loss that is not portfolio income on Line 6, Schedule K, Form 720S. **Kentucky converted Schedule D must be attached to Form 720S.** Otherwise, enter the amount from Line 13 of the federal Schedule D (Form 1120S) that is portfolio income.

Line 4(f)—Enter any other portfolio income not reported on Lines 4(a) through 4(e), Schedule K, Form 720S.

Line 5—See page 5 of the 2007 Form 720S instructions regarding **differences in gain or loss from disposition of assets**. If applicable, enter the amount from Line 7 of the Kentucky converted Form 4797, and **Kentucky converted Form 4797 must be attached to Form 720S.** Otherwise, enter net gain (loss) under Section 1231 from federal Form 4797. Do not include net gains (losses) from involuntary conversions due to casualties or thefts on this line. Instead, report them on Line 6.

Line 6—Enter all other items of income (loss) of the S corporation not included on Lines 1 through 5. See federal instructions for Schedule K, Form 1120S.

Line 7—Enter total contributions paid by the S corporation during its taxable year and attach a schedule showing separately the contributions subject to the 50 percent, 30 percent and 20 percent limitations. These percentage limitations must be applied to the Kentucky amounts rather than the federal amounts.

Also, enter amount of deduction allowable from Schedule HH for the value of leasehold interest of property donated for living quarters for a homeless family. The ordinary charitable contribution deduction must be reduced by any amount attributable to property on which this deduction is taken.

Line 8—See page 5 of the 2007 Form 720S instructions regarding **depreciation and Section 179 deduction differences**, and if applicable, include the amount from Line 12 of the Kentucky converted Form 4562. **Kentucky converted Form 4562 must be attached.** Otherwise, enter Section 179 deduction from federal Form 4562.

Line 9—Enter the expenses related to portfolio income reported on federal Schedule K, Form 1120S, adjusted to exclude expenses related to tax-exempt interest income and other exempt income.

Line 10—Enter any other deductions of the S corporation not included on Lines 7, 8 and 9. See federal instructions for Schedule K, Form 1120S.

Line 11(a)—Enter the S corporation's deductible interest expense allocable to debt on property held for investment purposes. Property held for investment purposes includes property that produces investment income (interest, dividends, annuities, royalties, etc.). The total amount entered should equal the amount of interest expense reported on federal Schedule K, Form 1120S, adjusted to exclude any interest expense on debts incurred to purchase or carry investment property producing, or held for the production of, U.S. government interest income.

Lines 11(b)(1) and (b)(2)—Enter only the investment income included on Lines 4(a), 4(b), 4(c) and 4(f), Schedule K, Form 720S, and only the investment expenses related thereto included on Line 9, Schedule K, Form 720S. See federal instructions for Schedule K, Form 1120S.

Line 12—Enter the Skills Training Investment Credit Act (STICA) tax credit as provided by KRS 141.405 and attach a copy of the final resolution received from the Bluegrass State Skills Corporation.

Line 13—Enter the Historic Preservation Restoration Tax Credit as provided by KRS 171.397 and attach a copy of the final resolution received from the Kentucky Heritage Council.

Line 14—Enter the Kentucky Unemployment Tax Credit as provided by KRS 141.065 and attach Kentucky Schedule UTC (Form 42A740-UTC).

Line 15—Enter the Recycling and Composting Equipment Tax Credit as provided by KRS 141.390 and attach Kentucky Schedule RC (Form 41A720RC).

Line 16—Enter the Kentucky Investment Fund Tax Credit as provided by KRS 154.20-258 and attach a copy of the notification from Kentucky Economic Development Finance Authority (KEDFA) reflecting the amount of credit granted and the year in which the credit may first be claimed.

Line 17—Enter the Coal Incentive Tax Credit for electric power generation as provided by KRS 141.0405 and attach Kentucky Schedule CI (Form 41A720-CI).

Line 18—Enter the Qualified Research Facility Tax Credit as provided by KRS 141.395 and attach Kentucky Schedule QR (Form 41A720QR).

Line 19—Enter the GED Incentive Tax Credit as provided by KRS 151B.127 and attach GED-Incentive Program Final Report (Form DAEL-31) for each employee that completed a learning contract during the year.

Line 20—Enter the Voluntary Environmental Remediation Tax Credit (Brownfield) as provided by KRS 141.418 and attach Kentucky Schedule VERB (Form 41A720VERB).

Line 21—Enter the Biodiesel Tax Credit as provided by KRS 141.424 and attach Kentucky Schedule BIO (Form 41A720BIO).

Line 22—Enter the Environmental Stewardship Tax Credit as provided by KRS 141.430 and attach Kentucky schedule.

Line 23—Enter the Clean Coal Incentive Tax Credit as provided by KRS 141.428 and attach Kentucky schedule.

Line 24(a)—Enter the information provided on federal Schedule K, Form 1120S, Line 12c(1).

Line 24(b)—Enter the amount reported on federal Schedule K, Form 1120S, Line 12c(2).

Line 25—Enter the total amount of interest income of the S corporation from U.S. government bonds and securities and obligations of Kentucky and its political subdivisions.

Line 26—Enter the total amount of any other type of income of the S corporation on which the shareholder is exempt from Kentucky income tax.

Line 27—Enter the total amount of nondeductible expenses paid or incurred by the S corporation including, but not limited to, state taxes measured by gross/net income, expenses related to tax-exempt income, etc. Do not include a deduction reported elsewhere on Schedule K, Form 720S, capital expenditures or items the deductions for which are deferred to a later year.

Line 28—Enter the amount reported on federal Schedule K, Form 1120S, Line 16d.

Line 29—Attach schedules to report the S corporation's total income, expenses and other information applicable to items not included on Lines 1 through 11 and lines 24 through 28 including, but not limited to, any recapture of Section 179 deduction, gross income and other information relating to oil and gas well properties enabling the shareholders to figure the

allowable depletion deduction, and any other information the shareholders need to prepare their Kentucky income tax returns. See federal instructions for Schedule K, Form 1120S, Line 17d.

Kentucky domestic production activities deduction (KDPAD): KDPAD is only computed for corporations as defined in KRS 141.010(24). General partnerships (Form 765-GP), limited liability partnerships (Form 765), S corporations (Form 720S) and individually owned single member LLC(s) (Form 725 or Schedule CP, Form 725) shall provide for partners/shareholders/members that are corporations, individual nonresidents, estates, trusts or general partnerships the Kentucky domestic production gross receipts, the federal domestic production gross receipts, and Kentucky wages. In addition, general partnerships shall provide the Kentucky qualified production activities income from the general partnership to its partners or the necessary Kentucky information to compute this amount. Attach this information to this return and the distributive share to each Schedule K-1. Also, see additional instructions on Kentucky Form 8903-K.

Line 30—Enter the amount reported on federal Schedule K, Form 1120S, Line 17c.

Line 31—Enter the recapture of Recycling and Composting Equipment Tax Credit as provided by KRS 141.390 and attach Kentucky Schedule RC-R (41A720RC-R).

Section II – LLET Pass-through Items

Lines 1 through 8 of this section do not need to be completed unless the S corporation has a shareholder that is a single member individually owned limited liability company disregarded for federal tax purposes. In order to enter correct amounts on lines 1 through 8, Schedule A (Form 41A720A) must be completed and attached to the return.

Line 1—Enter the S corporation's Kentucky sales from Schedule A, Section I, Line 1.

Line 2—Enter the S corporation's total sales from Schedule A, Section I, Line 2.

Line 3—Enter the S corporation's Kentucky property from Schedule A, Section I, Line 5.

Line 4—Enter the S corporation's total property from Schedule A, Section I, Line 6.

Line 5—Enter the S corporation's Kentucky payroll from Schedule A, Section I, Line 8.

Line 6—Enter the S corporation's total payroll from Schedule A, Section I, Line 9.

Line 7—Enter the S corporation's Kentucky gross profits from Schedule LLET, Section A, Column A, Line 5.

Line 8—Enter the S corporation's total gross profits from Schedule LLET, Section A, Column B, Line 5.

Line 9—Enter the limited liability entity tax (LLET) nonrefundable credit from page 1, Part II, the total of Lines 4 and 6, less \$175.

Tax Payment Summary

The payment submitted with Form 720S must be itemized. Enter the amount of LLET payment from Part II, Line 11 and/or corporation income tax payment from Part III, Line 8 on the applicable tax payment lines in addition to its respective amount of penalties and interest. Subtotal each and enter the total payment on the Total Payment line.



Signature—Form 720S must be signed by an authorized corporate officer. Failure by corporate officers to sign the return, to complete all applicable lines on any required Kentucky form, to attach all applicable schedules including copies of federal forms, or to complete all information on the questionnaire will delay the processing of tax returns and may result in the assessment of penalties.

SCHEDULE K-1 (FORM 720S)—KENTUCKY SHAREHOLDER'S SHARE OF INCOME, CREDITS, DEDUCTIONS, ETC.

General Instructions

Schedule K-1 (Form 720S) shows each shareholder's pro rata share of the S corporation's income, deductions, credits, etc. On each Schedule K-1 (Form 720S) enter the names, addresses and identifying numbers of the shareholder and S corporation, and complete items A, B, C, D and E. All shareholders' names, Social Security or identifying numbers and other shareholder information must be complete and legible. Schedule K-1 (Form 720S) must be completed and given to each shareholder with instructions on or before the day on which Form 720S is filed with the Department of Revenue.

A copy of each shareholder's K-1 (Form 720S) must be attached to Form 720S filed with the Department of Revenue, and a copy kept as part of the S corporation's records.

Photocopies of Schedule K-1 (Form 720S) may be used in lieu of the official schedule printed by the Department of Revenue, provided the photocopies are on bond paper of at least 16 pounds and are of good quality.

Specific Instructions

Federal instructions for Schedule K-1 (Form 1120S) explain the rules for allocating items of income (loss), deductions, credits, etc., to each shareholder. The total share items reported on all Schedules K-1, Column (b), Lines 1 through 31 must equal the amounts reported on Schedule K, Lines 1 through 31. The total share items reported on all Schedules K-1, Column (b), Lines 32 through 40 must equal the amounts reported on the

comparable lines of Schedule K, Section II, Lines 1 through 9. Schedule K-1, Column (b), Lines 41 through 43 do not correspond with Schedule K.

Multiple Activities—If items of income, loss or deduction from more than one activity are reported on Lines 1, 2 or 3 of Schedule K-1 (Form 720S), the S corporation must provide information for each activity to its shareholders. See **Passive Activity Reporting Requirements** in the instructions for Schedule K-1 (Form 1120S) for details on the information to be provided on an attachment to Schedule K-1 (Form 720S) for each activity.

At-Risk Activities—If the S corporation is involved in one or more at-risk activities for which a loss is reported on Schedule K-1 (Form 720S), the S corporation must report information separately for each at-risk activity. See **Special Reporting Requirements for At-Risk Activities** in the federal instructions for Schedule K-1 (Form 1120S) for details on the information to be provided on an attachment to Schedule K-1 (Form 720S) for each at-risk activity.

Lines 1 through 40—Enter the shareholder's total pro rata share of each item listed on Schedule K, Form 720S. **Do not multiply these amounts by the percentage entered on Item B(2).** Attach schedules showing separately the required information for each IRC Section 469 passive activity and each Section 465 at-risk activity. Other schedules are to be attached for line items where requested on Schedule K-1 (Form 720S).

Enter on attached schedules the supplemental information required to be reported separately to each shareholder for Lines 1 through 40 and any other information or items and amounts not included on Schedule K-1 (Form 720S) for which the shareholder needs to prepare a Kentucky income tax return including, but not limited to, any recapture of Section 179 deduction, gross income and other information relating to oil and gas well properties enabling the shareholder to figure the allowable depletion deduction, etc. See instructions for federal Schedule K-1 (Form 1120S), Line 17.

Lines 41 through 43—The amounts in Column (b) are to be entered by the shareholder, not the S corporation.

Instructions for Excess Net Passive Income Tax Worksheet:

1. Enter the gross receipts for the tax year as defined in Section 1362(d)(3)(B) of the Internal Revenue Code. Income on Line 1 is from total operations for the year and includes income from Form 720S, Part I as well as income reported separately on Schedule K.
2. Enter the passive investment income as defined in Section 1362(d)(3)(C) of the Internal Revenue Code. Deductions on Line 2 are from total operations for the year and include deductions from Form 720S, Part I as well as those reported separately on Schedule K. See Section 1375(b)(4) of the Internal Revenue Code for an exception regarding this line.
3. Enter 25% of the amount on Line 1 (If Line 2 is less than Line 3, stop here. You are not liable for this tax.)
4. Enter the amount of Line 2 less Line 3.
5. Enter deductions directly connected with the production of income on Line 2 (See Section 1375(b)(2) of the Internal Revenue Code). Deductions on Line 5 are from total operations for the year and include deductions from Form 720S, Part I as well as those reported separately on Schedule K. See Section 1375(b)(4) of the Internal Revenue Code for an exception regarding this line.
6. Enter the amount of Line 2 less Line 5. This is your Net Passive Income.
7. Enter the amount of Line 4 divided by the amount on Line 2.
8. Enter the amount of Line 6 multiplied by Line 7. This is your Excess Net Passive Income.
9. Enter taxable income as defined in Section 1.1374-1A(d) of the Treasury Regulations. Figure this income by completing Form 720, Part I, lines 1 through 18. Include the Form 720 computation with the worksheet computation you attach to Form 720S. You do not have to attach the schedules, etc., called for on Form 720. However, you may want to complete certain Form 720 schedules, such as Kentucky converted Schedule D, if you have capital gains or losses.
10. Enter the lesser of the amount from Line 8 or Line 9.
11. Enter 100% or if taxable in Kentucky and taxable in another state, the apportionment factor from Schedule A, Section I, Line 12.
12. Enter the amount on Line 10 multiplied by the percentage on Line 11.
13. Excess net passive income tax—enter 6% of Line 12. Enter here and on Form 720S, Part III, Line 1.

**Excess Net Passive Income Tax Worksheet
(Attach this Worksheet to Form 720S)**

1. Enter gross income receipts for the tax year as defined in IRC Section 1362(d)(3)(B)
2. Enter passive investment income as defined in IRC Section 1362(d)(3)(C)
3. Enter 25% of line 1 (If line 2 is less than line 3, stop here. You are not liable for the tax.)
4. Enter line 2 less line 3 (This is your excess passive investment income.)
5. Enter deduction directly connected with the production of income on line 2 (see instructions)
6. Enter line 2 less line 5 (This is your net passive income.)
7. Line 4 divided by the amount on line 2
8. Multiply line 6 by line 7 (This is your excess net passive income.)
9. Enter taxable income (see instructions)
10. Enter the lesser of the amount on line 8 or line 9
11. Enter 100% or the apportionment factor from Schedule A, Section I, line 12
12. Multiply the amount on Line 10 by the percentage on line 11
13. Enter 6% of line 12 on this line and on Form 720S, Part III, line 1

Instructions for Built-in Gains Tax Worksheet:

1. Enter the amount that would be the taxable income of the corporation for the tax year if only recognized built-in gains (including any carryover of gain under Section 1374(d)(2)(B) of the Internal Revenue Code) and recognized built-in losses were taken into account.
2. Figure taxable income by completing Form 720, Part II, Lines 1 through 18. Follow the instructions for Form 720. Enter the amount from Form 720, Part II, Line 18 on Line 2 of the Built-in Gains Tax Worksheet.
3. Enter the lesser of the amount from Line 1 or Line 2. If for any year the amount on Line 1 exceeds the taxable amount on Line 2, the excess is treated as a recognized built-in gain in the succeeding tax year.
4. Enter the IRC Section 1374(b)(2) deduction. Generally, this is any net operating loss carryforward (to the extent of net capital gain included in recognized built-in-gain for the tax year) arising in tax years for which the corporation was a C corporation. See Section 1374(b)(2) of the Internal Revenue Code and Section 1.1374-5 of the Treasury Regulations.
5. Enter the amount of Line 3 less Line 4. If zero or less, enter zero here and on Line 8.
6. Enter 100% or the apportionment factor from the last C corporation return, Schedule A, Section I, Line 12.
7. Enter the amount on Line 5 multiplied by the percentage on Line 6.
8. Multiply the amount on Line 7 by 6% and enter the amount on this line and on Form 720S, Part III, Line 2, and attach computation to Form 720S.

**Built-in Gains Tax Worksheet
(Attach this Worksheet to Form 720S)**

1. Excess of recognized built-in gains over recognized built-in losses (see instructions)
2. Taxable income (see instructions)
3. Net recognized built-in gains. Enter the lesser of Line 1 or Line 2
4. Section 1374(b)(2) deduction
5. Enter Line 3 less Line 4. If zero or less enter zero here and on Line 8
6. Enter 100% or the apportionment factor from the last C corporation return, Schedule A, Section I, Line 12
7. Multiply the amount on Line 5 by the percentage on Line 6, and enter the amount
8. Enter 6% of Line 7 on this line and on Form 720S, Part III, Line 2

Tax Credit Summary Schedule—Schedule TCS

Schedule TCS is used by corporations and limited liability pass-through entities to apply tax credits for entities subject to the corporation income tax imposed under KRS 141.040 and/or the limited liability entity tax (LLET) imposed under KRS 141.0401. The amount of tax credit against each tax can be different. *Taxpayer* as used in this section refers to corporations and limited liability pass-through entities.

Economic Development Tax Credits—This section is completed only if the taxpayer has been approved for one or more of the credits authorized by the Kentucky Rural Economic Development Act (KREDA–KRS 154.22), the Kentucky Jobs Development Act (KJDA–KRS 154.24), the Kentucky Industrial Revitalization Act (KIRA–KRS 154.26), the Kentucky Industrial Development Act (KIDA–KRS 154.28), the Kentucky Economic Opportunity Zone (KEOZ–KRS 154.23), the Skills Training Investment Credit Act (STICA–KRS 154.12–2084 to 2089), the Kentucky Reinvestment Act (KRA–KRS 154.34), or the Kentucky Jobs Retention Agreement (KJRA–KRS 154.25). **If an amount is entered, the return and applicable schedules must be mailed to Economic Tax Credits, Tax Credits Section, Department of Revenue, P.O. Box 181, Frankfort, KY 40602-0181.**

To qualify for the KREDA, KJDA, KIRA, KIDA, KEOZ, KRA or KJRA credits, the taxpayer must be approved by the Kentucky Economic Development Finance Authority (KEDFA) and have executed and activated the appropriate agreement with KEDFA. Form(s) and instructions for the computation of the credit(s) will be mailed to the approved taxpayer. To claim any of these credits, the applicable tax credit schedule must be attached.

To claim the STICA credit, a copy of the final authorizing resolution received from the Bluegrass State Skills Corporation reflecting the amount of credit awarded must be attached. The credit shall be claimed on the income tax return filed for the taxable year during which the final authorizing resolution is adopted by the Bluegrass State Skills Corporation. If the amount of the credit exceeds the income tax liability for the taxable year during which the final authorizing resolution is adopted by the Bluegrass State Skills Corporation, the excess may be carried forward for three successive years. If the credit claimed is being carried forward from a prior year, attach a schedule reflecting the computation of the amount of credit available to be carried forward in addition to the final authorizing resolution from the Bluegrass State Skills Corporation.

Economic Development Credits are allowed against the taxes imposed by KRS 141.040 and KRS 141.0401.

Information regarding the approval process for these credits may be obtained from the Cabinet for Economic Development, Department of Financial Incentives at (502) 564-4554.

Historic Preservation Restoration Tax Credit—This credit is allowed only if the taxpayer has been approved for the credit by the Kentucky Heritage Council. Credit is allowed against the taxes imposed by KRS 141.020, KRS 141.040, KRS 141.0401 and KRS 136.505 for qualified rehabilitation expenses on certified historic structures. Information regarding this credit is at www.heritage.ky.gov. **KRS 171.397**

Unemployment Tax Credit—If a taxpayer has hired a Kentucky resident classified as unemployed for at least 60 days and the resident remains in the employ of the taxpayer for 180 consecutive days during the tax year (a qualified person), the taxpayer may be entitled to the unemployment tax credit against the taxes imposed by KRS 141.020, KRS 141.040 and KRS 141.0401. For each qualified person, a one-time nonrefundable credit of \$100 may be claimed. The period of unemployment must be certified by the Education Cabinet, Department of Workforce Investment, Office of Employment and Training, Frankfort, KY, and a copy of the certification must be maintained by the taxpayer. For certification questions, call (502) 564-7456. Schedule UTC must be attached to the return claiming this credit. **KRS 141.065**

Recycling/Composting Tax Credit—A taxpayer, which purchases recycling and/or composting equipment to be used exclusively in Kentucky for recycling or composting post-consumer waste materials, may be entitled to a nonrefundable credit against the taxes imposed by KRS 141.020, KRS 141.040 and KRS 141.0401 in an amount equal to 50 percent of the installed cost of the equipment. Application for this credit must be made on Schedule RC, and a copy of the schedule reflecting the amount of credit approved by the Department of Revenue must be attached to the tax return on which the credit is claimed. The amount of this credit claimed for the tax year may not exceed 25 percent of the tax liability and cannot exceed 10 percent of the credit approved in the first year of eligibility.

For taxable years beginning after December 31, 2004, a taxpayer which purchases recycling and/or composting equipment to be used exclusively in Kentucky for recycling or composting post-consumer waste material that qualifies as a Major Recycling Project is entitled to a nonrefundable credit against the taxes imposed by KRS 141.020, KRS 141.040 and KRS 141.0401. The credit is an amount equal to 50 percent of the installed cost of the recycling or composting equipment limited to: 50 percent of the excess of the total of each tax liability over the baseline tax liability of the taxpayer or \$2,500,000. To qualify, the taxpayer must: (1) invest more than \$10,000,000 in recycling or composting equipment to be used exclusively in this state; (2) have more than 750 full-time employees with an average hourly wage of more than 300 percent of the federal minimum wage; and (3) have plant and equipment with a total cost of more than \$500,000,000. Application for this credit must be made on Schedule RC, and a copy of the schedule reflecting the amount of credit approved by the Department of Revenue must be attached to the tax return on which the credit is claimed. The credit is limited to a period of 10 years commencing with the approval of the recycling credit application.

A taxpayer is entitled to claim the recycling credits in KRS 141.390(a) and (b) but cannot claim both for the same recycling and/or composting equipment.

Enter the amount of additional recycling credit allowed from Schedule RC-R, Disposition of Recycling or Composting Equipment, Line 10. **Schedule RC-R must be attached. KRS 141.390**

Coal Conversion Tax Credit—A corporation which converts boilers from other fuels to the use of Kentucky coal or which substitutes Kentucky coal for other fuels in a boiler capable of burning coal and other fuels to produce energy for specific purposes may be entitled to a credit against the taxes imposed by KRS 141.040 and KRS 141.0401 equal to 4.5 percent of expenditures for Kentucky coal (less transportation costs). Unused portions of this credit may not be carried forward or back. Schedule CC must be attached to the tax return claiming this credit. **KRS 141.041**

Enterprise Zone Tax Credit—The Hopkinsville enterprise zone expired on December 31, 2007 and qualified corporations in this enterprise zone can claim a credit for tax year ended 2007. Previous year carryforwards are allowed for the enterprise zones that previously expired. **Schedule EZC must be attached. KRS 154.45-090**

Kentucky Investment Fund Tax Credit—A taxpayer which makes a cash contribution to an investment fund approved by KEDFA in accordance with KRS 154.20-250 to 154.20-284 is entitled to a nonrefundable credit equal to 40 percent of the investor's proportional ownership share of all qualified investments made

by its investment fund and verified by the authority. The credit may be applied against the taxes imposed by KRS 141.020, KRS 141.040, KRS 141.0401, KRS 136.320, KRS 136.300, KRS 136.310, KRS 136.505 and KRS 304.3-270. **A copy of the notification from KEDFA reflecting the amount of credit granted and the year in which the credit may first be claimed must be attached to the tax return claiming this credit.**

The tax credit amount that may be claimed by an investor in any tax year shall not exceed 50 percent of the initial aggregate credit amount approved by the authority for the investment fund which is proportionally available to the investor. **Example:** *An investor with a 10 percent investment in a fund which has been approved for a total credit to all investors of \$400,000 is limited to \$20,000 maximum credit in any given year (\$400,000 x 10% x 50%).*

If the amount of credit that may be claimed in any tax year exceeds the tax liabilities, the excess credit may be carried forward, but the carryforward of any excess tax credit shall not increase the limitation that may be claimed in any tax year. Any credit not used in 15 years, including the year in which the credit may first be claimed, shall be lost.

Information regarding the approval process for these credits may be obtained from the Cabinet for Economic Development, Department of Financial Incentives at (502) 564-4554.

Coal Incentive Tax Credit—Effective for tax returns filed after July 15, 2001, an electric power company or a company that owns and operates a coal-fired electric generating plant may be entitled to a coal incentive tax credit first against the taxes imposed by KRS 141.020, KRS 141.040 and KRS 141.0401 and then against tax imposed by KRS 136.120. Application for this credit is made on Schedule CI, Application for Coal Incentive Tax Credit, and a copy of the credit certificate issued by the Kentucky Department of Revenue must be attached to the tax return on which the credit is claimed. **KRS 141.0405**

Qualified Research Facility Tax Credit—A taxpayer is entitled to a credit against the taxes imposed by KRS 141.020, KRS 141.040 and KRS 141.0401 of 5 percent of the qualified costs of construction, remodeling, expanding and equipping facilities in Kentucky for "qualified research." Any unused credit may be carried forward 10 years. Schedule QR, Qualified Research Facility Tax Credit, must be attached to the tax return on which this credit is claimed. Federal Form 6765, Credit for Increasing Research Activities, must also be attached if applicable. See instructions for Schedule QR for more information regarding this credit. **KRS 141.395**

GED Incentive Tax Credit—A taxpayer is entitled to a credit against the taxes imposed by KRS 141.020, KRS 141.040 and KRS 141.0401. The credit reflected on this line must equal the sum of the credits reflected on the attached GED-Incentive Program Final Reports. This credit may be claimed only in the year during which the learning contract was completed and unused portions of the credit may not be carried forward or back. For information regarding the program, contact the Education Cabinet, Kentucky Adult Education, Council on Postsecondary Education. The GED-Incentive Program Final Report (DAEL-31) for each employee that completed a learning contract during the tax year must be attached to the tax return claiming the credit. **KRS 151B.127**

Voluntary Environmental Remediation Tax Credit (Brownfield)—The taxpayer must have an agreed order and be approved by the Environmental and Public Protection Cabinet under the provisions of KRS 224.01-518. Maximum allowed to be claimed per taxable year is 25 percent of the approved credit. This credit

may be claimed against the taxes imposed by KRS 141.020, KRS 141.040 and KRS 141.0401. For more information regarding credit for voluntary environmental remediation property, contact the Environmental and Public Protection Cabinet at (502) 564-3350. Schedule VERB must be attached to the tax return claiming this credit. **KRS 141.418**

Biodiesel Tax Credit—The 2007 Second Extraordinary Session amended 141.422 to include renewable diesel to be subject to the biodiesel tax credit. Producers and blenders of biodiesel and producers of renewable diesel are entitled to a tax credit against the taxes imposed by KRS 141.020, KRS 141.040 and KRS 141.0401. The taxpayer must file a claim for biodiesel credit with the Department of Revenue by January 15 each year for biodiesel produced or blended and the renewable diesel produced in the previous calendar year. The department shall issue a credit certification (Schedule BIO) to the taxpayer by April 15. The credit certification must be attached to the tax return claiming this credit. **KRS 141.423 and Regulation 103 KAR 15:140**

Environmental Stewardship Tax Credit—For tax years beginning on or after January 1, 2006, an approved company may be entitled to a credit against the taxes imposed by KRS 141.020, KRS 141.040 or KRS 141.0401 on the income and the LLET of the approved company generated by or arising out of a project as determined under KRS 154.48-020. An "environmental stewardship product" means any new manufactured product or substantially improved existing manufactured product that has a lesser or reduced adverse effect on human health and the environment or provides for improvement to human health and the environment when compared with existing products or competing products that serve the same purpose. A company must have eligible costs of at least \$5 million and within six months after the activation date, the approved company compensates a minimum of 90 percent of its full-time employees whose jobs were created or retained with base salary wages equal to either: (1) 75 percent of the average hourly wage for the commonwealth; or (2) 75 percent of the average hourly wage for the county in which the project is to be undertaken. The maximum amount of negotiated inducement that can be claimed by a company for any single tax year may be up to 25 percent of the authorized inducement. The agreement shall expire on the earlier of the date the approved company has received inducements equal to the approved costs of its project, or 10 years from the activation date. For more information, contact the Cabinet for Economic Development, Department of Financial Incentives at (502) 564-4554. **KRS 154.48**

Caution: An approved company under the Environmental Stewardship Act shall not be entitled to the recycling credit provided under the provisions of KRS 141.390 for equipment used in the production of an environmental stewardship project.

Clean Coal Incentive Tax Credit—Effective for tax years ending on or after December 31, 2006, a nonrefundable, nontransferable credit against taxes imposed by KRS 136.120, KRS 141.020, KRS 141.040 or KRS 141.0401 shall be allowed for a clean coal facility. As provided by KRS 141.428, a clean coal facility means an electric generation facility beginning commercial operation on or after January 1, 2005, at a cost greater than \$150 million that is located in the Commonwealth of Kentucky and is certified by the Environmental and Public Protection Cabinet as reducing emissions of pollutants released during generation of electricity through the use of clean coal equipment and technologies. The amount of the credit shall be \$2 per ton of eligible coal purchased that is used to generate electric power at a certified clean coal facility, except that no credit shall be allowed if the eligible coal has been used to generate a credit under KRS 141.0405 for the taxpayer, parent or subsidiary. **KRS 141.428**

TAXPAYER ASSISTANCE

Forms:

Operations and Support Services Branches
501 High Street
Frankfort, KY 40620
(502) 564-3658



Web site: www.revenue.ky.gov
E-mail: Financerevenueformsandenvelopes@ky.gov

Information:

Division of Corporation Tax
Department of Revenue
P.O. Box 1302
Frankfort, KY 40602-1302



Department of Revenue
501 High Street
Frankfort, KY 40620
(502) 564-8139

TANGIBLE PERSONAL PROPERTY TAXES—The listing period for tangible personal property is January 1 through May 15 of each year. Each taxpayer is responsible for reporting his tangible personalty subject to ad valorem taxation. The Tangible Personal Property Tax Return, Revenue Form 62A500, and instructions can be obtained from your local county property valuation administrator’s office or the Office of Property Valuation. You may also go to www.revenue.ky.gov to download these forms. A separate form must be filed for each location in Kentucky where you have tangible personal property.

KENTUCKY TAXPAYER SERVICE CENTERS

Information and forms are available from Kentucky Taxpayer Service Centers in the following cities.

Ashland, 134 Sixteenth Street, 41101-7670
(606) 920-2037

Bowling Green, 201 West Professional Park Court, 42104-3278
(270) 746-7470

Central Kentucky, 501 High Street, Frankfort, 40620
(502) 564-4581 (*Taxpayer Assistance*)

Corbin, 15100 North US 25E, Suite 2, 40701-6188
(606) 528-3322

Hopkinsville, 181 Hammond Drive, 42240-7926
(270) 889-6521

Louisville, 620 South Third Street, Suite 102, 40202-2446
(502) 595-4512

Northern Kentucky, Turfway Ridge Office Park
7310 Turfway Road, Suite 190, Florence, 41042-4871
(859) 371-9049

Owensboro, 311 West Second Street, 42301-0734
(270) 687-7301

Paducah, Clark Business Complex, Suite G
2928 Park Avenue, 42001-4024
(270) 575-7148

Pikeville, Uniplex Center, Suite 203,
126 Trivette Drive, 41501-1275
(606) 433-7675

**Kentucky Department of Revenue
Mission Statement**

As part of the Finance and Administration Cabinet, the mission of the Kentucky Department of Revenue is to administer tax laws, collect revenue, and provide services in a fair, courteous, and efficient manner for the benefit of the Commonwealth and its citizens.

* * * * *

The Kentucky Department of Revenue does not discriminate on the basis of race, color, national origin, sex, religion, age or disability in employment or the provision of services.

Printing costs paid from state funds.

YOUR RIGHTS AS A KENTUCKY TAXPAYER

As part of the Finance and Administration Cabinet the mission of the Kentucky Department of Revenue (DOR) is to administer tax laws, collect revenue, and provide services in a fair, courteous, and efficient manner for the benefit of the Commonwealth and its citizens.

As a Kentucky taxpayer, you have the right to expect the DOR to honor its mission and uphold your rights every time you contact or are contacted by the DOR.

RIGHTS OF TAXPAYER

Privacy—You have the right to privacy of information provided to the DOR.

Assistance—You have the right to advice and assistance from the DOR in complying with state tax laws.

Explanation—You have the right to a clear and concise explanation of:

- basis of assessment of additional taxes, interest and penalties, or the denial or reduction of any refund or credit claim;
- procedure for protest and appeal of a determination of the DOR; and
- tax laws and changes in tax laws so that you can comply with the law.

Protest and Appeal—You have the right to protest and appeal a determination of the DOR if you disagree with an assessment of tax or penalty, reduction or a denial of a refund, a revocation of a license or permit, or other determination made by the DOR.

Conference—You have the right to request a conference to discuss the issue.

Representation—You have the right to representation by your authorized agent (attorney, accountant or other person) in any hearing or conference with the DOR. You have the right to be informed of this right prior to the conference or hearing. If you intend for your representative to attend the conference or hearing in your place, you may be required to give your representative a power of attorney before the DOR can discuss tax matters with your authorized agent.

Recordings—You have the right to make an audio recording of any meeting, conference, or hearing with the DOR. The DOR has the right to make an audio recording, if you are notified in writing in advance or if you make a recording. You have the right to receive a copy of the recording.

Consideration—You have the right to consideration of:

- waiver of penalties or collection fees if "reasonable cause" for reduction or waiver is given ("reasonable cause" is defined in KRS 131.010(9) as: "an event, happening, or circumstance entirely beyond the knowledge or control of a taxpayer who has exercised due care and prudence in the filing of a return or report or the payment of monies due the department pursuant to law or administrative regulation");
- installment payments of delinquent taxes, interest and penalties;

- waiver of interest and penalties, but not taxes, resulting from incorrect written advice from the DOR if all facts were given and the law did not change or the courts did not issue a ruling to the contrary;
- extension of time for filing reports or returns; and
- payment of charges incurred resulting from an erroneous filing of a lien or levy by the DOR.

Guarantee—You have the right to a guarantee that DOR employees are not paid, evaluated or promoted based on taxes assessed or collected, or a tax assessment or collection quota or goal imposed or suggested.

Damages—You have the right to file a claim for actual and direct monetary damages with the Kentucky Board of Claims if a DOR employee willfully, recklessly and intentionally disregards your rights as a Kentucky taxpayer.

Interest—You have the right to receive interest on an overpayment of tax, except delinquent property tax, payable at the same rate you would pay if you underpaid your tax.

DEPARTMENT OF REVENUE RESPONSIBILITIES

The DOR has the responsibility to:

- perform audits, conduct conferences and hearings with you at reasonable times and places;
- authorize, require or conduct an investigation or surveillance of you only if it relates to a tax matter;
- make a written request for payment of delinquent taxes which are due and payable at least 30 days prior to seizure and sale of your assets;
- conduct educational and informational programs to help you understand and comply with the laws;
- publish clear and simple statements to explain tax procedures, remedies, your rights and obligations, and the rights and obligations of the DOR;
- notify you in writing when an erroneous lien or levy is released and, if requested, notify major credit reporting companies in counties where lien was filed;
- advise you of procedures, remedies and your rights and obligations with an original notice of audit or when an original notice of tax due is issued, a refund or credit is denied or reduced, or whenever a license or permit is denied, revoked or canceled;
- notify you in writing prior to termination or modification of a payment agreement;
- furnish copies of the agent's audit workpapers and a written narrative explaining the reason(s) for the assessment;
- resolve tax controversies on a fair and equitable basis at the administrative level whenever possible; and
- notify you in writing at your last known address at least 60 days prior to publishing your name on a list of delinquent taxpayers for which a tax or judgment lien has been filed.

PROTEST AND APPEAL PROCEDURE

Protest—If you receive a notice of assessment, a Notice of Tax Due for tax or penalty or if the DOR notifies you that a tax refund or credit has been reduced or denied, a license or permit revoked or denied, or other determination made by the DOR, you have the right to protest. To do so:

- submit a written protest within 45 days from the original notice date;
- identify the type of tax involved and give the account number, Social Security number or other identification number and attach a copy of the DOR notice of determination to support that protest is timely;
- explain why you disagree;
- attach any proof or documentation available to support your protest or request additional time to support your protest;
- sign your statement, include your daytime telephone number and mailing address; and
- mail to the Kentucky Department of Revenue, Frankfort, KY 40620.

Independent Informal Review—You have the right to request an independent informal review.

Conference—You have the right to request a conference to discuss the issue.

Final Ruling—If you do not want to have a conference or if the conference did not resolve your protest, you have the right to request a final ruling of the DOR so that you can appeal your case further.

Appeal—If you do not agree with the DOR’s final ruling, you can file a written appeal with the Kentucky Board of Tax Appeals. If you do not agree with the decision of the Kentucky Board of Tax Appeals, you have the right to appeal their ruling to the Kentucky courts (first to the circuit court in your home county or in Franklin County, then to the Kentucky Court of Appeals, and finally to the Kentucky Supreme Court).

TAXPAYER OMBUDSMAN

The DOR has a Taxpayer Ombudsman whose job is to serve as an advocate for taxpayers’ rights. One of the main functions of the Ombudsman is to ensure that your rights as a Kentucky taxpayer are protected.

Also, an important function of the Taxpayer Ombudsman is to confer with DOR employees when you have a problem or conflict that you have been unable to resolve. However, it is not the role of the Ombudsman to intercede in an audit, handle a protest, waive taxes, penalty or interest, or answer technical tax questions. To file a protest, see PROTEST AND APPEAL PROCEDURE. Please do not mail your protest to the Ombudsman.

The Taxpayer Ombudsman is your advocate and is there to make sure your rights are protected. If you think you are not being treated fairly or if you have a problem or complaint, please contact the Ombudsman for assistance.

The Taxpayer Ombudsman may be contacted by telephone at (502) 564-7822 (between 8:00 a.m. and 5:00 p.m. weekdays). The mailing address is: Department of Revenue, Taxpayer Ombudsman, P.O. Box 930, Frankfort, Kentucky 40602-0930.

WHERE TO GET ASSISTANCE

The DOR has offices in Frankfort and taxpayer service centers in nine cities and towns throughout Kentucky. DOR employees in the service centers answer tax questions and provide assistance. You may obtain assistance by contacting any of the following:

Ashland Taxpayer Service Center

134 Sixteenth Street, 41101-7670
(606) 920-2037

Bowling Green Taxpayer Service Center

201 West Professional Park Court, 42104-3278
(270) 746-7470

Central Kentucky Taxpayer Service Center

501 High Street
Frankfort 40620
(502) 564-4581 (*Taxpayer Assistance*)

Corbin Taxpayer Service Center

15100 North US 25E, Suite 2, 40701-6188
(606) 528-3322

Hopkinsville Taxpayer Service Center

181 Hammond Drive, 42240-7926
(270) 889-6521

Louisville Taxpayer Service Center

620 South Third Street, Suite 102, 40202-2446
(502) 595-4512

Northern Kentucky Taxpayer Service Center

Turfway Ridge Office Park
7310 Turfway Road, Suite 190
Florence 41042-4871
(859) 371-9049

Owensboro Taxpayer Service Center

311 West Second Street, 42301-0734
(270) 687-7301

Paducah Taxpayer Service Center

Clark Business Complex, Suite G
2928 Park Avenue, 42001-4024
(270) 575-7148

Pikeville Taxpayer Service Center

Uniplex Center, 126 Trivette Drive, Suite 203, 41501-1275
(606) 433-7675

The DOR has an online taxpayer service center where you can download forms, publications, and obtain general information about the department. The address is www.revenue.ky.gov.

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This information merely summarizes your rights as a Kentucky taxpayer and the responsibilities of the Department of Revenue. The Kentucky Taxpayers’ Bill of Rights may be found in the Kentucky Revised Statutes (KRS) at Chapter 131.041—131.081. Additional rights and responsibilities are provided for in KRS 131.020, 131.110, 131.170, 131.183, 131.500, 133.120, 133.130, 134.580 and 134.590.