

Kentucky Tax Alert

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CLARIFICATION ON COMPUTING COSTS OF GOODS SOLD

In the September 2013 *Kentucky Tax Alert*, the Department released guidance regarding cost of goods sold (COGS) in computing the gross profits component of the Limited Liability Entity Tax (LLET). Subsequently, the Department developed a new schedule (Schedule COGS) to assist taxpayers in calculating Kentucky COGS for LLET purposes.

In completing the Schedule COGS, separate accounting must be utilized in order to calculate and report the amount of Kentucky COGS. However, several taxpayers and tax practitioners have recently contacted the Department to explain why separate accounting is not feasible for them or their clients. For those taxpayers, the Department provides the following additional information for assistance in completing Schedule COGS.

If separate accounting is not possible for the taxpayer, a supporting statement explaining why separate accounting cannot be used to complete Schedule COGS must be attached. In such instances, as an alternative to separate accounting, the taxpayer must then take the following four steps in filling out Schedule COGS:

1. Complete the column titled Federal Form 1125-A Cost of Goods Sold, in its entirety.
2. Complete Column B, Total Costs of Goods Sold, in its entirety. Please note that the beginning and ending inventory may be different from the amounts reported on Federal Form 1125-A because of costs excluded from the COGS calculation. For a discussion of what costs must be excluded, please see the September 2013 *Kentucky Tax Alert* and the instructions to Schedule COGS.
3. Multiply the Total Cost of Goods Sold in Column B by the taxpayer's Kentucky sales factor.
4. Enter the result of step 3 on Column A, Cost of Goods Sold, Line 8.

It is critical that such taxpayers comply with these steps. For example, without the supporting statement, the Department will assume that separate accounting was possible and compliance the return on that basis.

Kentucky Tax Alert comments and suggestions should be addressed to the Office of Income Taxation/Training Branch, Finance Cabinet, Department of Revenue, Frankfort, Kentucky, (502) 564-0937.

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