

**CHAPTER 18****(HB 258)**

AN ACT relating to corporation income tax and limited liability entity tax.

WHEREAS, the General Assembly recognizes that during the normal course of a taxable year, many corporate transactions occur; and

WHEREAS, the General Assembly also recognizes that some of these corporate transactions may create situations where the apportionment provisions of KRS 141.120(8) do not result in a fair representation of the extent of the corporation's business activity in the Commonwealth; and

WHEREAS, the General Assembly has enacted KRS 141.120(9) which allows a corporation to petition for or the department to require an alternative apportionment formula in respect to all or any part of the corporation's business activity; and

WHEREAS, the General Assembly acknowledges that, for a corporation employing a treasury function strategy related to liquid assets, the apportionment provisions of KRS 141.120(8) will not result in a fair representation of the corporation's business activity in the Commonwealth;

*Be it enacted by the General Assembly of the Commonwealth of Kentucky:*

➔Section 1. KRS 141.0401 is amended to read as follows:

(1) As used in this section:

- (a) "Kentucky gross receipts" means an amount equal to the computation of the numerator of the sales factor under the provisions of KRS 141.120(8)(c), ***subsection (9) of Section 2 of this Act, any administrative regulations related to the computation of the sales factor, and Section 3 of this Act*** and includes the proportionate share of Kentucky gross receipts of all wholly or partially owned limited liability pass-through entities, including all layers of a multi-layered pass-through structure;
- (b) "Gross receipts from all sources" means an amount equal to the computation of the denominator of the sales factor under the provisions of KRS 141.120(8)(c), ***subsection (9) of Section 2 of this Act, any administrative regulations related to the computation of the sales factor, and Section 3 of this Act*** and includes the proportionate share of gross receipts from all sources of all wholly or partially owned limited liability pass-through entities, including all layers of a multi-layered pass-through structure;
- (c) "Combined group" means all members of an affiliated group as defined in KRS 141.200(9)(b) and all limited liability pass-through entities that would be included in an affiliated group if organized as a corporation;
- (d) "Cost of goods sold" means:
  - 1. Amounts that are:
    - a. Allowable as cost of goods sold pursuant to the Internal Revenue Code and any guidelines issued by the Internal Revenue Service relating to cost of goods sold, unless modified by this paragraph; and
    - b. Incurred in acquiring or producing the tangible product generating the Kentucky gross receipts.
  - 2. For manufacturing, producing, reselling, retailing, or wholesaling activities, cost of goods sold shall only include costs directly incurred in acquiring or producing the tangible product. In determining cost of goods sold:
    - a. Labor costs shall be limited to direct labor costs as defined in paragraph (f) of this subsection;
    - b. Bulk delivery costs as defined in paragraph (g) of this subsection may be included; and
    - c. Costs allowable under Section 263A of the Internal Revenue Code may be included only to the extent the costs are incurred in acquiring or producing the tangible product

generating the Kentucky gross receipts. Notwithstanding the foregoing, indirect labor costs allowable under Section 263A shall not be included;

3. For any activity other than manufacturing, producing, reselling, retailing, or wholesaling, no costs shall be included in cost of goods sold.

As used in this paragraph, "guidelines issued by the Internal Revenue Service" includes regulations, private letter rulings, or any other guidance issued by the Internal Revenue Service that may be relied upon by taxpayers under reliance standards established by the Internal Revenue Service;

- (e)
  1. "Kentucky gross profits" means Kentucky gross receipts reduced by returns and allowances attributable to Kentucky gross receipts, less the cost of goods sold attributable to Kentucky gross receipts. If the amount of returns and allowances attributable to Kentucky gross receipts and the cost of goods sold attributable to Kentucky gross receipts is zero, then "Kentucky gross profits" means Kentucky gross receipts; and
  2. "Gross profits from all sources" means gross receipts from all sources reduced by returns and allowances attributable to gross receipts from all sources, less the cost of goods sold attributable to gross receipts from all sources. If the amount of returns and allowances attributable to gross receipts from all sources and the cost of goods sold attributable to gross receipts from all sources is zero, then gross profits from all sources means gross receipts from all sources;
- (f) "Direct labor" means labor that is incorporated into the tangible product sold or is an integral part of the manufacturing process;
- (g) "Bulk delivery costs" means the cost of delivering the product to the consumer if:
  1. The tangible product is delivered in bulk and requires specialized equipment that generally precludes commercial shipping; and
  2. The tangible product is taxable under KRS 138.220;
- (h) "Manufacturing" and "producing" means:
  1. Manufacturing, producing, constructing, or assembling components to produce a significantly different or enhanced end tangible product;
  2. Mining or severing natural resources from the earth; or
  3. Growing or raising agricultural or horticultural products or animals;
- (i) "Real property" means land and anything growing on, attached to, or erected on it, excluding anything that may be severed without injury to the land;
- (j) "Reselling," "retailing," and "wholesaling" mean the sale of a tangible product;
- (k) "Tangible personal property" means property, other than real property, that has physical form and characteristics; and
- (l) "Tangible product" means real property and tangible personal property;
- (2)
  - (a) For taxable years beginning on or after January 1, 2007, an annual limited liability entity tax 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 except as provided in this subsection. A small business exclusion from this tax shall be provided based on the reduction contained in this subsection. The tax shall be the greater of the amount computed under paragraph (b) of this subsection or one hundred seventy-five dollars (\$175), regardless of the application of any tax credits provided under this chapter or any other provisions of the Kentucky Revised Statutes for which the business entity may qualify.
  - (b) The limited liability entity tax shall be the lesser of subparagraph 1. or 2. of this paragraph:
    1. a. If the corporation's or limited liability pass-through entity's gross receipts from all sources are three million dollars (\$3,000,000) or less, the limited liability entity tax shall be zero;

- b. If the corporation's or limited liability pass-through entity's gross receipts from all sources are greater than three million dollars (\$3,000,000) but less than six million dollars (\$6,000,000), the limited liability entity tax shall be nine and one-half cents (\$0.095) per one hundred dollars (\$100) of the corporation's or limited liability pass-through entity's Kentucky gross receipts reduced by an amount equal to two thousand eight hundred fifty dollars (\$2,850) multiplied by a fraction, the numerator of which is six million dollars (\$6,000,000) less the amount of the corporation's or limited liability pass-through entity's Kentucky gross receipts for the taxable year, and the denominator of which is three million dollars (\$3,000,000), but in no case shall the result be less than zero;
  - c. If the corporation's or limited liability pass-through entity's gross receipts from all sources are equal to or greater than six million dollars (\$6,000,000), the limited liability entity tax shall be nine and one-half cents (\$0.095) per one hundred dollars (\$100) of the corporation's or limited liability pass-through entity's Kentucky gross receipts.
- 2. a. If the corporation's or limited liability pass-through entity's gross profits from all sources are three million dollars (\$3,000,000) or less, the limited liability entity tax shall be zero;
  - b. If the corporation's or limited liability pass-through entity's gross profits from all sources are at least three million dollars (\$3,000,000) but less than six million dollars (\$6,000,000), the limited liability entity tax shall be seventy-five cents (\$0.75) per one hundred dollars (\$100) of the corporation's or limited liability pass-through entity's Kentucky gross profits, reduced by an amount equal to twenty-two thousand five hundred dollars (\$22,500) multiplied by a fraction, the numerator of which is six million dollars (\$6,000,000) less the amount of the corporation's or limited liability pass-through entity's Kentucky gross profits, and the denominator of which is three million dollars (\$3,000,000), but in no case shall the result be less than zero;
  - c. If the corporation's or limited liability pass-through entity's gross profits from all sources are equal to or greater than six million dollars (\$6,000,000), the limited liability entity tax shall be seventy-five cents (\$0.75) per one hundred dollars (\$100) of all of the corporation's or limited liability pass-through entity's Kentucky gross profits.

In determining eligibility for the reductions contained in this paragraph, a member of a combined group shall consider the combined gross receipts and the combined gross profits from all sources of the entire combined group, including eliminating entries for transactions among the group.

- (c) A credit shall be allowed against the tax imposed under paragraph (a) of this subsection for the current year to a corporation or limited liability pass-through entity that owns an interest in a limited liability pass-through entity. The credit shall be the proportionate share of tax calculated under this subsection by the lower-level pass-through entity, as determined after the amount of tax calculated by the pass-through entity has been reduced by the minimum tax of one hundred seventy-five dollars (\$175). The credit shall apply across multiple layers of a multi-layered pass-through entity structure. The credit at each layer shall include the credit from each lower layer, after reduction for the minimum tax of one hundred seventy-five dollars (\$175) at each layer.
  - (d) The department may promulgate administrative regulations to establish a method for calculating the cost of goods sold attributable to Kentucky.
- (3) A nonrefundable credit based on the tax calculated under subsection (2) of this section shall be allowed against the tax imposed by KRS 141.020 or 141.040. The credit amount shall be determined as follows:
    - (a) The credit allowed a corporation subject to the tax imposed by KRS 141.040 shall be equal to the amount of tax calculated under subsection (2) of this section for the current year after subtraction of any credits identified in KRS 141.0205, reduced by the minimum tax of one hundred seventy-five dollars (\$175), plus any credit determined in paragraph (b) of this subsection for tax paid by wholly or partially owned limited liability pass-through entities. The amount of credit allowed to a corporation based on the amount of tax paid under subsection (2) of this section for the current year shall be applied to the income tax due from the corporation's activities in this state. Any remaining credit from the corporation shall be disallowed.

- (b) The credit allowed members, shareholders, or partners of a limited liability pass-through entity shall be the members', shareholders', or partners' proportionate share of the tax calculated under subsection (2) of this section for the current year after subtraction of any credits identified in KRS 141.0205, as determined after the amount of tax paid has been reduced by the minimum tax of one hundred seventy-five dollars (\$175). The credit allowed to members, shareholders, or partners of a limited liability pass-through entity shall be applied to income tax assessed on income from the limited liability pass-through entity. Any remaining credit from the limited liability pass-through entity shall be disallowed.
- (4) Each taxpayer subject to the tax imposed in this section shall file a return, on forms prepared by the department, on or before the fifteenth day of the fourth month following the close of the taxpayer's taxable year. Any tax remaining due after making the payments required in KRS 141.042 shall be paid by the original due date of the return.
- (5) The department shall prescribe forms and promulgate administrative regulations as needed to administer the provisions of this section.
- (6) The tax imposed by subsection (2) of this section shall not apply to:
  - (a) Financial institutions, as defined in KRS 136.500, except banker's banks organized under KRS 287.135 or 286.3-135;
  - (b) Savings and loan associations organized under the laws of this state and under the laws of the United States and making loans to members only;
  - (c) Banks for cooperatives;
  - (d) Production credit associations;
  - (e) Insurance companies, including farmers' or other mutual hail, cyclone, windstorm, or fire insurance companies, insurers, and reciprocal underwriters;
  - (f) Corporations or other entities exempt under Section 501 of the Internal Revenue Code;
  - (g) Religious, educational, charitable, or like corporations not organized or conducted for pecuniary profit;
  - (h) 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:
    - 1. The property consists of the final printed product, or copy from which the printed product is produced; and
    - 2. The corporation has no individuals receiving compensation in this state as provided in KRS 141.120(8)(b);
  - (i) Public service corporations subject to tax under KRS 136.120;
  - (j) Open-end registered investment companies organized under the laws of this state and registered under the Investment Company Act of 1940;
  - (k) Any property or facility which has been certified as a fluidized bed energy production facility as defined in KRS 211.390;
  - (l) An alcohol production facility as defined in KRS 247.910;
  - (m) Real estate investment trusts as defined in Section 856 of the Internal Revenue Code;
  - (n) Regulated investment companies as defined in Section 851 of the Internal Revenue Code;
  - (o) Real estate mortgage investment conduits as defined in Section 860D of the Internal Revenue Code;
  - (p) Personal service corporations as defined in Section 269A(b)(1) of the Internal Revenue Code;
  - (q) Cooperatives 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; or

- (r) Publicly traded partnerships as defined by Section 7704(b) of the Internal Revenue Code that are treated as partnerships for federal tax purposes under Section 7704(c) of the Internal Revenue Code, or their publicly traded partnership affiliates. "Publicly traded partnership affiliates" shall include any limited liability company or limited partnership for which at least eighty percent (80%) of the limited liability company member interests or limited partner interests are owned directly or indirectly by the publicly traded partnership.
- (7) (a) As used in this subsection, "qualified exempt organization" means an entity listed in subsection (6)(a) to (r) of this section and shall not include any entity whose exempt status has been disallowed by the Internal Revenue Service.
- (b) Notwithstanding any other provisions of this section, any limited liability pass-through entity that is owned in whole or in part by a qualified exempt organization shall, in calculating its Kentucky gross receipts or Kentucky gross profits, exclude the proportionate share of its Kentucky gross receipts or Kentucky gross profits attributable to the ownership interest of the qualified exempt organization.
- (c) Any limited liability pass-through entity that reduces Kentucky gross receipts or Kentucky gross profits in accordance with paragraph (b) of this subsection shall disregard the ownership interest of the qualified exempt organization in determining the amount of credit available under subsection (3) of this section.
- (d) The Department of Revenue may promulgate an administrative regulation to further define "qualified exempt organization" to include an entity for which exemption is constitutionally or legally required, or to exclude any entity created primarily for tax avoidance purposes with no legitimate business purpose.
- (8) The credit permitted by subsection (3) of this section shall flow through multiple layers of limited liability pass-through entities and shall be claimed by the taxpayer who ultimately pays the tax on the income of the limited liability pass-through entity.

➔Section 2. KRS 141.120 is amended to read as follows:

- (1) As used in this section, unless the context requires otherwise:
  - (a) "Business income" means income arising from transactions and activity in the regular course of a trade or business of the corporation and includes income from tangible and intangible property if the acquisition, management, or disposition of the property constitutes integral parts of the corporation's regular trade or business operations;
  - (b) "Commercial domicile" means the principal place from which the trade or business of the corporation is managed;
  - (c) "Compensation" means wages, salaries, commissions, and any other form of remuneration paid or payable to employees for personal services;
  - (d) "Financial organization" means any bank, trust company, savings bank, industrial bank, land bank, safe deposit company, private banker, savings and loan association, credit union, cooperative bank, investment company, or any type of insurance company;
  - (e) "Nonbusiness income" means all income other than business income;
  - (f) "Public service company" means any business entity subject to taxation under KRS 136.120;
  - (g) "Sales" means all gross receipts of the corporation not allocated under subsections (3) through (7) of this section, *except as provided by Section 3 of this Act*; and
  - (h) "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, and any foreign country or political subdivision thereof.
- (2) Any corporation which is required by KRS 141.010(14)(b) to allocate and apportion its net income shall allocate and apportion its net income as provided in this section.
- (3) Rents and royalties from real, intangible or tangible personal property, capital gains and losses, interest, or patent or copyright royalties, to the extent that they constitute nonbusiness income, shall be allocated as provided in subsections (4) through (7) of this section.

- (4) (a) Net rents and royalties from real property located in this state are allocable to this state.
- (b) Net rents and royalties from tangible personal property are allocable to this state if and to the extent that the property is utilized in this state; or in their entirety if the corporation's commercial domicile is in this state and the corporation is not organized under the laws of or taxable in the state in which the property is utilized.
- (c) The extent of utilization of tangible personal property in a state is determined by multiplying the rents and royalties by a fraction, the numerator of which is the number of days of physical location of the property in the state during the rental or royalty period in the taxable year and the denominator of which is the number of days of physical location of the property everywhere during all rental or royalty periods in the taxable year. If the physical location of the property during the rental or royalty period is unknown or unascertainable by the corporation, the tangible personal property is utilized in the state in which the property was located at the time the rental or royalty payer obtained possession.
- (d) Net rents and royalties from intangible personal property located in this state are allocable to this state. For purposes of this section, royalties from property leased in Kentucky shall be considered as royalties from intangible personal property.
- (5) (a) Capital gains and losses from sales or other dispositions of real property located in this state are allocable to this state.
- (b) Capital gains and losses from sales or other dispositions of tangible personal property are allocable to this state if the property had a situs in this state at the time of the sale, or the corporation's commercial domicile is in this state and the corporation is not taxable in the state in which the property had a situs.
- (c) Capital gains and losses from sales or other dispositions of intangible personal property are allocable to this state if the corporation's commercial domicile is in this state.
- (6) Interest is allocable to this state if the corporation's commercial domicile is in this state.
- (7) (a) Patent and copyright royalties are allocable to this state if and to the extent that the patent or copyright is utilized by the payer in this state; or if and to the extent that the patent or copyright is utilized by the payer in a state in which the corporation is not taxable and the corporation's commercial domicile is in this state.
- (b) A patent is utilized in a state to the extent that it is employed in production, fabrication, manufacturing, or other processing in the state or to the extent that a patented product is produced in the state. If the basis of receipts from patent royalties does not permit allocation to states or if the accounting procedures do not reflect states of utilization, the patent is utilized in the state in which the corporation's commercial domicile is located.
- (c) A copyright is utilized in a state to the extent that printing or other publication originates in the state. If the basis of receipts from copyright royalties does not permit allocation to states or if the accounting procedures do not reflect states of utilization, the copyright is utilized in the state in which the corporation's commercial domicile is located.
- (8) Except as provided in subsection (9) of this section, all business income shall be apportioned to this state by multiplying the income by a fraction, the numerator of which is the property factor, representing twenty-five percent (25%) of the fraction, plus the payroll factor, representing twenty-five percent (25%) of the fraction, plus the sales factor, representing fifty percent (50%) of the fraction, and the denominator of which is four (4), reduced by the number of factors, if any, having no denominator, provided that if the sales factor has no denominator, then the denominator shall be reduced by two (2).
- (a) The property factor is a fraction, the numerator of which is the average value of the corporation's real and tangible personal property owned or rented and used in this state during the tax period and the denominator of which is the average value of all the corporation's real and tangible personal property owned or rented and used during the tax period; provided, however, that property which has been certified as a pollution control facility as defined in KRS 224.01-300 shall be excluded from the property factor.
1. Property owned is valued at its original cost. If the original cost of any property is not determinable or is nominal or zero (0) the property shall be valued by the department pursuant to

- administrative regulations promulgated by the department. Property rented is valued at eight (8) times the net annual rental rate. Net annual rental rate is the annual rental rate paid by the corporation less any annual rental rate received by the corporation from subrentals, provided that the rental and subrentals are reasonable. If the department determines that the annual rental or subrental rate is unreasonable, or if a nominal or zero (0) rate is charged, the department may determine and apply the rental rate as will reasonably reflect the value of the property rented by the corporation.
2. The average value of property shall be determined by averaging the values at the beginning and ending of the tax period but the department may require the averaging of monthly values during the tax period if reasonably required to reflect properly the average value of the property.
- (b) The payroll factor is a fraction, the numerator of which is the total amount paid or payable in this state during the tax period by the corporation for compensation, and the denominator of which is the total compensation paid or payable by the corporation everywhere during the tax period. Compensation is paid or payable in this state if:
1. The individual's service is performed entirely within the state;
  2. The individual's service is performed both within and without the state, but the service performed without the state is incidental to the individual's service within the state; or
  3. Some of the service is performed in the state and the base of operations or, if there is no base of operations, the place from which the service is directed or controlled is in the state, or the base of operations or the place from which the service is directed or controlled is not in any state in which some part of the service is performed, but the individual's residence is in this state.
- (c) 1. The sales factor is a fraction, the numerator of which is the total sales of the corporation in this state during the tax period, and the denominator of which is the total sales of the corporation everywhere during the tax period.
2. Sales of tangible personal property are in this state if:
    - a. The property is delivered or shipped to a purchaser, other than the United States government, or to the designee of the purchaser within this state regardless of the f.o.b. point or other conditions of the sale; or
    - b. The property is shipped from an office, store, warehouse, factory, or other place of storage in this state and the purchaser is the United States government.
  3. Sales, other than sales of tangible personal property, are in this state if the income-producing activity is performed in this state; or the income-producing activity is performed both in and outside this state and a greater proportion of the income-producing activity is performed in this state than in any other state, based on costs of performance.
- (9) (a) If the allocation and apportionment provisions of this section do not fairly represent the extent of the corporation's business activity in this state, the corporation may petition for or the department may require, in respect to all or any part of the corporation's business activity, if reasonable:
1. Separate accounting;
  2. The exclusion of any one (1) or more of the factors;
  3. The inclusion of one (1) or more additional factors which will fairly represent the corporation's business activity in this state; or
  4. The employment of any other method to effectuate an equitable allocation and apportionment of income.
- (b) A corporation may elect the allocation and apportionment methods for the corporation's business income provided for in subparagraphs 1. and 2. of this paragraph. The election, if made, shall be irrevocable for a period of five years.
1. All business income derived directly or indirectly from the sale of management, distribution, or administration services to or on behalf of regulated investment companies, as defined under the

Internal Revenue Code of 1986, as amended, including trustees, and sponsors or participants of employee benefit plans which have accounts in a regulated investment company, shall be apportioned to this state only to the extent that shareholders of the investment company are domiciled in this state as follows:

- a. Total business income shall be multiplied by a fraction, the numerator of which shall be Kentucky receipts from the services for the tax period and the denominator of which shall be the total receipts everywhere from the services for the tax period.
  - b. For purposes of subdivision a. of this subparagraph, Kentucky receipts shall be determined by multiplying total receipts for the tax period from each separate investment company for which the services are performed by a fraction. The numerator of the fraction shall be the average of the number of shares owned by the investment company's shareholders domiciled in this state at the beginning of and at the end of the investment company's taxable year, and the denominator of the fraction shall be the average of the number of the shares owned by the investment company shareholders everywhere at the beginning of and at the end of the investment company's taxable year.
  - c. Nonbusiness income shall be allocated to this state as provided in subsections (4) through (7) of this section.
2. All business income derived directly or indirectly from the sale of securities brokerage services by a business which operates within the boundaries of any area of the Commonwealth, which on June 30, 1992, was designated as a Kentucky Enterprise Zone, as defined in KRS 154.655(2), shall be apportioned to this state only to the extent that customers of the securities brokerage firm are domiciled in this state. The portion of business income apportioned to Kentucky shall be determined by multiplying the total business income from the sale of these services by a fraction determined in the following manner:
- a. The numerator of the fraction shall be the brokerage commissions and total margin interest paid in respect of brokerage accounts owned by customers domiciled in Kentucky for the brokerage firm's taxable year; and
  - b. The denominator of the fraction shall be the brokerage commissions and total margin interest paid in respect of brokerage accounts owned by all of the brokerage firm's customers for that year.
  - c. Nonbusiness income shall be allocated to this state as provided in subsections (4) through (7) of this section.
- (10) Public service companies and financial organizations required by KRS 141.010(14)(b) to allocate and apportion net income shall allocate and apportion such income as follows:
- (a) Nonbusiness income shall be allocated to this state as provided in subsections (4) through (7) of this section.
  - (b) Business income shall be apportioned to this state by multiplying the business income by a fraction, the numerator of which is the property factor, representing twenty-five percent (25%) of the fraction, plus the payroll factor, representing twenty-five percent (25%) of the fraction, plus the sales factor, representing fifty percent (50%) of the fraction, and the denominator of which is four (4), reduced by the number of factors, if any, having no denominator, provided that if the sales factor has no denominator, then the denominator shall be reduced by two (2). The payroll factor shall be determined as provided in subsection (8)(b) of this section. The property factor and sales factor shall be determined as provided by administrative regulations promulgated by the department.
  - (c) An affiliated group electing to file a consolidated return under KRS 141.200(4) or required to file a consolidated return under KRS 141.200(11) that includes a public service company, a provider of communications services or multichannel video programming services as defined in KRS 136.602, or financial organization shall determine the amount of payroll to be included in the apportionment factor as provided in subsection (8)(b) of this section. The amount of property and sales of the public service company, provider of communications services or multichannel video programming services as defined in KRS 136.602, or financial organization to be included in the apportionment factors of the affiliated



group shall be determined in accordance with administrative regulations promulgated by the department under paragraph (b) of this subsection.

(11) For taxable years beginning on or after January 1, 2007, a corporation that:

- (a) Owns an interest in a limited liability pass-through entity; or
- (b) Owns an interest in a general partnership organized or formed as a general partnership after January 1, 2006;

shall include the proportionate share of sales, property, and payroll of the limited liability pass-through entity or general partnership when apportioning income, and shall include the proportionate share of sales in calculating the tax due pursuant to KRS 141.0401. The phrases "an interest in a limited liability pass-through entity" and "an interest in a general partnership organized or formed as a general partnership after January 1, 2006," shall extend to each level of multiple-tiered pass-through entities.

➔SECTION 3. A NEW SECTION OF KRS CHAPTER 141 IS CREATED TO READ AS FOLLOWS:

(1) *As used in this section:*

- (a) *"Kentucky revenue passenger miles" means the total revenue passenger miles within the borders of Kentucky for all flight stages that either originate or terminate in this state;*
- (b) *"Liquid asset" means an asset, other than functional currency or funds held in bank accounts, held to provide a relatively immediate source of funds to satisfy the liquidity needs of the trade or business. "Liquid assets" include:*
  - 1. *Foreign currency and trading positions therein, other than functional currency used in the regular course of the corporation's trade or business;*
  - 2. *Marketable instruments, including stocks, bonds, debentures, options, warrants, and futures contracts; and*
  - 3. *Mutual funds which hold liquid assets;*
- (c) *"Marketable instrument" means an instrument that is traded in an established stock or securities market and is regularly quoted by brokers or dealers in making a market;*
- (d) *"Overall net gain" means the total net gain from all transactions incurred at each treasury function for the entire taxable period. "Overall net gain" does not mean the net gain from a specific transaction if multiple transactions occur during the taxable period;*
- (e) *"Passenger airline" means a person or corporation engaged primarily in the carriage by aircraft of passengers in interstate commerce;*
- (f) *"Revenue passenger miles" means miles calculated in accordance with 14 C.F.R. Part 241; and*
- (g) *"Treasury function" means the pooling and management of liquid assets for the purpose of satisfying the cash flow needs of the trade or business and includes the following situations:*
  - 1. *Providing liquidity for a corporation's business cycle; and*
  - 2. *Providing a reserve for business contingencies or business acquisitions.*

(2) *If a corporation holds liquid assets in connection with one (1) or more treasury functions of the corporation, and the liquid assets produce business income when sold, exchanged, or otherwise disposed of, the overall net gain from those transactions for each treasury function for the tax period shall be included in the sales factor. For purposes of this subsection:*

- (a) *Each treasury function shall be considered separately; and*
- (b) *A corporation principally engaged in the trade or business of purchasing and selling instruments or other items included in the definition of liquid assets is not performing a treasury function with respect to that income produced.*

(3) *For purposes of apportioning business income to this state, passenger airlines shall determine the property, payroll, and sales factors as follows:*

- (a) *Except as modified by this subsection, the property factor shall be determined as provided in subsection (8)(a) of Section 2 of this Act. Aircraft operated by a passenger airline shall be included in both the numerator and denominator of the property factor. Aircraft shall be included in the numerator of the property factor by determining the product of:*
1. *The total average value of the aircraft operated by the passenger airline; and*
  2. *A fraction, the numerator of which is the Kentucky revenue passenger miles of the passenger airline for the taxable year and the denominator of which is the total revenue passenger miles of the passenger airline for the taxable year;*
- (b) *Except as modified by this subsection, the payroll factor shall be determined as provided in subsection (8)(b) of Section 2 of this Act. Compensation paid during the tax period by a passenger airline to flight personnel shall be included in the numerator of the payroll factor by determining the product of:*
1. *The total amount paid during the taxable year to flight personnel; and*
  2. *A fraction, the numerator of which is the Kentucky revenue passenger miles of the passenger airline for the taxable year and the denominator of which is the total revenue passenger miles of the passenger airline for the taxable year; and*
- (c) *Except as modified by this subsection, the sales factor shall be determined as provided in subsection (8)(c) of Section 2 of this Act. Transportation revenues shall be included in the numerator of the sales factor by determining the product of:*
1. *The total transportation revenues of the passenger airline for the taxable year; and*
  2. *A fraction, the numerator of which is the Kentucky revenue passenger miles for the taxable year and the denominator of which is the total revenue passenger miles for the taxable year.*

➔Section 4. This Act shall apply to taxable periods beginning after December 31, 2007.

**Signed by Governor April 9, 2008.**