

Kentucky Tax Alert

A REVENUE PUBLICATION FOR THE TAX PROFESSIONAL

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USE TAX DUE ON ONLINE AND MAIL ORDER PURCHASES

The 6 percent use tax is still due even when the sales and use tax is not collected by the retailer when a customer makes a purchase online or by mail order. With the imposition of sales tax there is also the corresponding use tax as a backstop to ensure that the proper tax is paid on retail purchases for storage, use or other consumption in Kentucky (KRS 139.310, 139.330). When the out-of-state retailer does not collect the tax at the point of sale, the tax liability remains with the purchaser if the items are taxable in Kentucky.



Examples of taxable items purchased from out-of-state vendors may include: computers; prewritten computer software; downloaded ringtones; books (paper and electronic); digital property; jewelry; furniture; ATVs; and lawn equipment.

Use tax may be reported by individuals and entities on Form 51A113(O), available at <http://revenue.ky.gov>. In addition, individuals may also report use tax on the designated line of their Kentucky individual income tax return. Retail businesses registered for sales and use tax should report their purchases subject to Kentucky use tax on Form 51A102 or Form 51A103, line 23(a). Other nonretail business entities with recurring use tax liability should register for a consumer's use tax account number. Those businesses should report purchases on Form 51A113 and remit the tax accordingly.

2009 KENTUCKY INDIVIDUAL INCOME TAX UPDATES AND TIPS

What's New For Kentucky

Kentucky Energy Efficiency Products Tax Credit (KRS 141.436)—A nonrefundable tax credit against the individual income tax imposed under KRS 141.020 was established by House Bill 2 in the 2008 General Assembly. The credit is applicable for the installation of energy efficiency products in a Kentucky residence. This credit went into effect after the Dec. 31, 2008 tax period and is available until Jan. 1, 2016. Therefore, the credit may be claimed on 2009 Kentucky Individual Income Tax returns. Form 5695-K Kentucky

Energy Efficiency Products Tax Credit has been created to claim this credit.

Requirements and features of this credit include the following:

- Credit is reported and computed on Form 5695-K
- Credit applies in the tax year in which the installation is completed
- Credit is equal to 30 percent of installed costs subject to limitations

Examples of applications for this credit include: upgraded insulation; energy efficient windows; qualified energy property; active and passive solar heating systems; qualified solar water-heating systems; qualified wind turbine or wind machines; and qualified solar photovoltaic systems.

Form 8863-K Kentucky Education Tuition Tax Credit—Provisions included in the American Recovery and Reinvestment Act (ARRA) of 2009 that impacted the federal Form 8863 do not apply to state income tax returns. Taxpayers must use the Kentucky form and instructions to correctly compute the allowable Kentucky Education Tuition Tax Credit.

New Home Tax Credit—The New Home Tax Credit is a nonrefundable individual income tax credit that became effective July 26, 2009 and applies to a *qualified buyer* who purchases a *qualified principal residence* during the one-year period of July 26, 2009 through July 25, 2010.

Qualified buyer(s) approved for the credit will receive a credit allocation letter with a four-digit approval code from the Department of Revenue (DOR). This letter must be attached to the income tax return filed for the taxable year during which the qualified principal residence was purchased.

Approved buyers filing electronically must include information from the credit allocation letter and the New Home Tax Credit (for electronic filers only) with any electronic return submitted. Any software used to submit the return must meet these requirements.

The New Home Tax Credit application and additional information is available on the DOR's Web site: www.revenue.ky.gov

Family Size Tax Credit—This credit provides benefits to individuals and families at incomes up to 133 percent of the threshold amount based on the federal poverty level. The 2009

threshold amount is \$10,830 for a family size of one, \$14,570 for a family of two, \$18,310 for a family of three and \$22,050 for a family of four or more.



Standard Deduction—For 2009, the standard deduction is \$2,190.

Unemployment Compensation—Provisions included in the American Recovery and Reinvestment Act of 2009 that exempted the first \$2,400 of unemployment benefits received by an individual do not apply to state income tax returns. All unemployment compensation will still be considered income for Kentucky purposes and subject to Kentucky tax. Therefore, an adjustment must be made on Schedule M, Part 1, Line 6 to report this income.

Mortgage Debt Forgiveness—The Mortgage Forgiveness Debt Relief Act of 2007 has been enacted to provide relief to those families who have been adversely affected by problems in the subprime mortgage market. This act will provide relief to those families by permanently excluding debt forgiven under these circumstances for tax liability for federal purposes. However, because Kentucky has not adopted this legislation, any mortgage debt forgiveness will still be considered income for Kentucky purposes and subject to Kentucky tax. Therefore, an adjustment must be made on Schedule M, Part 1, Line 7 to report this income.

FILING TIPS:

File Electronically—Filing electronically is the fastest way to receive your refund. Electronically filed returns generally process within 7–21 days, and is the only way to have your refund check direct deposited into your bank account.

Direct Deposit—If you are filing electronically and request that your refund be direct deposited, be sure to verify that all account and routing numbers are current.

Payments—When submitting payments for electronically filed returns, **do not** send a copy of your return. Use Form 740-V to remit your payment. Include your Social Security number and tax year on the check.

Wage and Tax Statements—Ensure that all necessary statements are attached to support the *Kentucky* withholding claimed on the return.

Social Security Numbers—The numbers are *not* on the preprinted labels. Please enter them legibly and in the appropriate boxes on the return.

Addresses—If your address is correct, use the preprinted labels furnished with your booklet. Otherwise, make sure the address

entered on the return is the correct address. If you move after you have submitted your return, please contact the DOR to update your address.

Form 2210-K—When applicable, use Form 2210-K to calculate any underpayment tax penalties or to claim an exception to the penalty. Check the appropriate box on Form 740 when Form 2210-K is attached.

2D Barcode Returns—Even though some W-2 information is included, wage statements need to be attached for verification of withholding claimed.

Credit for Tax Paid to Another State—Paper returns *must* include copies of returns from other state(s) if claiming a credit. Electronically filed returns must have the Credit for Tax Paid to Another State worksheet completed and submitted with the electronic submission for proper processing.

Amended Returns—Use the proper form for the year you are amending and include a complete explanation of the changes.

Attach Supporting Schedules—Make sure all appropriate schedules and worksheets are attached to the return (i.e. K-1s, 8863-K, etc.).

K-4E SPECIAL WITHHOLDING EXEMPTION CERTIFICATE

Employers: Kentucky DOR strongly encourages all employers to utilize Form K-4E, Special Withholding Exemption Certificate, when applicable.

This certificate should be completed by employees that anticipate no Kentucky income tax liability. If the employee is eligible to claim this exemption, the employer will **not** withhold Kentucky income tax from wages. This certificate may be used instead of Form K-4 by those employees qualified to claim the exemption.



To download the form along with instructions go to the Kentucky DOR's Web site at www.revenue.ky.gov and click on Tax Forms, Current Year Forms, Withholding Tax.

MILITARY SPOUSES RESIDENCY RELIEF ACT (MSRRA)

The Military Spouses Residency Relief Act (MSRRA) (Public Law 111-97) was signed into law on Nov. 11, 2009. This new law is effective for taxable year 2009. The MSRRA allows the

same residency benefits permitted to military personnel under the Servicemembers Civil Relief Act (SCRA) to also apply for a military spouse's nonmilitary service income under certain circumstances.

The MSRRA prohibits a servicemember's spouse from either losing or acquiring a residence or domicile for purposes of taxation because he or she is absent or present in any U.S. tax jurisdiction solely to be with the servicemember in compliance with the servicemember's military orders, if the residence or domicile is the same for the servicemember and the spouse. The MSRRA also prohibits a spouse's income from being considered income earned in a tax jurisdiction if the spouse is not a resident or domiciliary of such jurisdiction when the spouse is in that jurisdiction solely to be with a servicemember serving under military orders.



For 2009, those military spouses who fall under this law should file Form 740-NP Kentucky Individual Income Tax Nonresident or Part-Year Resident Return to request a refund of the Kentucky income tax withheld from his or her 2009 pay. The income would not be reported as taxable on the Kentucky income tax return. To assist the department in identifying those returns, please write across the top of the return MILITARY SPOUSE. For 2010, those military spouses should file a new Form K-4 with his or her employer to claim the exemption from withholding of Kentucky income tax. The updated K-4 Form is now available on the DOR's Web site. Please address any further questions to the Taxpayer Assistance Section at (502) 564-4581.



ATTENTION INSURERS, SURPLUS LINES BROKERS, AND AGENTS

Adjustment of premium surcharge rate effective April 1, 2010

Pursuant to KRS 136.392(1)(b), the premium surcharge rate will increase from \$1.50 to \$1.80 per \$100 of premiums, assessments or other charges for insurance coverage provided to policyholders on risks located in Kentucky. The adjustment to the premium surcharge rate will be effective and applied to all payments for insurance coverage due on or after April 1, 2010.

Forms will be updated to reflect this change and will be available on the Current Year Insurance Premiums Tax/

Surcharge Forms page prior to the effective date of the change. This page can be found at: <http://revenue.ky.gov/forms/cityfrms.htm>

EXCEPTIONS:

It should be noted that the exceptions listed in KRS 136.392(5) remain in full force and effect. Also be advised of the following exceptions:

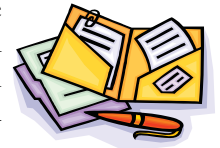
- Municipal premium taxes imposed pursuant to KRS 91A are not to be included in calculation of the premium surcharge;
- Life and health insurers are not subject to the premium surcharge imposed by KRS 136.392; and
- Pursuant to KRS 342.122(1)(e), the premium surcharge shall not be imposed on Workers' Compensation.

IRS REMINDS TAXPAYERS THAT KEEPING GOOD RECORDS REDUCES STRESS AT TAX TIME

The tax filing season is just around the corner, so if you haven't already done so, it's time to organize your records.

Whether you are a business owner or an individual taxpayer, you can avoid headaches at tax time with good records because they will help you remember transactions made during the past year.

Keeping well-organized records help you answer questions if your return is selected for examination or can be referenced to prepare a response if you are billed for additional tax. In most cases, the IRS does not require taxpayers to keep records in any special manner, although you should keep any and all documents that may have an impact on your federal tax return.



Small Business Owners

If you are a small business owner, you must keep all employment tax records for at least four years after the tax becomes due or is paid, whichever is later. Examples of important documents business owners should keep include:

- Gross receipts: Cash register tapes, bank deposit slips, receipt books, invoices, credit card charge slips and Forms 1099-MISC;
- Proof of purchases: Canceled checks, cash register tape receipts, credit card sales slips and invoices;
- Expense documents: Canceled checks, cash register tapes, account statements, credit card sales slips, invoices and petty cash slips for small cash payments; and
- Documents to verify assets: Purchase and sales invoices, real estate closing statements and canceled checks.

Individuals

The IRS suggests that individual taxpayers keep the following records supporting items on their tax returns for at least three years*:

- Bills
- Credit card and other receipts
- Invoices
- Mileage logs
- Canceled, imaged or substitute checks or any other proof of payment
- Any other records to support deductions or credits claimed on a return

For more information about recordkeeping, check out IRS Publications:

- Pub 552 at <http://www.irs.gov/pub/irs-pdf/p552.pdf>, Recordkeeping for Individuals;
- Pub 583 at <http://www.irs.gov/pub/irs-pdf/p583.pdf>, Starting a Business and Keeping Records
- Pub 463 at <http://www.irs.gov/pub/irs-pdf/p463.pdf>, Travel, Entertainment, Gift and Car Expenses

These publications are available on the IRS Web site, IRS.gov or by calling 800-TAX-FORM (800-829-3676).

To get the latest IRS news and products and services subscribe to our FREE e-News on IRS.gov at <http://www.irs.gov/businesses/small/article/0,,id=154825,00.html>, click "Subscribe Now" at the bottom of the page and enter your e-mail address.

**For state tax purposes, individual taxpayers should keep supporting records for at least four years.*

SALES AND USE TAX FORM UPDATES

Updated Kentucky sales and use tax returns (Form 51A102, 51A102E, 51A103, and 51A103E) became effective with the January 2010 period. The annual interest rate was adjusted to 3 percent with the statutory mandate effective Jan. 1, 2010. Late payments will accrue interest at the rate of 5 percent as reflected on the returns. In addition, note that line 13 of the worksheet is blank. The deduction previously referred to as Freight has not been an applicable deduction since July 2004. Also, deduction lines 15, 16, 17 and line 23(a) are modified to reflect more accurate descriptions based on recent legislative changes. Please ensure that the paper sales and use tax return filed constitutes the correct form either mailed by the DOR or provided by an approved forms provider. Filing electronically via KY E-Tax is also a voluntary alternative for all retail account holders.

The Energy Exemption Annual Return (sales and use tax Form 51A129) is only available for download at the DOR's Web site at <http://revenue.ky.gov>. The form is only applicable to authorized energy direct pay entities and was previously mailed by the DOR according to each account holder's filing deadline. Filers of this form should go to the Web site and print the form for use. All sales and use tax form questions may be directed to the Division of Sales and Use Tax at (502) 564-5170 or via e-mail at DORWebResponseSalesTax@ky.gov.

Kentucky Tax Alert comments and suggestions should be addressed to the Office of Public Information, Finance Secretary's Office, Frankfort, Kentucky, (502) 564-9165.

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The Department of Revenue can be found at...

www.revenue.ky.gov



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NOTE: If a return due date falls on a scheduled holiday or weekend, returns will be due the next working day.

January	15	Estimated Corporation Income Tax/Limited Liability Entity Tax/One Half Est. (FY ending 7/31)	
	15	Estimated Corporation Income Tax/Limited Liability Entity Tax/One Fourth Est. (FY ending 1/31)	
	15	Estimated Corporation Income Tax/Limited Liability Entity Tax/One Fourth Est. (FY ending 4/30)	
	15	Estimated Tax/Individuals/One Fourth Est.	
	20	Coal Severance Tax Returns (December Payment)	
	20	Oil Production Tax Returns (December Payment)	
	20	Monthly Sales Tax Returns (December Payment)	
	20	Quarterly Sales Tax Returns	
	20	Annual Sales Tax Returns	
	20	Health Care Provider Tax Returns (December Payment)	
	25	Monthly Motor Fuels Tax Returns (December Payment)	
	25	Monthly Sales Tax Returns (Accelerated Payment)	
	February	1	Income Tax Withholding Returns/Electronic Funds Transfer (EFT) Filers/Annual Reconciliation
		1	Monthly Income Tax Withholding Returns (December Payment and K-2s)
		1	Quarterly Income Tax Withholding Returns (Quarterly Payment and K-2s)
		1	Annual Income Tax Withholding Returns (Annual Payment and K-2s)
		1	Minerals and Gas Severance Tax Returns (December Payment)
		1	Annual Report of Distilled Spirits in Bonded Warehouses (as of 1/1/07)
		10	Twice-Monthly Income Tax Withholding Returns (January 1 - January 31 Payment/EFT Payment)
		15	Estimated Corporation Income Tax/Limited Liability Entity Tax/One Half Est. (FY ending 8/31)
		15	Estimated Corporation Income Tax/Limited Liability Entity Tax/One Fourth Est. (FY ending 2/29)
		15	Estimated Corporation Income Tax/Limited Liability Entity Tax/One Fourth Est. (FY ending 5/31)
		15	Monthly Income Tax Withholding Returns (January Payment)
		22	Coal Severance Tax Returns (January Payment)
		22	Oil Production Tax Returns (January Payment)
22		Monthly Sales Tax Returns (January Payment)	
22		Health Care Provider Tax Returns (January Payment)	
25		Twice-Monthly Income Tax Withholding Returns (February 1 - February 15 Payment/EFT Payment)	
25		Monthly Motor Fuels Tax Returns (January Payment)	
25		Monthly Sales Tax Returns (Accelerated Payment)	
March		1	Minerals and Gas Severance Tax Returns (January Payment)
		1	Watercraft Property Tax Return (as of 1/1/07)
	10	Twice-Monthly Income Tax Withholding Returns (February 16 - February 28 Payment/EFT Payment)	
	15	Estimated Corporation Income Tax/Limited Liability Entity Tax/One Half Est. (FY ending 9/30)	
	15	Estimated Corporation Income Tax/Limited Liability Entity Tax/One Fourth Est. (FY ending 3/31)	
	15	Estimated Corporation Income Tax/Limited Liability Entity Tax/One Fourth Est. (FY ending 6/30)	
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	15	Bank Franchise Tax Returns	
	22	Coal Severance Tax Returns (February Payment)	
	22	Oil Production Tax Returns (February Payment)	
	22	Monthly Sales Tax Returns (February Payment)	
	22	Health Care Provider Tax Returns (February Payment)	
	25	Twice-Monthly Income Tax Withholding Returns (March 1 - March 15 Payment/EFT Payment)	
25	Monthly Motor Fuels Tax Returns (February Payment)		
25	Monthly Sales Tax Returns (Accelerated Payment)		
April	1	Minerals and Gas Severance Tax Returns (February Payment)	
	1	Electric Plant Board Property Tax Returns (as of 1/1/07)	
	12	Twice-Monthly Income Tax Withholding Returns (March 16 - March 31 Payment/EFT Payment)	
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	15	Quarterly Estimated Tax Returns/Individuals (One Fourth Payment)	
	15	Annual Individual Income Tax Returns	
	20	Monthly Sales Tax Returns (March Payment)	
	20	Quarterly Sales Tax Returns	
	20	Coal Severance Tax Returns (March Payment)	
	20	Oil Production Tax Returns (March Payment)	
	20	Health Care Provider Tax Returns (March Payment)	
	26	Twice-Monthly Income Tax Withholding Returns (April 1 - April 15 Payment/EFT Payment)	
	26	Monthly Motor Fuels Tax Returns (March Payment)	
	26	Monthly Sales Tax Returns (Accelerated Payment)	
30	Income Tax Withholding Returns/Electronic Funds Transfer (EFT) Filers/First Quarter Reconciliation		
30	Quarterly Income Tax Withholding Returns		

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May	3	Minerals and Gas Severance Tax Returns (March Payment)	
	3	Public Service Company Property Tax Returns (as of 12/31/06)	
	3	Railroad Car Line Property Tax Returns (as of 12/31/06)	
	10	Twice-Monthly Income Tax Withholding Returns (April 16 - April 30 Payment/EFT Payment)	
	17	Intangible Personal Property Tax Return (Taxpayer will be billed later)	
	17	Tangible Personal Property Tax Return (Taxpayer will be billed later)	
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	25	Monthly Motor Fuels Tax Returns (April Payment)	
	25	Monthly Sales Tax Returns (Accelerated Payment)	
	June	1	Minerals and Gas Severance Tax Returns (April Payment)
		10	Twice-Monthly Income Tax Withholding Returns (May 16 - May 31 Payment/EFT Payment)
		15	Estimated Corporation Income Tax/Limited Liability Entity Tax/One Half Est. (FY ending 12/31)
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		1	Cigarette License Annual Renewal Applications and License Fee
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25	Monthly Sales Tax Returns (Accelerated Payment)		

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September	1	Minerals and Gas Severance Tax Returns (July Payment)	
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	20	Oil Production Tax Returns (August Payment)	
	20	Monthly Sales Tax Returns (August Payment)	
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		11	Twice-Monthly Income Tax Withholding Returns (September 16 - September 30 Payment/EFT Payment)
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2009 FEDERAL/KENTUCKY INDIVIDUAL INCOME TAX DIFFERENCES

Kentucky income tax law is based on the federal income tax law in effect on December 31, 2006. The Department of Revenue generally follows the administrative regulations and rulings of the Internal Revenue Service in those areas where no specific Kentucky law exists.

The chart below provides a quick reference guide to the major federal/Kentucky differences. It is not intended to be all inclusive. Items not listed may be referred to the Department of Revenue to determine Kentucky tax treatment.

PROVISION	FEDERAL TAX TREATMENT	KENTUCKY TAX TREATMENT
1. Interest from Federal Obligations	Taxable	Exempt
2. Retirement Income from:		-----
Commonwealth of Kentucky Retirement Systems	Taxable	Partially exempt if retired after December 31, 1997; exempt if retired before January 1, 1998; Schedule P may be required
Kentucky Local Government Retirement Systems	Taxable	-----
Federal and Military Retirement Systems	Taxable	-----
3. Pensions and Annuities Starting After 7/1/86 and Before 1/1/90	3-year recovery rule eliminated	3-year recovery rule retained
4. Other Pension and Annuity Income	Taxable	100% excludable up to \$41,110; Schedule P may be required
5. Benefits from U.S. Railroad Retirement Board	May be taxable	Exempt; Schedule P may be required
6. Social Security Benefits	May be taxable	Exempt
7. Capital Gains on Sale of Kentucky Turnpike Bonds	Taxable	Exempt
8. Other States' Municipal Bond Interest Income	Exempt	Taxable
9. Kentucky Local Government Lease Interest Payments	Taxable	Exempt
10. Long-Term Care Insurance Premiums Paid With After-Tax Dollars	Limited deduction as self-employed health insurance	100% adjustment to gross income
11. Medical and Dental Insurance Premiums Paid With After-Tax Dollars	Limited deduction as self-employed health insurance	100% adjustment to gross income
12. Capital Gains on Property Taken by Eminent Domain	Taxable	Exempt
13. Election Workers—Income for Training or Working at Election Booths	Taxable	Exempt
14. Artistic Contributions	Noncash contribution allowed as itemized deduction	Appraised value allowed as itemized deduction or adjustment to income
15. State Income Taxes	Deductible	Nondeductible
16. Leasehold Interest—Charitable Contribution	May be deductible	Deductible; Schedule HH required
17. Kentucky Unemployment Tax Credit	No credit allowed	\$100 per certified employee; Schedule UTC required
18. Work Opportunity Credit (federal Form 5884)	Tax credit allowed; wage expense reduced by amount of credit	No credit allowed; entire wage expense is deductible
19. Welfare to Work Credit (federal Form 8861)	Tax credit allowed; wage expense reduced by amount of credit	No credit allowed; wage expense reduced by amount of federal credit
20. Child and Dependent Care Credit	Tax credit based on expenses	20% of federal credit
21. Family Size Tax Credit	No credit allowed	Decreasing tax credit allowed
22. Education Tuition Tax Credit	Tax credit based on expenses	25% of federal credit for Kentucky undergraduate studies
23. Taxpayer Who May be Claimed as Dependent on Another's Return (i.e., full-time student)	May not claim self	May claim self
24. Child's Income Reported by Parent	Permitted; taxed at parent's rate	Not permitted
25. National Tobacco Settlement TLAP Income Quota Buyout (including imputed interest)	Taxable	Exempt
26. Bonus Depreciation/Additional Section 179 Expense	Deductible	Nondeductible
27. Mortgage Debt Forgiveness	Exempt	Taxable
28. Unemployment Compensation	First \$2,400.00 excluded per taxpayer	Taxable