2004

IMPORTANT

This Packet Contains Your Sub-Chapter S Corporation Income Tax Instructions and Return

DUE DATE: MARCH 15, 2005

PLEASE READ IMPORTANT INFORMATION FOR TAX YEAR 2004 INSIDE

397207
State of Arkansas
State Income Tax
P. O. Box 1000
Little Rock, AR 72203-1000

IMPORTANT INFORMATION FOR 2004

NOTE: THE FOLLOWING IS A BRIEF DESCRIPTION OF EACH ACT AND IS NOT INTENDED TO REPLACE A CAREFUL READING OF THE ACT IN ITS ENTIRETY.

State Tax Depreciation Unaffected by New Federal Law
Arkansas has not adopted the depreciation provisions contained in the Job Creation Workers Act of 2002 and the Jobs and Growth Tax Relief Reconciliation Act of 2003.

While the new depreciation provision may be used for federal returns, many states, including Arkansas, operate under a different tax code. On Arkansas income tax returns, taxpayers must file following the rules in sections 167, 168, 179, and 179A under the Internal Revenue Code of 1986, enacted January 1, 1999.

Return Filing Dates Changed (Act 774 of 2003)
1. Changes the due dates of state income tax returns to the due date for the corresponding federal income tax return, March 15 for calendar year filers.
2. Changes the dates that interest and penalty on unpaid income tax begins to accrue to the new return due dates.
3. Changes the dates that estimated tax payments are due to the corresponding federal due date for payments of estimated tax.

Retirement Contribution Limits Clarified (Act 218 of 2003)
This act readopts federal law to allow Arkansas taxpayers to take advantage of increased annual contribution limits for IRAs, 401k, 403b, 457 and SIMPLE plans for state income tax purposes. The act also readopts federal law regarding the taxation of educational IRAs (IRAs established to provide funds for post-secondary education). The act will allow Arkansas taxpayers to take advantage of increased annual contribution limits for educational IRAs for state income tax purposes. This act is effective for tax years 2002 and later.

Income Tax Technical Corrections Act (Act 663 of 2003)
This act amends various state income tax provisions to adopt recent changes to the Internal Revenue Code (IRC) and other changes:
1. Clarifies that qualified withdrawals from IRC §529 Plans established in other states are tax exempt. Non qualified withdrawals are subject to Arkansas income tax.
2. Adopts IRC §117 to clarify the taxability of scholarships, fellowships and stipends.
3. Readopts IRC §131 regarding the exclusion from gross income of qualified foster care payments received by a foster home provider.
4. Readopts IRC §132 regarding the exclusion from gross income of certain non-cash fringe benefits.
5. Readopts IRC §127 regarding the exclusion from gross income of education expenses paid by a taxpayer's employer.
6. Adopts IRC §137 to allow a taxpayer to exclude from gross income adoption-related expenses paid or incurred by the taxpayer's employer under the employer's adoption assistance program.
7. Readopts Subchapter S of the Internal Revenue Code.
8. Adopts IRC §1042 regarding the deferral of gain realized on the sale of a corporation's shares of stock to the corporation's employee stock ownership plan (ESOP).
9. Readopts IRC §221 regarding the deduction of interest paid on qualified educational loans.
10. Readopts IRC §220 regarding the deduction of contributions made to a medical savings account (MSA).
11. Readopts IRC §23 regarding the credit allowed for adoption-related fees and expenses.
12. Adopts IRC §151(c)(6) regarding the tax treatment of kidnapped children.
13. Readopts IRC §21 regarding the credit allowed for household and child care services when such services are used for the purpose of holding gainful employment.

Partnerships and LLCs File Same as Federal (Act 965 of 2003)
This act adopts the federal "check the box" regulations and requires partnerships and LLCs to file in the same manner in which the entity files and pays federal income tax.

Interest on Arkansas Soil and Water Bonds Tax Exempt (Act 598 of 2003)
Revenue bonds issued by the Arkansas Soil and Water Commission are exempt from all state, county and municipal taxes, including income, inheritance and property taxes.

Certain Venture Capital Investments Exempt from Capital Gain (Act 857 of 2003)
Provides an income tax exemption for 100% of the net capital gain derived from a venture capital investment made in a qualified technology-based enterprise, a qualified biotechnology-based enterprise, or a qualified technology incubator client.

New Biodiesel Incentives (Act 1287 of 2003)
The act establishes new incentives for biodiesel suppliers and biodiesel producers. The act provides an income tax credit to biofuels suppliers equal to 5% of the costs of facilities and equipment used directly in the wholesale or retail distribution of biodiesel fuels.

Arkansas Capital Development Corporation Act Amended (Act 860 of 2003)
This act amends current law to broaden the types of business entities that may be formed and reinstates tax credits for investors that purchase equity interests in a capital development company ("CDC"). The act authorizes the formation of statewide venture capital companies with access to state income tax credits as an incentive for investors. The act allows a CDC to be formed as a Limited Liability Company or Partnership in addition to a Corporation. The act also strengthens the regulatory authority of the State Bank Department and requires CDCs to comply with Arkansas securities laws.

New Coal Incentives (Act 993 of 2003)
This act provides an income or insurance premium tax credit of $2.00 per ton of coal mined, produced or extracted on each ton of coal mined in Arkansas by a coal mining enterprise in a tax year. An additional credit of $3.00 per ton will be allowed for each ton of coal mined in Arkansas in excess of 50,000 tons by a coal mining enterprise in a tax year.

Arkansas Existing Workforce Training Act of 1995 Amended (Act 609 of 2003)
This act:
1. Replaces SIC code classifications for manufacturers and firms primarily engaged in commercial physical and biological research with North American Industry Classification System Codes as in effect on January 1, 2003.
2. Increases the out-of-state sales requirement for computer firms;
3. Imposes a completion requirement relating to a consortium;
4. Increases the maximum instructional hourly rate;
5. Added maximum instructional hourly rates for hours delivered by adjunct or part time instructors, safety related training, and for courses with less than 50% eligible participants completing the course.

Consolidated Incentive Act of 2003 (Act 182 of 2003)
This act replaces a number of existing incentive programs including:
1. Advantage Arkansas/Enterprise Zone job creation tax credits;
2. Arkansas Economic Development Act;
3. Sales and Use tax incentive credit.

The act creates new incentives as follows:
1. Provides a Sales and Use tax refund to new and expanding businesses similar to the existing Advantage Arkansas/Enterprise Zone incentive;
2. Establishes a new incentive aimed at businesses that fall into one or more of six categories called "Targeted Businesses";
3. Act provides a payroll rebate that is substantially similar to the old payroll rebate program called "Create Rebate";
4. Provides income tax credits for research and development expenditures;
5. Provides transferable income tax credits for new targeted businesses.

Income Tax Surcharge (Act 38 of the First Extraordinary Session of 2003)
For tax years beginning in 2003, the act imposes a 3% income tax surcharge on all Arkansas taxpayers. The 3% applies to the tax liability computed using existing rates. The surcharge also applies to residents of Texarkana who are otherwise exempt from Arkansas income tax.

BUSINESS AND INCENTIVE TAX CREDITS

1. Purchase of Common Stock of a County and Regional Industrial Development Corporation

ACA 15-4-1224 allows the original purchaser of common stock of a County and Regional Industrial Development Corporation an income tax credit equal to 33%, increased to 33 1/3% beginning January 1, 1999, of the actual purchase price of the stock. In any one tax year the credit shall not exceed 50% of the income tax liability, after all other credits and reductions in tax have been calculated. Any unused credit may be carried forward for the next 3 succeeding tax years or until exhausted, whichever occurs first. Act 37 of 1999 extended the qualifying years through year 2003 and allows Limited Liability Companies (LLC) to participate in this credit. County and Regional Industrial Development Corporations are exempt from Arkansas income tax but are required to file returns according to ACA 15-4-1223.

2. Purchase of Waste Reduction, Reuse or Recycling Machinery or Equipment

ACA 26-51-506 provides an income tax credit equal to 30% of the cost of approved waste reduction, reuse or recycling machinery and equipment. No other credit or deductions, except depreciation, may be claimed on that equipment. Any unused credit may be carried forward for the next 3 succeeding years or until exhausted, whichever comes first.

3. Consolidated Incentive Act

Act 182 of 2003 consolidates the current Biotechnology, Economic Development Incentive Act of 1993, Enterprize Zone, Arkansas Economic Development Act of 1995, Economic Investment Credit and Emerging Technology Credits into a comprehensive set of tax credits with new criteria, measuring devices and documentation requirements. Eligible businesses which signed a financial incentive agreement with the Department of Economic Development prior to March 3, 2003 will continue to be provided the benefits of those programs. Act 182 establishes a Job-Creation Tax Credit equal to 1% of the payroll for new full-time permanent employees for the first 60 months after the incentive agreement is approved. The credits may offset 50% of the business' tax liability. Any unused tax credits may be carried forward for 9 years after the credit is established. Act 182 creates an investment tax credit equal to 10% of the total investment in land, buildings, equipment and costs of licensing and protecting intellectual property of an approved project. The credit may offset 50% of the business' tax liability. Any unused tax credits may be carried forward for 9 years after the credit is established. Act 182 expands the research and development tax credit available under ACA 26-51-1102 by allowing an income tax credit equal to 10% of the amount spent on in-house research in Arkansas, or 33% of the amount spent on in-house research in Arkansas for targeted businesses or in a strategic research area approved by the Department of Economic Development and the Arkansas Science and Technology Authority. The credits may offset 50% of the business tax liability. Any unused tax credits may be carried forward for 3 years after the tax credit is established.

Act 182 establishes a targeted business income tax credit equal to 10% of annual payroll during the term of the financial agreement for a period not to exceed 5 years. The credit cannot exceed $100,000 per year. All credits under Act 182 of 2003 are administered by the Department of Economic Development.

4. Child Care Facility

ACA 26-51-507 provides for an income tax credit of 3.9% of the annual salary of employees employed exclusively in providing child care services if the revenue to the business does not exceed the direct operating costs of the facility. Act 413 of 2001 requires certification of eligible childcare facilities by the Division of Childcare and Early Childhood Education.

ACA 26-51-508 provides that a business which qualifies for the refund of the Gross Receipts Tax or Compensating Use Tax under ACA 26-52-516 or 26-53-132 shall be allowed an income tax credit of 3.9% of the annual salary of its employees employed exclusively in providing child care service, or a $5,000 income tax credit for the first tax year the business provides its employees with a child care facility. This credit is for a business which operates a child care facility for its employees only. Any unused credit may be carried forward for the next 2 succeeding tax years or until exhausted, whichever occurs first.

5. Water Resource Conservation

(a) Water Impoundment outside and within critical areas:

ACA 26-51-1005 and 26-51-1006 provides an income tax credit equal to 50% of the cost of construction and installation or restoration of water impoundments or water control structures of 20 acre-feet or more. The credit shall not exceed the lesser of income tax otherwise due or $9,000. Any unused credit may be carried forward for the next 9 succeeding tax years or until exhausted, whichever occurs first. After March 12, 2001, projects used for commercial purposes can qualify for this credit.

(b) Surface Water Conversion:

1. Outside Critical Areas-ACA 26-51-1007 provides an income tax credit equal to 10% of the cost incurred for the reduction of groundwater use by substitution of surface water for water used for industrial, commercial, agricultural or recreational purposes. The credit shall not exceed the lesser of income tax otherwise due or $9,000. Any unused credit may be carried forward for the next 2 succeeding tax years or until exhausted, whichever occurs first.

2. Within Critical Areas-ACA 26-51–1008 provides an income tax credit equal to 50% of the cost incurred for the reduction of groundwater use by substitution of surface water for water used for industrial, commercial, agricultural or recreational purposes. The credit shall not exceed the lesser of income tax otherwise due or $9,000 for projects approved before August 1, 1997 or using water for agricultural or recreational purposes. For projects using water for industrial or commercial purposes, the credit is limited to the lesser of the income tax otherwise due or $30,000 for projects approved on or after August 1, 1997 and $200,000 for projects approved on or after January 1, 1999. Any unused credit may be carried forward for the next 2 succeeding tax years or until exhausted, whichever occurs first, for projects using water for agricultural or recreational purposes. For projects approved on or after August 1, 1997 and using water for industrial or commercial purposes, any unused credit may be carried forward for the next 4 succeeding tax years or until exhausted, whichever occurs first.

(c) Land Leveling for Water Conservation:

ACA 26-51-1009 provides an income tax credit equal to 10% of the project cost incurred for agricultural land leveling to conserve water. The credit shall not exceed the lesser of income tax otherwise due or $9,000. Any unused credit may be carried forward for the next 2 succeeding tax years or until exhausted, whichever occurs first.

(d) Wetland and Riparian Zone Creation and Restoration:

ACA 26-51-1505 provides for an income tax credit for any taxpayer engaged in the development or restoration of wetlands and riparian zones. The amount of credit shall be equal to the project costs not to exceed the lesser of income tax due or $5,000. Any unused credit may be carried forward for the next 9 succeeding tax years or until exhausted, whichever occurs first.

Any water resource or surface water conservation project ap- proved prior to December 31, 1995 must comply with the provisions established under the Water Resource Conservation and Development Incentives Act of 1985. "Critical areas" means those areas so designated by the Arkansas Soil and Water Conservation Commission.

6. Equipment Donation, Sale Below Cost Or Qualified Research Expenditure

(a) ACA 26-51-1102 provides an income tax credit for a taxpayer who donates or sells below cost new machinery or equipment to a Qualified Educational Institution, or a taxpayer who has qualified research expenditures under a Qualified Research Program. This credit is equal to 33% of the cost of the donation, sale below cost, or qualified expenditure.

(b) ACA 26-51-1103 limits the credit to 50% of the net income tax liability. Any unused credit may be carried forward for the next 3 succeeding tax years or until exhausted, whichever occurs first.

7. Arkansas Economic Development Credit

ACA 15-4-1901 et seq. provides for an income tax credit based on the average wage of the new permanent employees for new or expanding facilities that employ at least 50 new permanent employees and expend at least $5,000,000 on the project. Twenty-five percent (25%) of the employee's annual bonus can be added to calculate the average hourly wage beginning January 1, 1999. The income tax credit amount may vary according to established guidelines. The amount of income tax credit that may be taken in any tax year shall not exceed the Arkansas income tax liability resulting from the project plant or facility. The project plant or facility's income tax liability is to be computed by adding the sales, payroll and property factors of the plant or facility and dividing the sum by 3. This percentage is multiplied by the corporation's Arkansas income tax liability to arrive at the income tax credit available to offset the income tax liability arising from the project as referenced in the financial incentive plan. Form AR1100AEDA, Income Tax Apportionment Worksheet, may be used to compute the project apportionment percentage and available income tax credit. This form may be obtained by contacting Corporation Income Tax Section, P. O. Box 919, Little Rock, AR 72203-0919.

Act 975 of 2001 expands the definition of distribution centers to include facilities that store products owned by other companies, or sells to the public if at least 75% of sales are from out-of-state customers. All other businesses must also derive at least 75% of sales revenue from out-of-state customers. High unemployment is defined as being 150% of the state rate if it is 6% or below, 3% above the state rate if it is above 6%. The credit is now based on the total amount invested divided by the number of years of the incentive plan, instead of the debt service payments.

8. Workforce Training Credit

Act 609 of 2003 amends ACA 6-50-704 which permits an income tax credit based on a portion of the cost of workforce training. If the training is in an Arkansas state supported educational institution, the credit allowed is the lesser of one-half (1/2) of the amount paid by the company or the hourly training cost up to $60 per instructional hour. If training is by company employees or company paid consultants, the tax credit cannot be more than $15 per hour. There is no carryforward period for this credit. Applications for this credit are available from the Arkansas Department of Economic Development at (501) 682-7675.

9. Energy Technology Development Credit
ACA 15-4-2104 allows a tax credit of 50% of the amount spent during the taxable year on a facility located in Arkansas which designs, develops or produces photovoltaic devices, electric vehicle equipment or fuel cells and is put in use after January 1, 2000. The credit allowed may not exceed the amount of the tax imposed for the taxable year reduced by all other state credits allowable. A taxpayer who receives this credit may not claim any other state income tax credit or deduction based on the purchase of machinery and equipment other than depreciation expense. Any unused credit may be carried forward to the next 6 succeeding tax years or until exhausted, whichever occurs first. Act 1284 of 2001 expands the credit to include businesses that design, develop, or produce microturbines, stirling engines or devices reliant on nanotechnology.

10. Tourism Development Credit
ACA 15-11-509 provides for an income tax credit equal to 100 times the average hourly wage paid, up to $3,000, for each new full-time permanent employee of a tourist attraction project approved on or after March 1, 1999. In high unemployment areas this credit increases by a factor of 4 up to $6,000 per employee. Any unused credit may be carried forward to the next 9 succeeding tax years or until exhausted, whichever occurs first. The tourist attraction project will be qualified through the Arkansas Department of Economic Development.

11. Youth Apprenticeship Program
ACA 26-51-509 provides for an income tax credit of $2,000 or 10% of the wages earned by a youth apprentice, whichever is less, to a business participating in the United States Department of Labor apprenticeship program. The credit may not exceed the income tax otherwise due. Any unused credit may be carried forward for the next 2 succeeding tax years or until exhausted, whichever occurs first.

ACA 26-51-1601 et seq. provides for an income tax credit of $2,000 or 10% of the wages earned by a youth apprentice, whichever is less, to a business participating in the Arkansas Vocational and Technical Education Division apprenticeship program. The occupation in which the youth apprentice is employed must not be covered by the United States Department of Labor apprenticeship program as in effect on January 1, 1995. The credit may not exceed the income tax otherwise due. Any unused credit may be carried forward for the next 2 succeeding tax years or until exhausted, whichever occurs first.

12. Biotechnology Development And Training Credit
ACA 2-8-101 et seq. provides an income tax credit for a qualified biotechnology business that is approved through the Arkansas Department of Economic Development as follows:
(a) Biotechnology Facility – 5% of the cost of such facility,
(b) Biotechnology Training – 30% of the cost of employee training or of the Higher Education Partnership,
(c) Biotechnology Research – 20% of the cost of qualified research that exceeds the cost of such research in the base year.

Act 1367 of 1999, effective April 12, 1999, amends the Biotechnology Development and Training Act to provide an income tax credit for an Arkansas taxpayer engaged in the business of producing advanced biofuels through biological means other than fermentation. The credit is limited to 30% of the cost of the buildings, equipment, higher education and licenses necessary to manufacture advanced biofuels. These credits can be used to offset the first $50,000 of income tax liability arising during the credit year and 50% of any remaining tax liability for the year. Any unused credit may be carried forward for the next 9 succeeding years or until exhausted, whichever occurs first. Act 900 of 2001 extends the carryforward period to 14 years and requires the project to be certified before incurring expenditures that qualify for the credit as of August 13, 2001.

13. Biodiesel Incentive Act
ACA 15-4-2801 et seq. establishes an income tax credit to biofuels suppliers equal to 5% of the costs of facilities and equipment used directly in the wholesale or retail distribution of biodiesel fuels. The costs of service contracts, sales tax, or the acquisition of undeveloped land cannot be included in determining the amount of the credit. The credit cannot be claimed by a supplier for any facility or equipment in use on or before the certification of the company for tax credits, or for any facility or equipment for which a supplier previously claimed a tax credit for any other tax year. The limitations on the use of the credit will not apply if an entity is sold and the entity is entitled to credit. The credit can be carried forward for a period not to exceed 3 years. The provisions of the Act apply to tax years beginning on or after January 1, 2003.

14. Tuition Reimbursement Credit
ACA 26-51-1902 permits an income tax credit equal to 30% of the cost of tuition reimbursed by the employer to a full-time permanent employee on or after July 30, 1999. The credit cannot exceed 25% of the business' income tax liability in any tax year. There is no carryforward for this credit. This credit is administered by the Arkansas Department of Economic Development.

15. Family Savings Initiative Credit
ACA 20-86-109, creates the Family Savings Initiative Act, effective July 1, 1999, which provides a tax credit to those taxpayers who make contributions to a designated fiduciary organization created pursuant to this Act. The fiduciary will notify the Department of Human Services of the deposits and will issue a certificate to be attached to the tax return for the first year the credit is taken. The credit allowed is the lesser of the income tax due or $25,000 per taxpayer. The total tax credit allowed for all taxpayers is $100,000 per year. Any unused credit may be carried forward for the next 3 succeeding tax years or until exhausted, whichever occurs first.

16. Public Road Improvement
ACA 15-4-2306 provides a tax credit for those taxpayers who contribute to the "Public Roads Incentive Fund" for the improvement of public roads. The credit is limited to 33% of the total contributions made to the fund and in any tax year is limited to 50% of the Arkansas tax liability after all other credits have been taken. This credit is available for tax years beginning on or after January 1, 1999. Any unused credit can be carried forward for the next 3 succeeding tax years or until the credit is exhausted, whichever occurs first. This program is administered by the Arkansas Department of Economic Development.

17. Low Income Housing Credit
ACA 26-51-1702 provides an income tax credit for a taxpayer owning an interest in a qualified low income building which is approved through the Arkansas Development Finance Authority. The tax credit is computed by multiplying the Federal Low Income Housing Tax Credit for the qualified project by 20%. The credit may not exceed the income tax otherwise due. Any unused credit may be carried forward for the next 5 succeeding tax years or until exhausted, whichever comes first.

18. Purchase of Equity in a Capital Development Company
ACA 15-4-1026 allows the original purchaser of an equity interest in a Capital Development Company an income tax credit equal to 33% of the actual purchase price, limited to 50% of the net income tax liability. Any unused credit may be carried forward for the next 3 succeeding tax years or until exhausted, whichever occurs first. No credit will be allowed for any tax year ending after December 31, 2019.

19. Affordable Neighborhood Housing Credit
ACA 15-5-1301 et seq. provides an income tax credit for any business firm engaged in providing affordable housing which is approved through the Arkansas Development Finance Authority. The tax credit is limited to 30% of the total amount invested in affordable housing assistance activities. The credit may not exceed the income tax otherwise due. Any unused credit may be carried forward for the next 5 succeeding tax years or until exhausted, whichever occurs first.

20. Manufacturer's Investment Tax Credit
ACA 26-51-2001 et seq. provides an income tax credit for investment of at least $100 million before December 31, 2004 in a qualified paper manufacturing business equal to 7% of the investment. The credit shall not exceed 50% of the income tax liability, after all other credits and reductions in tax have been calculated. Any unused credit may be carried forward for the next 6 succeeding years or until exhausted, whichever comes first.

21. Coal Mining Tax Credit
ACA 26-51-511 provides an income or insurance premium tax credit of $2.00 per ton of coal mined, produced or extracted on each ton of coal mined in Arkansas in a tax year. An additional credit of $3.00 per ton will be allowed for each ton of coal mined in Arkansas in excess of 50,000 tons in a tax year. The credit can only be earned if the coal is sold to an electric generation plant for less than $40 per ton excluding freight charges. The credit expires 5 tax years following the tax year in which the credit was earned.

22. Venture Capital Investment Credit
ACA 15-5-1401 et seq. provides an income tax credit up to $10 million per year as recommended by the Arkansas Development Finance Authority and approved by the State Board of Finance. The credit may not exceed the income tax otherwise due. Any unused credit may be carried forward for the next 5 succeeding tax years or until exhausted, whichever occurs first.

The Business and Incentive Tax Credit Forms and instructions may be obtained from:

Department of Finance and Administration
Tax Credit/Special Refunds Section
P.O. Box 1272
Little Rock, AR 72203-1272

or call (501) 682-7106

Important Reminders for 2004

1. Subchapter S of the Federal Internal Revenue code of 1986, as amended, and in effect as of January 1, 2003 has been adopted for Arkansas income tax purposes.

2. If the corporation is the parent of one or more Qualified Subchapter S Subsidiaries (QSSS), the Arkansas subchapter S election, Form AR1103, must be accompanied by Federal Form 966 for each subsidiary that will be filing with the corporation.

3. Small Business Entity Pass Through Act (Act 1103 of 1993)

   A Limited Liability Company is a hybrid business entity with characteristics of a Sub S Corporation and a limited partnership. The members of a Limited Liability Company are shareholders in that they have no personal liability for the debts of the Limited Liability Company. A Limited Liability Company is required to file a Partnership Tax Form, AR1050.

   Act 479 of 1997 amends State law concerning Limited Liability Companies (LLCs), the Uniform Partnership Act, and the Revised Limited Partnership Act to allow mergers and consolidations between LLCs corporation and partnership. Currently, partnerships are not included in the merger provision. The franchise tax provisions are amended to apply to LLCs.

4. Privately Designed Tax Forms

   Computer generated substitute tax forms are not acceptable unless the computer generated format is approved (in advance of use) by the Manager of the Individual Income Tax Section.

5. For telephone information or assistance regarding Small Business Corporate income matters, call (501) 682-7276.

6. To expedite processing of the AR1100S, it is essential that the following items are completed:

   A. Tax Year
   B. Corporation name, address, city, state, zip code
   D. FEIN (Federal Identification Number)
   C. Date of Incorporation
   E. Business Code Number
   F. Date began business in Arkansas
   G. Filing Status (check only one box)
   H. Type of corporation (check only one box)

Subchapter S Corporation Return and Instructions

General Information

Qualifying corporations may select to be treated as a "Small Business (S) Corporation" for Arkansas income tax purposes. The election may be made only if the corporation meets all of the following tests:

1. It is treated as a Small Business Corporation with the Federal Government.
2. It has no more than seventy-five (75) stockholders. A husband and wife (and their estates) are treated as one shareholder for this requirement. All other persons are treated as separate shareholders.
3. It must be a corporation organized or created under the laws of the United States, a state, or territory or it is a similar association taxed as a corporation.
4. Its shareholders are individuals, estates and certain trusts described in IRC 1361.
5. It has no nonresident alien shareholders.
6. It has only one class of stock.
7. It is not an ineligible corporation as defined in IRC 1361.

TO BE RECOGNIZED AS AN ARKANSAS S-CORPORATION
The following must be completed:

1. The business must register with the Arkansas Secretary of State. (501) 682-1010.
2. The business must file an Election by Small Business Form (Federal Form 2553) with the Internal Revenue Service and apply for a Federal Identification Number (Federal Form SS-4). 1-800-829-3676
3. The business must file an Election by Small Business Form (AR1103) with the State of Arkansas (AR1103). 682-7276

For an election to be valid, all persons who are shareholders of the corporation on the first day of the corporation's taxable year or on the day of the election whichever is later, must consent to such election. The Arkansas election form is AR1103.

The election is to be filed with the:

DEPARTMENT OF FINANCE AND ADMINISTRATION
INDIVIDUAL INCOME TAX/S-CORP ELECTION
P. O. BOX 3628
LITTLE ROCK, AR 72203-3628

The annual income tax return of a Small Business Corporation is to be submitted on Form AR1100S. A "Small Business" election permits the taxable income of the Small Business Corporation to be taxed to the shareholders rather than to the corporation. All resident and nonresident shareholders of S Corporations doing business in Arkansas must file a properly executed Arkansas Income Tax Return with the Department of Finance and Administration. Arkansas Income Tax must be paid on the shareholders' taxable income.

Failure to report and remit on the part of any shareholder is grounds upon which the Director shall be authorized to revoke the corporations Subchapter S election and collect the tax from the corporation by any manner authorized by the Arkansas Income Tax Act of 1929 as amended.

Domestic or Foreign Corporation Income Tax-Subchapter S

GENERAL INSTRUCTIONS

The instruction numbers correspond with the item numbers on the return. Unnumbered instructions give general information.

WHO MUST FILE

Every corporation organized or registered under the laws of this state, or having income from Arkansas Code Section 26-51-201 (with the exception of those corporations exempted by Arkansas Code section 26-51-303) must file an income tax return. Consolidated returns are permitted under certain conditions. D.I.S.C. and F.S.C. Corporations should use Form AR1100CT. Corporations must file Form AR1100S if: (a) they elected to be taxed as an S Corporation within seventy-five (75) days of incorporation or doing business in Arkansas, (b) the State of Arkansas accepted the election, and (c) the election remains in effect. Life insurance companies who pay a premium tax as provided by law are exempt from filing.

TIME AND PLACE FOR FILING

Form AR1100S is due on or before the 15th day of the 3rd month following the close of the Corporation's tax year. Forms must be filed with the Department of Finance and Administration, Individual Income Tax/S-Corp, P. O. Box 3628, Little Rock, Arkansas 72203-3628.

EXTENSION OF TIME FOR FILING

If you have received an automatic federal extension (Form 7004), the time for filing your Arkansas S Corporation Income Tax Return shall be extended until the date of your Federal Tax Return. For any extension beyond the automatic federal extension, or in lieu of the federal extension, you must make a written application on or before the due date of your Arkansas Return. The application should be made on Form AR1055.

PERIOD COVERED/ACCOUNTING METHOD

A corporation must calculate its Arkansas Taxable Income using the same income year and accounting method for Arkansas tax purposes as used for Federal income tax purposes. For tax years beginning after 1986 all S Corporations are required to have a permitted tax year. A permitted tax year is a tax year ending December 31, or any other tax year for which the S Corporation established a business purpose.

Application for changes must be made and forwarded to the Department of Finance and Administration, Individual Income Tax Management, at least 60 days before the close of the proposed or new taxable year or period and/or accounting method. The corporation must provide to the Commissioner a copy of any certification or approval from the Internal Revenue Service authorizing the corporation to change its accounting method or income year.

When the Commissioner of Revenue approves a change in the accounting period, the net income computed on the separate return for a fractional part of a year shall be placed on an annual basis by multiplying the amount of income earned during the taxable period by twelve and dividing by the number of months included in the period. Calculate the tax on the annualized income. The annualized tax is then multiplied by the number of months in the taxable period and then divided by twelve (12). The result is the tax liability.

SIGNATURES AND VERIFICATION

The President, Vice-President, Treasurer, or other principal officer shall certify the return. Such agent may certify to the return of a foreign corporation having an agent in the state. If receiver, trustee in bankruptcy, or assignee are operating the property or business of the corporation, such receiver trustee, or assignees shall execute the return for such corporation under certification.

REPORT OF CHANGE IN FEDERAL TAXABLE INCOME

Revenue Agent Reports (RARs) must be reported to this state within 30 days after the receipt of the RAR or supplemental report reflecting correct net income of taxpayer. Amended returns must be filed with payment of any additional tax due. The Statute of Limitation will remain open for eight (8) years if the taxpayer fails to disclose Federal Revenue Agent Reports.

PENALTIES

Willful failure to pay or file a return required under any state tax law is guilty of a Class A Misdemeanor. An additional penalty of $500.00 will be assessed if any taxpayer files what purports to be a return but does not contain information on which substantial correctness may be judged and such conduct is due to a position which impedes the administration of any tax law.

LIABILITY FOR FILING RETURNS

A corporation subject to the provisions of the Income Tax Act of 1929, regardless of the amount of its net income, is required to file a return.

BALANCE SHEET

The balance sheet submitted with the return should be prepared from the books and should agree therewith, or any difference should be reconciled. All corporations engaged in an interstate trade or business and reporting to the Interstate Commerce Commission and to any national, state municipal or other public office may submit copies of their balance sheets prescribed by said Commission, or state and municipal authorities, as of the beginning and end of the taxable year.

If the balance sheet as of the beginning of the current taxable year does not agree in every respect with the balance sheet which was submitted as of the end of the previous taxable year, the difference should be fully explained.

TYPE RETURN

Whether the S Corporation is filing an Initial (first time filing), an Amended Return (making changes to an original return), or a Final Return (going out of business), clearly mark the return and check the applicable box at the top of the form.

INCOME

CAUTION: *Report only trade or business activity income or loss on Line 6 through 11. Do not report rental activity or portfolio income or loss on these lines. Report the Arkansas portion of rental income and expenses and portfolio income and expenses distributable to each shareholder on a Federal Schedule K. Clearly mark "Arkansas" on the Federal Schedule K that contains the Arkansas amounts.*

GROSS SALES

If engaged in trading or manufacturing, enter as item 6 on page 1 of return, the gross receipts, less goods returned and any allowances or discounts from the sale price.

COST OF GOODS SOLD

Enter as item 7 the cost of goods sold, submit schedule and explain fully the method used.

If the production, purchase, or sale of merchandise is an income producing factor in the trade or business, inventories of merchandise on hand should be taken at the beginning and end of the taxable year, which may be valued at the lower of cost or market. Explain fully the method used. In case the inventories reported on the return do not agree with those shown on the balance sheet, attach a statement explaining how the difference occurred.

Balance sheets as of the beginning and close of the year and a reconciliation of surplus must be attached to the return.

GROSS PROFITS

Enter as item 8 the gross profit which is obtained by deducting item 7, the cost of goods sold as extended from item 6, the gross sales.

NET GAIN OR (LOSS) FROM FORM 4797

Enter as item 9, gains or losses from the sale, exchange, or involuntary conversion of assets used in trade or business activity. If the corporation is also a partner in a partnership, include the partner's share of gains (losses) from sales or exchanges, involuntary or compulsory (other then casualties or thefts), of the partnership's trade or business assets. Do not include any recapture of expense deduction for recovery property (Federal Code Section 179).

OTHER INCOME

Enter as line 10 any other taxable trade or business income not listed above and explain its nature on an attached schedule.

DEDUCTIONS

CAUTION: *Report only trade or business activity related expenses on lines 12 through 24. Do not report rental activity expenses or expenses related to any portfolio income on these lines. Report the Arkansas rental activity income and expenses and portfolio income and expenses distributable to each shareholder on a Federal Schedule K. Clearly mark "Arkansas" on the Federal Schedule K that contains the Arkansas amounts.*

COMPENSATION OF OFFICERS

Enter as item 12 the compensation of officers in whatever form paid.

SALARIES AND WAGES

Enter as item 13 the amount of salaries and wages (other than wages and salaries deducted elsewhere on your return) paid or incurred for the tax year. Do not reduce this figure by Federal jobs credit.

REPAIRS

Enter as item 14 the cost of incidental repairs related to any trade or business activity.

Excess Net Passive Income Tax Worksheet

1. Enter Arkansas gross receipts tax for the tax year (See IRC Section 1362 (d)(3)(C) for gross receipts from the sale of capital assets.)* .... ___________
2. Enter Arkansas passive investment income as defined in IRC* Section 1362 (d)(3)(D) .... ___________
3. Enter 25% of Line 1 (If Line 2 is less than Line 3, stop here. You are not liable for this tax.) .... ___________
4. Excess Arkansas passive investment income (Subtract Line 3 from Line 2.) .... ___________
5. Arkansas expenses directly connected with the production of income on Line 2 [See IRC* Section 1375(b)(2)] .... ___________
6. Net passive income (Subtract Line 5 from Line 2.) .... ___________
7. Divide amount on Line 4 by amount on Line 2. .... ___________
8. Excess net passive income (Multiply Line 6 by Line 7.) .... ___________
9. Enter taxable income (See instructions for taxable income below.) .... ___________
10. Enter the smaller of Line 8 or 9. .... ___________
11. Excess net passive income tax – Enter 6.5% of Line 10. Enter here and on Line 27, page 1, Form AR1100S. .... ___________

*Income and expenses on Line 1, 2, and 5 are from total Arkansas operations for the tax year. This includes applicable income and expenses from page 1, Form AR1100S, as well as those that are reported separately on Federal Schedule K. See IRC Section 1375(b)(4) for exceptions regarding Lines 2 and 5.

BAD DEBTS

Enter as item 15 the amount of bad debt incurred during the year. The S Corporation can only use the specific charge-off method for figuring its bad debt deduction.

RENT

Enter as item 16 rent paid for trade or business property in which the S Corporation has no equity.

TAXES

Enter as item 17 taxes paid or accrued during the taxable year. Do not include Arkansas income taxes, Federal income taxes, or taxes assessed against local benefits tending to increase the value of the property.

INTEREST

Enter as item 18 only interest incurred in the trade or business activity of the corporation that is not reported elsewhere on the return. Do not include interest expense related to rental activity, portfolio or investment income.

DEPRECIATION

Enter as item 19 depreciation expense from Federal Form 4562. Do not include any expense for recovery property (Section 179) on this line.

DEPLETION

Enter as item 20 depletion expense from Federal Form 4562. Do not include any depletion deduction for oil and gas properties on this line.

OTHER DEDUCTIONS

Enter as item 24 any other authorized deductions related to any trade or business activity for which there is no line on page 1 of this form.

EXCESS NET PASSIVE INCOME TAX

Enter as item 27 the amount of excess net passive income tax due. If the corporation has always been a Subchapter S Corporation, then line 27 tax does not apply to the corporation. If the corporation has Subchapter C earning and profits at the close of the tax year, has passive investment income that is in excess of 25% of gross receipts, **and** has taxable income at year end, the corporation must pay a tax on the excess passive income. Complete Line 1 through 3 and Line 9 of the worksheet on this page to make this determination. If Line 2 is greater than Line 3 and the corporation has taxable income it must pay the tax. Complete a separate schedule using the format of Line 1 through 11 of the worksheet to figure the tax.

Taxable Income (Line 9 of the Excess Net Passive Income Tax worksheet) - Line 9, taxable income, is defined in IRC Section 1374(d). Figure this income by completing Lines 9 through 32 of **Form AR1100CT**, Arkansas Corporation Income Tax Return. Include the Form AR1100CT computation with the worksheet computation you attached to Form AR1100S. You do not have to attach the schedules etc. called for on Form AR1100CT. However you may want to complete certain schedules such as Federal Schedule D, Form AR1100S.

TAX FORM SCHEDULE D (Form AR1100S)

Enter as item 28 the tax from Schedule D, Form AR1100S, page 2. If net capital gain for Arkansas is $25,000 or less, the corporation is not liable for capital gains tax. If the net capital gain is more than $25,000 you must determine if the corporation owes the tax in part A, or part B of Schedule D, Form AR1100S.

Part A – Capital gains tax computation

If the corporation made its election to be an S Corporation before 1987, IRC Section 1374 (as in effect before the enactment of the Tax Reform Act of 1986) continues to impose a tax on certain gains of the S Corporation. Consult the IRS instructions to determine if you are liable for this tax. If so, complete Part A, Schedule D, Form AR1100S.

Part B – Built-in gains tax computation

If the corporation made its election to be an S Corporation after December 31, 1986, IRC Section 1374 provides for a tax on built-in gains that applies to certain S Corporations. Consult the IRS instructions to determine if you are liable for this tax. If so, complete Part B, Schedule D, Form AR1100S.

INCOME TAX SURCHARGE

Multiple the amount on Line 29 by three percent (3%) and enter the result as item 30

PAYMENTS

Enter as item 32 payments you made on a 2004 Declaration of Estimated Income Tax Form.

Filing Declaration of Estimated Income Tax

Who must file: Every taxpayer who can reasonably expect to owe an Arkansas income tax in excess of $1,000 must make an estimate and pay in equal installments tax due thereon. The declaration shall be filed with the Commissioner of Revenue on or before the fifteenth (15th) day of the fourth (4th) month of the income year of taxpayer. Taxpayers whose income from farming for the income year can reasonably be expected to amount to at least two-thirds (2/3) of the total gross income from all sources for the income year, may file such declaration and pay the estimated tax on or before the fifteenth (15th) day of the second (2nd) month after the close of the income year. In lieu of filing any declaration, the taxpayer may file an income tax return and pay the tax on or before the fifteenth (15th) day of the (3rd) month after the close of the income year.

Payment of Taxes

The tax should be paid by attaching to the return a check or money order payable to "Department of Finance and Administration."

WORKSHEET FOR APPORTIONMENT OF MULTIPLE CORPORATION

For corporations with income from sources within and outside the State:

In general, taxpayers with income derived from activities both within and outside the State (Public Utilities excepted) are required to allocate and apportion the net income under the following provision:

Business and non-business income defined – Article IV 1 (A) defines "Business Income" as income arising from transactions and activities in the regular course of taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's trade or business operation. In essence, all income which arises from the conduct of trade or business operations of a taxpayer is business income. Income of any type or class and from any source is business income if it arises from transactions and activities occurring in the regular course of a trade or business. In general all transactions and activities of the taxpayer which are dependent upon, or contribute to, the operations of the taxpayer's economic enterprise as a whole constitute the taxpayer's trade or business and will be considered "Business Income" unless otherwise excluded by statute.

Business income is to be apportioned to this state by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus two (2) times the sales factor, and the denominator of which is four (4).

The average value of property owned by the taxpayer means the average of the original cost of the property at the beginning and ending of the tax period.

Property rented by the taxpayer is valued at eight times the net annual rental rate.

Tangible personal property includes inventories.

The payroll factor is a fraction, the numerator of which is the total amount paid in this state during the tax period by the taxpayer for compensation, and the denominator of which is the total compensation paid everywhere during the tax period.

Compensation is paid in this state **if**: (a) the individual's service is performed entirely within the state **or**, (b) the individual's service is performed both within and outside the state is incidental to the individual's service within the state **or** (c) some of the service is performed in the state **and** (1) the base of operations, or if there is no base of operations the place from which the service directed or controlled is in the State **or** (2) the base of operations or the place from which the service directed or controlled is not in any state in which some part of the service is performed, but the individual's residence is in the state.

The sales factor is a fraction, the numerator of which is the total sales of the taxpayer in this state during the tax period and the denominator of which is the total sales of the taxpayer everywhere during the tax period. The sale factor is then doubled.

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, 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 (1) the purchaser is the United States Government or (2) the taxpayer is not taxed in the State of the purchaser.

Sales, other than sales of tangible personal property, are in this State if the income producing activity is performed both within and without of the State, in which event the income allocable to this State shall be the percentage that is used in the formula for apportioning business income to this State.

The following items of income to the extent that they do not constitute business income are to be allocated to this state:

1. Net rents and royalties from real property located in the state

2. Net rents and royalties from tangible personal property (a) if and to the extent that the property is used in this state or (b) in their entirety if the commercial domicile is in the state and the taxpayer is not organized under the laws of or taxed in the state in which the property is utilized.

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 taxpayer tangible personal property is utilized in the state in which the property was located at the time the rental or royalty obtained possession.

3. Gains and losses from sales of assets:

    a. Sales of real property located in the state

    b. Sales of tangible personal property

        (1) The property had a situs in this state at the time of sale, **or**

        (2) The taxpayers commercial domicile is in this state, **or**

        (3) The property has been included in depreciation which has been allocated to this state, in which event gains or losses on sales shall be allocated on the percentage that is used in the formula for allocating income to the state.

    c. Sales of intangible personal property if the taxpayer's commercial domiciles in this state

4. Interest and dividends if the taxpayer's commercial domicile is in the state

5. Patent and copyright royalties. If and to the extent that the patent or copyright is utilized by the taxpayers in this state, or if and to the extent that the patent or copyright is utilized by the taxpayer in a state in which the taxpayer is not taxable and the taxpayer's commercial domicile is in this state

    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 the states or if the accounting procedures do not reflect states of utilization, the copyright is utilized in the state in which the taxpayer's commercial domicile is located.

Prior approval is required before deviation from the allocation and apportionment method.

If the allocated and apportionment provisions as set out above do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for, or the Director of Revenue, Department of Finance and Administration may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

1. separate accounting

2. the exclusion of any one or more of the factors

3. the inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state, or

4. the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.