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HOUSE BILL NO. 1417

Offered January 8, 2020

Prefiled January 8, 2020

A *BILL to amend the Code of Virginia by adding in Chapter 3 of Title 58.1 an article numbered 9.1, consisting of sections numbered 58.1-396 through 58.1-399.8, relating to income tax; reporting requirements for partnerships.*

 Patron—Watts

Referred to Committee on Finance

Be it enacted by the General Assembly of Virginia:

1. That the Code of Virginia is amended by adding in Chapter 3 of Title 58.1 an article numbered 9.1, consisting of sections numbered 58.1-396 through 58.1-399.8, as follows:

*Article 9.1.**Reporting Adjustments to Federal Taxable Income from Federal Partnership Audits.***§ 58.1-396. Definitions.**

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

"Administrative adjustment request" means an administrative adjustment request filed by a partnership pursuant to § 6227 of the Internal Revenue Code.

"Audited partnership" means a partnership subject to a partnership-level audit that results in a federal adjustment.

"Corporate partner" means a partner that is subject to tax under Article 10 (§ 58.1-400 et seq.).

"Direct" means, with respect to the relationship between a partner and an audited partnership, that such partner holds a direct interest in such audited partnership and that such interest is not held indirectly through another partnership.

"Exempt" means, with respect to a partner or partnership, that such partner or partnership is exempt from Virginia income taxation. If such partner or partnership has unrelated business taxable income but otherwise is exempt from Virginia income taxation, such partner or partnership shall be considered exempt.

"Federal adjustment" means a change to an item or amount determined under the Internal Revenue Code that is used by a taxpayer to compute Virginia tax owed, regardless of whether that change results from an action by the Internal Revenue Service including a partnership-level audit, or the filing of an amended federal return, federal refund claim, or administrative adjustment request by the taxpayer. A federal adjustment is positive to the extent that it increases Virginia taxable income and is negative to the extent that it decreases Virginia taxable income.

"Federal adjustments report" means any methods or forms required by the Department for use by a partner or partnership to report final federal adjustments.

"Federal partnership representative" means the person that a partnership designates for the taxable year as its representative or the person that the Internal Revenue Service appoints pursuant to § 6223(a) of the Internal Revenue Code to act as the federal partnership representative.

"Final determination date" means the date determined pursuant to the provisions of § 58.1-399.8.

"Final federal adjustment" means a federal adjustment for which the final determination date has passed.

"Indirect" means, with respect to the relationship between a partner and an audited partnership, that such partner does not hold a direct interest in such audited partnership but instead holds its interest indirectly through another partnership that has an interest in the audited partnership.

"Nonresident" means, with respect to a partner, that such partner is not a resident partner.

"Partner" means a person that holds an interest directly or indirectly in a partnership or pass-through entity.

"Partnership" means an entity subject to taxation under Subchapter K, 26 U.S.C. § 701 et seq., of Chapter 1 of Subtitle A of the Internal Revenue Code.

"Partnership-level audit" means an examination by the Internal Revenue Service at the partnership level pursuant to Subchapter C, 26 U.S.C. § 6221 et seq., of Chapter 63 of Subtitle F of the Internal Revenue Code that results in federal adjustments.

"Pass-through entity" means any pass-through entity as defined in § 58.1-390.1. "Pass-through entity" does not include a partnership.

"Resident" means, with respect to an individual partner, that such partner is a resident, as defined in § 58.1-302, for the relevant tax period. "Resident" means, with respect to an estate or trust partner, that

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59 *such partner is a resident estate or trust, as defined in § 58.1-302, for the relevant tax period.*

60 *"Reviewed year" means the taxable year of a partnership that is subject to a partnership-level audit*
61 *from which federal adjustments arise.*

62 *"State partnership representative" means the person identified as the representative of a partnership*
63 *pursuant to the provisions of § 58.1-398.*

64 *"Tiered partner" means any partner that is a partnership or a pass-through entity and is not an*
65 *individual.*

66 *"Unrelated business taxable income" has the same meaning as such term is defined in § 512 of the*
67 *Internal Revenue Code.*

68 **§ 58.1-397. Reporting requirement; administrative adjustment requests.**

69 *Partnerships and partners shall report final federal adjustments arising from a partnership-level*
70 *audit or an administrative adjustment request and make required payments pursuant to the provisions of*
71 *this article and shall not be required to comply with the provisions of § 58.1-311. This section shall not*
72 *apply to adjustments required to be reported for federal income tax purposes pursuant to § 6225(a)(2)*
73 *of the Internal Revenue Code and shall not apply to the distributive share of adjustments that have been*
74 *reported as required under § 58.1-311.*

75 **§ 58.1-398. State partnership representative.**

76 *A. With respect to an action required or permitted to be taken under this article, and with respect to*
77 *any administrative or judicial appeal of such action pursuant to Chapter 18 (§ 58.1-1800 et seq.), the*
78 *state partnership representative, as identified pursuant to the provisions of subsection B, shall have the*
79 *sole authority to act on behalf of a partnership. The actions of the state partnership representative shall*
80 *be binding on the direct partners and indirect partners of the partnership.*

81 *B. The state partnership representative for a reviewed year is the partnership's federal partnership*
82 *representative unless the partnership designates in writing another person as its state partnership*
83 *representative.*

84 *C. The Department shall establish reasonable qualifications and procedures for designating a person,*
85 *other than a federal partnership representative, to be the state partnership representative.*

86 **§ 58.1-399. Reporting and payment requirements for a partnership subject to a final federal**
87 **adjustment.**

88 *A. Except as otherwise provided in this article, any final federal adjustment shall be reported*
89 *pursuant to the provisions of subsection B. This subsection shall not apply to a final federal adjustment*
90 *for which election has been properly made pursuant to § 58.1-399.1.*

91 *B. No later than 90 days after the final determination date, a partnership shall:*

92 *1. File with the Department a completed federal adjustments report, which shall include any*
93 *information required by the Department;*

94 *2. Notify each direct partner of its distributive share of the final federal adjustments and provide to*
95 *each direct partner any other information required by the Department;*

96 *3. File an amended composite return pursuant to § 58.1-395 if such return previously was filed on*
97 *behalf of nonresident partners;*

98 *4. File an amended return pursuant to § 58.1-392; and*

99 *5. Pay any additional amount that may be required pursuant to the provisions of §§ 58.1-395 and*
100 *58.1-486.2.*

101 *C. Except as provided under § 58.1-321, no later than one year after the final determination date,*
102 *each direct partner subject to tax pursuant to the provisions of Article 2 (§ 58.1-320 et seq.), 6*
103 *(§ 58.1-360 et seq.), or 10 (§ 58.1-400) shall:*

104 *1. File a federal adjustments report that identifies the distributive share of adjustments reported to*
105 *such direct partner under subdivision B 2; and*

106 *2. Pay any additional amount of tax due as if final federal adjustments had been properly reported,*
107 *including any penalty and interest due under this title. Such payment may be reduced by any credit for*
108 *related amounts paid or withheld and remitted on behalf of the direct partner pursuant to subdivision B*
109 *3, 4, or 5.*

110 **§ 58.1-399.1. Elective payment by a partnership.**

111 *A. Notwithstanding §§ 58.1-390.2 and 58.1-399, an audited partnership may make an elective*
112 *payment pursuant to the provisions of this section. Such partnership shall:*

113 *1. No later than 90 days after the final determination date, file a completed federal adjustments*
114 *report, which shall include any information required by the Department;*

115 *2. No later than 90 days after a final determination date, notify the Department that it is making an*
116 *elective payment; and*

117 *3. No later than one year after the final determination date, pay the elective payment amount*
118 *specified in subsection B. Such amount shall be in lieu of taxes owed by the direct and indirect*
119 *partners.*

120 *B. The elective payment amount shall be the amount of final federal adjustments, subject to the*

following modifications:

1. The elective payment amount shall exclude the distributive share of final federal adjustments that is reported to a direct exempt partner, provided that such partner is not subject to tax pursuant to the provisions of § 58.1-401;

2. For the total distributive shares of the remaining final federal adjustments reported to (i) any direct corporate partner subject to tax under § 58.1-400 and (ii) any direct exempt partner subject to tax under § 58.1-400 on its unrelated business income or other taxable income, such adjustments shall be apportioned or allocated, as applicable, pursuant to the provisions of §§ 58.1-405 through 58.1-423 and, after such apportionment or allocation, shall be multiplied by the tax rate specified in § 58.1-400 and, after such multiplication, shall be included in the elective payment;

3. For the total distributive shares of the remaining final federal adjustments reported to any nonresident direct partner that is subject to tax under Article 2 (§ 58.1-320 et seq.) or 6 (§ 58.1-360 et seq.), such adjustments shall be sourced to Virginia pursuant to applicable laws governing sourcing, and any adjustments sourced to Virginia shall be multiplied by the highest tax rate specified in § 58.1-320 and, after such multiplication, shall be included in the elective payment;

4. For the total distributive shares of the remaining final federal adjustments reported to any tiered partner, the elective payment shall include the amount specified in this subdivision. Subject to the modifications specified in this subdivision, the amount shall (i) include that portion of the adjustments that are of a type that would be sourced to Virginia pursuant to applicable laws governing sourcing, and (ii) include all adjustments that are of a type that would not be subject to sourcing in Virginia pursuant to applicable laws governing sourcing. However, the amount specified in clause (ii) shall exclude any amount that can be established, under guidelines issued by the Department, to be properly (a) allocable to a nonresident indirect partner, (b) allocable to a partner that is not subject to tax on such amount, or (c) excludable under procedures for alternative reporting and payment as specified in § 58.1-399.3. The amount specified in clauses (i) and (ii), as reduced by the exclusions specified in clauses (a), (b), and (c), shall be multiplied by the highest tax rate specified in § 58.1-320 or 58.1-360, as applicable, and, after such multiplication, shall be included in the elective payment;

5. For the total distributive shares of the remaining final federal adjustments reported to any resident direct partner that is subject to tax under § 58.1-320 or 58.1-360, such adjustments shall be multiplied by the highest tax rate specified in § 58.1-320 or 58.1-360, as applicable, and, after such multiplication, shall be included in the elective payment; and

6. Any penalty and interest provided for by this title shall be included in the elective payment.

§ 58.1-399.2. Tiered partners.

A. The following categories of partners shall be subject to the reporting and payment requirements specified in § 58.1-399, entitled to make elections as provided in § 58.1-399.1, and entitled to elect an alternative reporting and payment method as provided in § 58.1-399.3:

1. Any direct tiered partner of an audited partnership;
2. Any indirect tiered partner of an audited partnership; and
3. Any partner of a partner specified in subdivision 1 or 2.

B. A partner subject to the provisions of subsection A shall make required reports and payments no later than 90 days after the time for filing and providing statements to tiered partners and their partners pursuant to the provisions of § 6226 of the Internal Revenue Code and any regulations promulgated thereunder. The Department may establish procedures and deadlines for reports and payments required pursuant to this section.

§ 58.1-399.3. Alternative reporting and payment method.

Under procedures adopted by and subject to the approval of the Department, an audited partnership or a tiered partner may enter into an agreement with the Department to use an alternative reporting and payment method. However, the Department shall enter into such agreement only if it such audited partnership or tiered partner demonstrates, to the satisfaction of the Department, that the alternative method is reasonably expected to provide for the reporting and payment of taxes, penalties, and interest due under the provisions of this article. Application for approval of an alternative reporting and payment method shall be made by the audited partnership or tiered partner within the applicable time period specified in § 58.1-399.1 or 58.1-399.2.

§ 58.1-399.4. Effect of election.

A. If a partnership or partner makes an election pursuant to § 58.1-399.1 or 58.1-399.3, such election shall not be revocable by such partnership or partner. However, the Department may make a discretionary determination that allows such election to be revoked.

B. If properly reported and paid by the audited partnership or tiered partner, the amount determined pursuant to § 58.1-399.1 or 58.1-399.3 shall be treated as paid in lieu of taxes owed by a direct or indirect partner, to the extent applicable, on the final federal adjustments. A direct partner or indirect partner shall be prohibited from claiming any subtraction, deduction, credit, or refund for such amount.

182 *This section shall not prohibit a partner that is a direct partner and a resident partner from (i) claiming*
183 *a credit against taxes paid to Virginia pursuant to § 58.1-332 or (ii) claiming a credit for any amount*
184 *paid by the audited partnership or tiered partner on the resident partner's behalf to another jurisdiction*
185 *in accordance with the provisions of § 58.1-332.*

186 **§ 58.1-399.5. Failure to pay.**

187 *If an audited partnership or tiered partner fails to timely make any report or payment required by*
188 *this article, the Department may assess the direct and indirect partners of such partnership or partner*
189 *for any taxes owed.*

190 **§ 58.1-399.6. De minimis exception.**

191 *The Department may establish a de minimis tax liability amount. If a partner or partnership has a*
192 *tax liability less than such amount, the Department may exempt such partner or partnership from the*
193 *reporting and payment requirements of this article.*

194 **§ 58.1-399.7. Administration.**

195 *A. For partners and partnerships subject to the provisions of this article, the Department shall*
196 *assess, collect from, and refund any Virginia income tax, interest, and penalties arising from final*
197 *federal adjustments as set forth in this article. If any partner or partnership makes an election pursuant*
198 *to § 58.1-399.1, the Department shall assess and collect in-lieu-of amounts, interest, and penalties*
199 *arising from final federal adjustments as if the in-lieu-of-amounts are a corporate income tax imposed*
200 *pursuant to the provisions of Article 10 (§ 58.1-400 et seq.). Penalties and interest imposed on a partner*
201 *or partnership shall be determined based on the date the partnership return for the reviewed year*
202 *originally was due. If any partner or partnership subject to § 58.1-399 fails to file its federal*
203 *adjustments report within the time required, the provisions of § 58.1-394.1 shall be applicable to such*
204 *report, mutatis mutandis.*

205 *B. Notwithstanding the provisions of subsection C of § 58.1-312, an assessment shall be issued by the*
206 *following dates:*

207 *1. If a partner or partnership files with the Department a federal adjustments report or an amended*
208 *Virginia tax return within the time period specified in § 58.1-399, the Department may assess any*
209 *amounts, including taxes, in-lieu-of-amounts, interest, and penalties arising from those federal*
210 *adjustments, if the Department issues a notice of assessment to the partner or partnership no later than*
211 *the expiration of the one-year period following the date of filing with the Department of the federal*
212 *adjustments report.*

213 *2. If a partner or partnership fails to file the federal adjustments report within the time period*
214 *specified in § 58.1-399, or if the federal adjustments report filed by the partner or partnership omits*
215 *final federal adjustments or understates the correct amount of tax owed, the Department may assess*
216 *amounts or additional amounts including taxes, in-lieu-of-amounts, interest, and penalties arising from*
217 *the final federal adjustments, if the Department issues a notice of assessment to the partner or*
218 *partnership no later than the expiration of the one-year period following the date of filing with the*
219 *Department of the federal adjustments report.*

220 *3. Notwithstanding clause (ii) of § 58.1-1823, an amended return for refund arising from federal*
221 *adjustments made by the Internal Revenue Service shall be filed no later than one year from the date a*
222 *federal adjustments report, as required by § 58.1-399, was due to the Department, including any*
223 *extensions issued pursuant to the provisions of this section. The partner or partnership may, on the*
224 *federal adjustments report, report additional tax due, report a claim for refund or credit of a tax, and*
225 *make any other adjustments resulting from adjustments to the partner's or partnership's federal taxable*
226 *income, including adjustments to its net operating losses.*

227 *4. Unless otherwise agreed to in writing by the partnership or partner and the Department, any*
228 *adjustments by the Department or by the partner or partnership that are made pursuant to the one-year*
229 *statute of limitations provided for in this subsection are limited to adjustments to the partner's or*
230 *partnership's tax liability that arise from federal adjustments.*

231 *C. The one-year statute of limitations provided for in subsection B may be extended:*

232 *1. Automatically, upon written notice to the Department, by 60 days for an audited partnership or a*
233 *tiered partner that has 10,000 or more direct partners; or*

234 *2. By written agreement between the partnership or partner and the Department pursuant to §*
235 *58.1-101.*

236 *D. 1. Any extension granted pursuant to subsection C shall extend by an equal time period the last*
237 *day for the Department to assess any additional amounts arising from the adjustments to federal taxable*
238 *income and the period for filing a claim for refund or credit of taxes.*

239 *2. The one-year statute of limitations provided for in subsection B shall not affect the time within*
240 *which or the amount for which an assessment may otherwise be made or a refund sought under this*
241 *title.*

242 **§ 58.1-399.8. Final determination date.**

243 *A. Except as provided in subsection B, if a federal adjustment arises from an Internal Revenue*

244 *Service audit or other action by the Internal Revenue service, the final determination date is the first*
245 *day on which no federal adjustments arising from such audit or other action remain to be fully*
246 *determined, whether by an Internal Revenue Service decision with respect to which all rights of appeal*
247 *have been exhausted, or, if the Internal Revenue Service decision is appealed or contested, by a final*
248 *judicial decision with respect to which all rights of appeal have been waived or exhausted. If such*
249 *adjustment is resolved by an agreement that is required to be signed by the Internal Revenue Service*
250 *and a partnership or partner, the final determination date is the date on which the last party signed the*
251 *agreement.*

252 *B. If a federal adjustment results from the filing of an amended federal return, a federal refund*
253 *claim, or an administrative adjustment request, or if such adjustment is reported on an amended federal*
254 *return or other similar report filed pursuant to § 6225(c) of the Internal Revenue Code, the final*
255 *determination date is the day on which the amended return, refund claim, administrative adjustment*
256 *request, or other similar report was filed.*

257 **2. That the Department of Taxation shall develop guidelines implementing the provisions of this**
258 **act. Such guidelines shall be exempt from the provisions of the Administrative Process Act**
259 **(§ 2.2-4000 et seq.).**