

AN ACT relating to scholarships for at-risk children.

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

➔SECTION 1. A NEW SECTION OF KRS CHAPTER 141 IS CREATED TO READ AS FOLLOWS:

(1) As used in this section:

(a) "Annual receipts" means the total amount of cash contributions received by a scholarship organization during the calendar year;

(b) "Educational scholarship" means a grant awarded to an eligible student to cover all or part of the following costs to attend a qualified school:

1. Tuition;

2. Educational fees, including fees for music, art, dance, drama, or other arts programs; and

3. Transportation to a qualified school outside the student's resident school district;

(c) "Eligible student" means a student who:

1. a. Is a member of a household whose income does not exceed the income standard used to qualify for a reduced lunch under the federal free or reduced-price lunch program established under 42 U.S.C. secs. 1751 et seq. for the tax year in which the credit provided in subsection (2) of this section is requested;

b. Was enrolled in an NCLB improvement school in the immediately preceding school year for any one hundred (100) instructional days from the first instructional day of the immediately preceding school year through the first day of the testing period designated annually by the Kentucky Department of Education within which all state-required assessments shall be administered; and

- c. Is enrolled full-time in a qualified school in the current school year; or
2. a. Received an educational scholarship under this section in the school year immediately preceding the current school year; and
- b. Is enrolled full-time in a qualified school in the current school year;
- (d) "Income" has the same meaning as in the United States Department of Agriculture, Food and Nutrition Service, Child Nutrition Programs, Income Eligibility Guidelines, Federal Register, Vol. 73, No. 69 and subsequent updates;
- (e) "NCLB improvement school" means a school that is identified by the Kentucky Department of Education as a school for improvement, a school subject to corrective action, or a school subject to restructuring in accordance with the No Child Left Behind Act of 2001, 20 U.S.C. secs. 6301 et seq., or its successor;
- (f) "Public school" has the same meaning as in KRS 158.182;
- (g) "Qualified nonpublic school" means an in-state nonpublic elementary or secondary school that:
1. Complies with all health and safety laws or codes that apply to nonpublic schools;
  2. Holds a valid local occupancy permit if required;
  3. Certifies that there will be no discrimination regarding admission on the basis of race, color, national origin, religion, or disability; and
  4. Provides academic accountability to parents of the students in the program by regularly reporting to the parent on the student's progress;
- (h) "Qualified school" means:

1. An in-state public elementary or secondary school that is not classified as an NCLB improvement school; or
  2. A qualified nonpublic school; and
- (i) "Scholarship organization" means a nonprofit entity that:
1. Is exempt from federal taxation under Section 501(c)(3) of the Internal Revenue Code; and
  2. Is organized solely for the purpose of receiving and distributing cash contributions to provide educational scholarships to eligible students at more than one (1) qualified school.
- (2) (a) 1. A scholarship for at-risk children tax credit program is hereby established.
2. For tax years beginning after December 31, 2015, a nonrefundable and nontransferable tax credit shall be allowed against the income tax imposed under KRS 141.020 or 141.040, and the limited liability entity tax imposed under KRS 141.0401, with the ordering of credits as provided in Section 3 of this Act, for cash contributions made during a tax year to one (1) or more scholarship organizations that are certified by the department as eligible to participate in the scholarship for at-risk children tax credit program established by this section.
  3. If the taxpayer is a pass-through entity, the taxpayer shall apply the credit against the limited liability entity tax imposed by KRS 141.0401, and shall also pass the credit through to its members, partners, or shareholders in the same proportion as the distributive share of income or loss is passed through.
  4. The credit shall be equal to the lesser of fifty percent (50%) of the total tax liability or two thousand dollars (\$2,000) per taxpayer per tax year regardless of the amount or number of contributions made to one (1)

or more certified scholarship organizations each tax year.

5. A tax credit not used in the tax year the contribution was made may be carried forward for three (3) years and shall not be carried back.

6. A taxpayer that qualifies for and uses the tax credit authorized by this section shall not be entitled to a deduction for charitable contributions for the same contribution.

7. The department shall not approve a tax credit if the taxpayer designates a contribution to the certified scholarship organization for the direct benefit of a specific qualified school, specific student, or specific group of students.

(b) To participate in the tax credit program, the scholarship organization shall:

1. File an application with the department. The application shall be in the form prescribed by the department;

2. Submit a copy of the organization's 501(c)(3) determination letter;

3. Demonstrate that the organization has conducted criminal background checks on all of its employees and board members to exclude from employment or governance any individual that might reasonably pose a risk to the appropriate use of contributed funds; and

4. Demonstrate its financial accountability by submitting a financial report for the organization that has been determined by a certified public accountant to be in compliance with generally accepted accounting principles and free of material misstatements.

(c) The department shall promulgate administrative regulations to establish:

1. The procedures and timelines for a nonprofit organization to receive approval as a scholarship organization;

2. The reporting requirements for a scholarship organization, including independent financial audits to verify use of contributions; and

3. Any other procedures necessary to implement this section.

(3) (a) The scholarship organization shall be responsible for determining:

1. If the student is eligible to receive an educational scholarship under this section; and

2. The amount of educational scholarship granted to an eligible student.

(b) A scholarship organization shall not:

1. Award an educational scholarship to a dependent of a member of the scholarship organization's board of directors or staff; or

2. Accept a contribution from a taxpayer if the taxpayer designates that the contribution shall be used to award an educational scholarship to a particular student, group of students, or particular qualified school.

(4) The scholarship organization shall:

(a) Distribute educational scholarship payments as checks made out to:

1. An eligible student's parent or guardian; and

2. The qualified school;

(b) Provide a written receipt to taxpayers for contributions made to the scholarship organization;

(c) Distribute at least ninety percent (90%) of all cash contributions received as educational scholarships under this section;

(d) Distribute one hundred percent (100%) of all revenue received from interest and investments as educational scholarships under this section; and

(e) Report to the department by December 1, 2016, and by September 1 of each year thereafter:

1. For each eligible student receiving an educational scholarship under this section:

a. The eligible student's name, age, and county of residence;

b. The name of the NCLB improvement school the student attended

- the previous year, if applicable;*
- c. The name of the qualified school in which the eligible student is currently enrolled;*
- d. The grade in which the student is enrolled;*
- e. The amount of educational scholarship granted to or on behalf of the eligible student;*
- f. The name and Social Security number of the eligible student's parent or guardian to whom payment was made; and*
- g. Any additional information the department may require;*
- 2. The total number of taxpayers who contributed to the scholarship organization;*
- 3. The total amount contributed by each taxpayer; and*
- 4. The total number of eligible students that received an educational scholarship under this section.*
- (5) The department shall publish on its Internet Web site an up-to-date list of scholarship organizations that qualify to participate. Only contributions to scholarship organizations on the list maintained by the department shall be recognized for awarding tax credits under this section. The department shall make the list available to the Kentucky Department of Education, which shall also publish the list on its Web site.*
- (6) If the department determines that a scholarship organization no longer meets the requirements of this section, the department shall remove the organization's name from the list required in subsection (5) of this section at the beginning of the next fiscal year, and the organization may not reapply for inclusion on the list until the fiscal year after the year of removal.*

➔Section 2. KRS 141.010 is amended to read as follows:

As used in this chapter, unless the context requires otherwise:

- (1) "Commissioner" means the commissioner of the Department of Revenue;
- (2) "Department" means the Department of Revenue;
- (3) "Internal Revenue Code" means the Internal Revenue Code in effect on December 31, 2013, exclusive of any amendments made subsequent to that date, other than amendments that extend provisions in effect on December 31, 2013, that would otherwise terminate, and as modified by KRS 141.0101;
- (4) "Dependent" means those persons defined as dependents in the Internal Revenue Code;
- (5) "Fiduciary" means "fiduciary" as defined in Section 7701(a)(6) of the Internal Revenue Code;
- (6) "Fiscal year" means "fiscal year" as defined in Section 7701(a)(24) of the Internal Revenue Code;
- (7) "Individual" means a natural person;
- (8) "Modified gross income" means the greater of:
  - (a) Adjusted gross income as defined in Section 62 of the Internal Revenue Code of 1986, including any subsequent amendments in effect on December 31 of the taxable year, and adjusted as follows:
    1. Include interest income derived from obligations of sister states and political subdivisions thereof; and
    2. Include lump-sum pension distributions taxed under the special transition rules of Pub. L. No. 104-188, sec. 1401(c)(2); or
  - (b) Adjusted gross income as defined in subsection (10) of this section and adjusted to include lump-sum pension distributions taxed under the special transition rules of Pub. L. No. 104-188, sec. 1401(c)(2);
- (9) "Gross income," in the case of taxpayers other than corporations, means "gross income" as defined in Section 61 of the Internal Revenue Code;
- (10) "Adjusted gross income," in the case of taxpayers other than corporations, means

gross income as defined in subsection (9) of this section minus the deductions allowed individuals by Section 62 of the Internal Revenue Code and as modified by KRS 141.0101 and adjusted as follows, except that deductions shall be limited to amounts allocable to income subject to taxation under the provisions of this chapter, and except that nothing in this chapter shall be construed to permit the same item to be deducted more than once:

- (a) Exclude income that is exempt from state taxation by the Kentucky Constitution and the Constitution and statutory laws of the United States and Kentucky;
- (b) Exclude income from supplemental annuities provided by the Railroad Retirement Act of 1937 as amended and which are subject to federal income tax by Public Law 89-699;
- (c) Include interest income derived from obligations of sister states and political subdivisions thereof;
- (d) Exclude employee pension contributions picked up as provided for in KRS 6.505, 16.545, 21.360, 61.560, 65.155, 67A.320, 67A.510, 78.610, and 161.540 upon a ruling by the Internal Revenue Service or the federal courts that these contributions shall not be included as gross income until such time as the contributions are distributed or made available to the employee;
- (e) Exclude Social Security and railroad retirement benefits subject to federal income tax;
- (f) Include, for taxable years ending before January 1, 1991, all overpayments of federal income tax refunded or credited for taxable years;
- (g) Deduct, for taxable years ending before January 1, 1991, federal income tax paid for taxable years ending before January 1, 1990;
- (h) Exclude any money received because of a settlement or judgment in a lawsuit brought against a manufacturer or distributor of "Agent Orange" for damages



resulting from exposure to Agent Orange by a member or veteran of the Armed Forces of the United States or any dependent of such person who served in Vietnam;

- (i) 1. For taxable years ending prior to December 31, 2005, exclude the applicable amount of total distributions from pension plans, annuity contracts, profit-sharing plans, retirement plans, or employee savings plans.

The "applicable amount" shall be:

- a. Twenty-five percent (25%), but not more than six thousand two hundred fifty dollars (\$6,250), for taxable years beginning after December 31, 1994, and before January 1, 1996;
  - b. Fifty percent (50%), but not more than twelve thousand five hundred dollars (\$12,500), for taxable years beginning after December 31, 1995, and before January 1, 1997;
  - c. Seventy-five percent (75%), but not more than eighteen thousand seven hundred fifty dollars (\$18,750), for taxable years beginning after December 31, 1996, and before January 1, 1998; and
  - d. One hundred percent (100%), but not more than thirty-five thousand dollars (\$35,000), for taxable years beginning after December 31, 1997.
2. For taxable years beginning after December 31, 2005, exclude up to forty-one thousand one hundred ten dollars (\$41,110) of total distributions from pension plans, annuity contracts, profit-sharing plans, retirement plans, or employee savings plans.
  3. As used in this paragraph:
    - a. "Distributions" includes but is not limited to any lump-sum distribution from pension or profit-sharing plans qualifying for the

- income tax averaging provisions of Section 402 of the Internal Revenue Code; any distribution from an individual retirement account as defined in Section 408 of the Internal Revenue Code; and any disability pension distribution;
- b. "Annuity contract" has the same meaning as set forth in Section 1035 of the Internal Revenue Code; and
  - c. "Pension plans, profit-sharing plans, retirement plans, or employee savings plans" means any trust or other entity created or organized under a written retirement plan and forming part of a stock bonus, pension, or profit-sharing plan of a public or private employer for the exclusive benefit of employees or their beneficiaries and includes plans qualified or unqualified under Section 401 of the Internal Revenue Code and individual retirement accounts as defined in Section 408 of the Internal Revenue Code;
- (j) 1. a. Exclude the portion of the distributive share of a shareholder's net income from an S corporation subject to the franchise tax imposed under KRS 136.505 or the capital stock tax imposed under KRS 136.300; and
- b. Exclude the portion of the distributive share of a shareholder's net income from an S corporation related to a qualified subchapter S subsidiary subject to the franchise tax imposed under KRS 136.505 or the capital stock tax imposed under KRS 136.300.
2. The shareholder's basis of stock held in a S corporation where the S corporation or its qualified subchapter S subsidiary is subject to the franchise tax imposed under KRS 136.505 or the capital stock tax imposed under KRS 136.300 shall be the same as the basis for federal income tax purposes;

- (k) Exclude, to the extent not already excluded from gross income, any amounts paid for health insurance, or the value of any voucher or similar instrument used to provide health insurance, which constitutes medical care coverage for the taxpayer, the taxpayer's spouse, and dependents, or for any person authorized to be provided excludable coverage by the taxpayer pursuant to the federal Patient Protection and Affordable Care Act of 2010, Pub. L. No. 111-148, or the Health Care and Education Reconciliation Act of 2010 Pub. L. No. 111-152, during the taxable year. Any amounts paid by the taxpayer for health insurance that are excluded pursuant to this paragraph shall not be allowed as a deduction in computing the taxpayer's net income under subsection (11) of this section;
- (l) Exclude income received for services performed as a precinct worker for election training or for working at election booths in state, county, and local primary, regular, or special elections;
- (m) Exclude any amount paid during the taxable year for insurance for long-term care as defined in KRS 304.14-600;
- (n) Exclude any capital gains income attributable to property taken by eminent domain;
- (o) Exclude any amount received by a producer of tobacco or a tobacco quota owner from the multistate settlement with the tobacco industry, known as the Master Settlement Agreement, signed on November 22, 1998;
- (p) Exclude any amount received from the secondary settlement fund, referred to as "Phase II," established by tobacco companies to compensate tobacco farmers and quota owners for anticipated financial losses caused by the national tobacco settlement;
- (q) Exclude any amount received from funds of the Commodity Credit Corporation for the Tobacco Loss Assistance Program as a result of a

reduction in the quantity of tobacco quota allotted;

- (r) Exclude any amount received as a result of a tobacco quota buydown program that all quota owners and growers are eligible to participate in;
- (s) Exclude state Phase II payments received by a producer of tobacco or a tobacco quota owner;
- (t) Exclude all income from all sources for active duty and reserve members and officers of the Armed Forces of the United States or National Guard who are killed in the line of duty, for the year during which the death occurred and the year prior to the year during which the death occurred. For the purposes of this paragraph, "all income from all sources" shall include all federal and state death benefits payable to the estate or any beneficiaries;~~and~~
- (u) For taxable years beginning on or after January 1, 2010, exclude all military pay received by active duty members of the Armed Forces of the United States, members of reserve components of the Armed Forces of the United States, and members of the National Guard, including compensation for state active duty as described in KRS 38.205; ***and***
- (v) ***For taxable years beginning after December 31, 2015, exclude the amount received by an eligible student or by an individual on behalf of an eligible student as an educational scholarship from a scholarship organization pursuant to Section 1 of this Act;***

(11) "Net income," in the case of taxpayers other than corporations, means adjusted gross income as defined in subsection (10) of this section, minus:

- (a) The deduction allowed by KRS 141.0202;
- (b) Any amount paid for vouchers or similar instruments that provide health insurance coverage to employees or their families;
- (c) For taxable years beginning on or after January 1, 2010, the amount of domestic production activities deduction calculated at six percent (6%) as

allowed in Section 199(a)(2) of the Internal Revenue Code for taxable years beginning before 2010; and

- (d) 1. All the deductions allowed individuals by Chapter 1 of the Internal Revenue Code as modified by KRS 141.0101 except:
- a. Any deduction allowed by the Internal Revenue Code for state or foreign taxes measured by gross or net income, including state and local general sales taxes allowed in lieu of state and local income taxes under the provisions of Section 164(b)(5) of the Internal Revenue Code;
  - b. Any deduction allowed by the Internal Revenue Code for amounts allowable under KRS 140.090(1)(h) in calculating the value of the distributive shares of the estate of a decedent, unless there is filed with the income return a statement that such deduction has not been claimed under KRS 140.090(1)(h);
  - c. The deduction for personal exemptions allowed under Section 151 of the Internal Revenue Code and any other deductions in lieu thereof;
  - d. For taxable years beginning on or after January 1, 2010, the domestic production activities deduction allowed under Section 199 of the Internal Revenue Code;
  - e. Any deduction for amounts paid to any club, organization, or establishment which has been determined by the courts or an agency established by the General Assembly and charged with enforcing the civil rights laws of the Commonwealth, not to afford full and equal membership and full and equal enjoyment of its goods, services, facilities, privileges, advantages, or accommodations to any person because of race, color, religion,

national origin, or sex, except nothing shall be construed to deny a deduction for amounts paid to any religious or denominational club, group, or establishment or any organization operated solely for charitable or educational purposes which restricts membership to persons of the same religion or denomination in order to promote the religious principles for which it is established and maintained;

- f. Any deduction directly or indirectly allocable to income which is either exempt from taxation or otherwise not taxed under this chapter;
- g. The itemized deduction limitation established in 26 U.S.C. sec. 68 shall be determined using the applicable amount from 26 U.S.C. sec. 68 as it existed on December 31, 2006; and
- h. A taxpayer may elect to claim the standard deduction allowed by KRS 141.081 instead of itemized deductions allowed pursuant to 26 U.S.C. sec. 63 and as modified by this section; and

- 2. Nothing in this chapter shall be construed to permit the same item to be deducted more than once;

(12) "Gross income," in the case of corporations, means "gross income" as defined in Section 61 of the Internal Revenue Code and as modified by KRS 141.0101 and adjusted as follows:

- (a) Exclude income that is exempt from state taxation by the Kentucky Constitution and the Constitution and statutory laws of the United States;
- (b) Exclude all dividend income received after December 31, 1969;
- (c) Include interest income derived from obligations of sister states and political subdivisions thereof;
- (d) Exclude fifty percent (50%) of gross income derived from any disposal of coal

- covered by Section 631(c) of the Internal Revenue Code if the corporation does not claim any deduction for percentage depletion, or for expenditures attributable to the making and administering of the contract under which such disposition occurs or to the preservation of the economic interests retained under such contract;
- (e) Include in the gross income of lessors income tax payments made by lessees to lessors, under the provisions of Section 110 of the Internal Revenue Code, and exclude such payments from the gross income of lessees;
  - (f) Include the amount calculated under KRS 141.205;
  - (g) Ignore the provisions of Section 281 of the Internal Revenue Code in computing gross income;
  - (h) Exclude income from "safe harbor leases" (Section 168(f)(8) of the Internal Revenue Code);
  - (i) Exclude any amount received by a producer of tobacco or a tobacco quota owner from the multistate settlement with the tobacco industry, known as the Master Settlement Agreement, signed on November 22, 1998;
  - (j) Exclude any amount received from the secondary settlement fund, referred to as "Phase II," established by tobacco companies to compensate tobacco farmers and quota owners for anticipated financial losses caused by the national tobacco settlement;
  - (k) Exclude any amount received from funds of the Commodity Credit Corporation for the Tobacco Loss Assistance Program as a result of a reduction in the quantity of tobacco quota allotted;
  - (l) Exclude any amount received as a result of a tobacco quota buydown program that all quota owners and growers are eligible to participate in;
  - (m) For taxable years beginning after December 31, 2004, and before January 1, 2007, exclude the distributive share income or loss received from a

corporation defined in subsection (24)(b) of this section whose income has been subject to the tax imposed by KRS 141.040. The exclusion provided in this paragraph shall also apply to a taxable year that begins prior to January 1, 2005, if the tax imposed by KRS 141.040 is paid on the distributive share income by a corporation defined in subparagraphs 2. to 8. of subsection (24)(b) of this section with a return filed for a period of less than twelve (12) months that begins on or after January 1, 2005, and ends on or before December 31, 2005. This paragraph shall not be used to delay payment of the tax imposed by KRS 141.040; and

- (n) Exclude state Phase II payments received by a producer of tobacco or a tobacco quota owner;
- (13) "Net income," in the case of corporations, means "gross income" as defined in subsection (12) of this section minus:
- (a) The deduction allowed by KRS 141.0202;
  - (b) Any amount paid for vouchers or similar instruments that provide health insurance coverage to employees or their families;
  - (c) For taxable years beginning on or after January 1, 2010, the amount of domestic production activities deduction calculated at six percent (6%) as allowed in Section 199(a)(2) of the Internal Revenue Code for taxable years beginning before 2010; and
  - (d) All the deductions from gross income allowed corporations by Chapter 1 of the Internal Revenue Code and as modified by KRS 141.0101, except:
    - 1. Any deduction for a state tax which is computed, in whole or in part, by reference to gross or net income and which is paid or accrued to any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, any territory or possession of the United States, or to any foreign country or political subdivision thereof;



2. The deductions contained in Sections 243, 244, 245, and 247 of the Internal Revenue Code;
3. The provisions of Section 281 of the Internal Revenue Code shall be ignored in computing net income;
4. Any deduction directly or indirectly allocable to income which is either exempt from taxation or otherwise not taxed under the provisions of this chapter, and nothing in this chapter shall be construed to permit the same item to be deducted more than once;
5. Exclude expenses related to "safe harbor leases" (Section 168(f)(8) of the Internal Revenue Code);
6. Any deduction for amounts paid to any club, organization, or establishment which has been determined by the courts or an agency established by the General Assembly and charged with enforcing the civil rights laws of the Commonwealth, not to afford full and equal membership and full and equal enjoyment of its goods, services, facilities, privileges, advantages, or accommodations to any person because of race, color, religion, national origin, or sex, except nothing shall be construed to deny a deduction for amounts paid to any religious or denominational club, group, or establishment or any organization operated solely for charitable or educational purposes which restricts membership to persons of the same religion or denomination in order to promote the religious principles for which it is established and maintained;
7. Any deduction prohibited by KRS 141.205;
8. Any dividends-paid deduction of any captive real estate investment trust;  
and
9. For taxable years beginning on or after January 1, 2010, the domestic

production activities deduction allowed under Section 199 of the Internal Revenue Code;

- (14) (a) "Taxable net income," in the case of corporations that are taxable in this state, means "net income" as defined in subsection (13) of this section;
- (b) "Taxable net income," in the case of corporations that are taxable in this state and taxable in another state, means "net income" as defined in subsection (13) of this section and as allocated and apportioned under KRS 141.120. A corporation is taxable in another state if, in any state other than Kentucky, the corporation is required to file a return for or pay a net income tax, franchise tax measured by net income, franchise tax for the privilege of doing business, or corporate stock tax;
- (c) "Taxable net income," in the case of homeowners' associations as defined in Section 528(c) of the Internal Revenue Code, means "taxable income" as defined in Section 528(d) of the Internal Revenue Code. Notwithstanding the provisions of subsection (3) of this section, the Internal Revenue Code sections referred to in this paragraph shall be those code sections in effect for the applicable tax year; and
- (d) "Taxable net income," in the case of a corporation that meets the requirements established under Section 856 of the Internal Revenue Code to be a real estate investment trust, means "real estate investment trust taxable income" as defined in Section 857(b)(2) of the Internal Revenue Code, except that a captive real estate investment trust shall not be allowed any deduction for dividends paid;
- (15) "Person" means "person" as defined in Section 7701(a)(1) of the Internal Revenue Code;
- (16) "Taxable year" means the calendar year or fiscal year ending during such calendar year, upon the basis of which net income is computed, and in the case of a return

made for a fractional part of a year under the provisions of this chapter or under regulations prescribed by the commissioner, "taxable year" means the period for which the return is made;

- (17) "Resident" means an individual domiciled within this state or an individual who is not domiciled in this state, but maintains a place of abode in this state and spends in the aggregate more than one hundred eighty-three (183) days of the taxable year in this state;
- (18) "Nonresident" means any individual not a resident of this state;
- (19) "Employer" means "employer" as defined in Section 3401(d) of the Internal Revenue Code;
- (20) "Employee" means "employee" as defined in Section 3401(c) of the Internal Revenue Code;
- (21) "Number of withholding exemptions claimed" means the number of withholding exemptions claimed in a withholding exemption certificate in effect under KRS 141.325, except that if no such certificate is in effect, the number of withholding exemptions claimed shall be considered to be zero;
- (22) "Wages" means "wages" as defined in Section 3401(a) of the Internal Revenue Code and includes other income subject to withholding as provided in Section 3401(f) and Section 3402(k), (o), (p), (q), and (s) of the Internal Revenue Code;
- (23) "Payroll period" means "payroll period" as defined in Section 3401(b) of the Internal Revenue Code;
- (24) (a) For taxable years beginning before January 1, 2005, and after December 31, 2006, "corporation" means "corporation" as defined in Section 7701(a)(3) of the Internal Revenue Code; and
- (b) For taxable years beginning after December 31, 2004, and before January 1, 2007, "corporations" means:
1. "Corporations" as defined in Section 7701(a)(3) of the Internal Revenue

- Code;
2. S corporations as defined in Section 1361(a) of the Internal Revenue Code;
  3. A foreign limited liability company as defined in KRS 275.015;
  4. A limited liability company as defined in KRS 275.015;
  5. A professional limited liability company as defined in KRS 275.015;
  6. A foreign limited partnership as defined in KRS 362.2-102(9);
  7. A limited partnership as defined in KRS 362.2-102(14);
  8. A limited liability partnership as defined in KRS 362.155(7) or in 362.1-101(7) or (8);
  9. A real estate investment trust as defined in Section 856 of the Internal Revenue Code;
  10. A regulated investment company as defined in Section 851 of the Internal Revenue Code;
  11. A real estate mortgage investment conduit as defined in Section 860D of the Internal Revenue Code;
  12. A financial asset securitization investment trust as defined in Section 860L of the Internal Revenue Code; and
  13. Other similar entities created with limited liability for their partners, members, or shareholders.

For purposes of this paragraph, "corporation" shall not include any publicly traded partnership as defined by Section 7704(b) of the Internal Revenue Code that is treated as a partnership for federal tax purposes under Section 7704(c) of the Internal Revenue Code or its publicly traded partnership affiliates. As used in this paragraph, "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;

- (25) "Doing business in this state" includes but is not limited to:
- (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 (1) 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.

Nothing in this subsection shall be interpreted in a manner that goes beyond the limitations imposed and protections provided by the United States Constitution or Pub. L. No. 86-272;

- (26) "Pass-through entity" means any partnership, S corporation, limited liability company, limited liability partnership, limited partnership, or similar entity recognized by the laws of this state that is not taxed for federal purposes at the entity level, but instead passes to each partner, member, shareholder, or owner their proportionate share of income, deductions, gains, losses, credits, and any other similar attributes;
- (27) "S corporation" means "S corporation" as defined in Section 1361(a) of the Internal Revenue Code;
- (28) "Limited liability pass-through entity" means any pass-through entity that affords

any of its partners, members, shareholders, or owners, through function of the laws of this state or laws recognized by this state, protection from general liability for actions of the entity; and

(29) "Captive real estate investment trust" means a real estate investment trust as defined in Section 856 of the Internal Revenue Code that meets the following requirements:

- (a)
  - 1. The shares or other ownership interests of the real estate investment trust are not regularly traded on an established securities market; or
  - 2. The real estate investment trust does not have enough shareholders or owners to be required to register with the Securities and Exchange Commission; and
- (b)
  - 1. The maximum amount of stock or other ownership interest that is owned or constructively owned by a corporation equals or exceeds:
    - a. Twenty-five percent (25%), if the corporation does not occupy property owned, constructively owned, or controlled by the real estate investment trust; or
    - b. Ten percent (10%), if the corporation occupies property owned, constructively owned, or controlled by the real estate investment trust.

The total ownership interest of a corporation shall be determined by aggregating all interests owned or constructively owned by a corporation;

- 2. For the purposes of this paragraph:
  - a. "Corporation" means a corporation taxable under KRS 141.040, and includes an affiliated group as defined in KRS 141.200, that is required to file a consolidated return pursuant to the provisions of KRS 141.200; and
  - b. "Owned or constructively owned" means owning shares or having

an ownership interest in the real estate investment trust, or owning an interest in an entity that owns shares or has an ownership interest in the real estate investment trust. Constructive ownership shall be determined by looking across multiple layers of a multilayer pass-through structure; and

- (c) The real estate investment trust is not owned by another real estate investment trust.

➔Section 3. KRS 141.0205 is amended to read as follows:

If a taxpayer is entitled to more than one (1) of the tax credits allowed against the tax imposed by KRS 141.020, 141.040, and 141.0401, the priority of application and use of the credits shall be determined as follows:

- (1) The nonrefundable business incentive credits against the tax imposed by KRS 141.020 shall be taken in the following order:
  - (a) 1. For taxable years beginning after December 31, 2004, and before January 1, 2007, the corporation income tax credit permitted by KRS 141.420(3)(a);
  - 2. For taxable years beginning after December 31, 2006, the limited liability entity tax credit permitted by KRS 141.0401;
  - (b) The economic development credits computed under KRS 141.347, 141.381, 141.384, 141.400, 141.401, 141.402, 141.403, 141.407, 141.415, 154.12-2088, and 154.27-080;
  - (c) The qualified farming operation credit permitted by KRS 141.412;
  - (d) The certified rehabilitation credit permitted by KRS 171.397(1)(a);
  - (e) The health insurance credit permitted by KRS 141.062;
  - (f) The tax paid to other states credit permitted by KRS 141.070;
  - (g) The credit for hiring the unemployed permitted by KRS 141.065;
  - (h) The recycling or composting equipment credit permitted by KRS 141.390;

- (i) The tax credit for cash contributions in investment funds permitted by KRS 154.20-263 in effect prior to July 15, 2002, and the credit permitted by KRS 154.20-258;
  - (j) The coal incentive credit permitted under KRS 141.0405;
  - (k) The research facilities credit permitted under KRS 141.395;
  - (l) The employer GED incentive credit permitted under KRS 164.0062;
  - (m) The voluntary environmental remediation credit permitted by KRS 141.418;
  - (n) The biodiesel and renewable diesel credit permitted by KRS 141.423;
  - (o) The environmental stewardship credit permitted by KRS 154.48-025;
  - (p) The clean coal incentive credit permitted by KRS 141.428;
  - (q) The ethanol credit permitted by KRS 141.4242;
  - (r) The cellulosic ethanol credit permitted by KRS 141.4244;
  - (s) The energy efficiency credits permitted by KRS 141.436;
  - (t) The railroad maintenance and improvement credit permitted by KRS 141.385;
  - (u) The Endow Kentucky credit permitted by KRS 141.438;
  - (v) The New Markets Development Program credit permitted by KRS 141.434;
  - (w) The food donation credit permitted by KRS 141.392;
  - (x) The distilled spirits credit permitted by KRS 141.389;~~and~~
  - (y) The angel investor credit permitted by KRS 141.396; ***and***
  - (z) ***The scholarship for at-risk children tax credit permitted by Section 1 of this Act.***
- (2) After the application of the nonrefundable credits in subsection (1) of this section, the nonrefundable personal tax credits against the tax imposed by KRS 141.020 shall be taken in the following order:
- (a) The individual credits permitted by KRS 141.020(3);
  - (b) The credit permitted by KRS 141.066;
  - (c) The tuition credit permitted by KRS 141.069;



- (d) The household and dependent care credit permitted by KRS 141.067; and
  - (e) The new home credit permitted by KRS 141.388.
- (3) After the application of the nonrefundable credits provided for in subsection (2) of this section, the refundable credits against the tax imposed by KRS 141.020 shall be taken in the following order:
- (a) The individual withholding tax credit permitted by KRS 141.350;
  - (b) The individual estimated tax payment credit permitted by KRS 141.305;
  - (c) For taxable years beginning after December 31, 2004, and before January 1, 2007, the corporation income tax credit permitted by KRS 141.420(3)(c);
  - (d) The certified rehabilitation credit permitted by KRS 171.3961 and 171.397(1)(b); and
  - (e) The film industry tax credit allowed by KRS 141.383.
- (4) The nonrefundable credit permitted by KRS 141.0401 shall be applied against the tax imposed by KRS 141.040.
- (5) The following nonrefundable credits shall be applied against the sum of the tax imposed by KRS 141.040 after subtracting the credit provided for in subsection (4) of this section, and the tax imposed by KRS 141.0401 in the following order:
- (a) The economic development credits computed under KRS 141.347, 141.381, 141.384, 141.400, 141.401, 141.402, 141.403, 141.407, 141.415, 154.12-2088, and 154.27-080;
  - (b) The qualified farming operation credit permitted by KRS 141.412;
  - (c) The certified rehabilitation credit permitted by KRS 171.397(1)(a);
  - (d) The health insurance credit permitted by KRS 141.062;
  - (e) The unemployment credit permitted by KRS 141.065;
  - (f) The recycling or composting equipment credit permitted by KRS 141.390;
  - (g) The coal conversion credit permitted by KRS 141.041;
  - (h) The enterprise zone credit permitted by KRS 154.45-090, for taxable periods

ending prior to January 1, 2008;

- (i) The tax credit for cash contributions to investment funds permitted by KRS 154.20-263 in effect prior to July 15, 2002, and the credit permitted by KRS 154.20-258;
- (j) The coal incentive credit permitted under KRS 141.0405;
- (k) The research facilities credit permitted under KRS 141.395;
- (l) The employer GED incentive credit permitted under KRS 164.0062;
- (m) The voluntary environmental remediation credit permitted by KRS 141.418;
- (n) The biodiesel and renewable diesel credit permitted by KRS 141.423;
- (o) The environmental stewardship credit permitted by KRS 154.48-025;
- (p) The clean coal incentive credit permitted by KRS 141.428;
- (q) The ethanol credit permitted by KRS 141.4242;
- (r) The cellulosic ethanol credit permitted by KRS 141.4244;
- (s) The energy efficiency credits permitted by KRS 141.436;
- (t) The ENERGY STAR home or ENERGY STAR manufactured home credit permitted by KRS 141.437;
- (u) The railroad maintenance and improvement credit permitted by KRS 141.385;
- (v) The railroad expansion credit permitted by KRS 141.386;
- (w) The Endow Kentucky credit permitted by KRS 141.438;
- (x) The New Markets Development Program credit permitted by KRS 141.434;
- (y) The food donation credit permitted by KRS 141.392;~~and~~
- (z) The distilled spirits credit permitted by KRS 141.389; **and**

**(aa) The scholarship for at-risk children tax credit permitted by Section 1 of this Act.**

- (6) After the application of the nonrefundable credits in subsection (5) of this section, the refundable credits shall be taken in the following order:
  - (a) The corporation estimated tax payment credit permitted by KRS 141.044;

- (b) The certified rehabilitation credit permitted by KRS 171.3961 and 171.397(1)(b); and
- (c) The film industry tax credit allowed in KRS 141.383.