

Rulings of the Tax Commissioner

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Tax Type: Income Tax
Brief Description: Pass-Through Entities
Topics: Pass-Through Entities; Penalties; Persons Subject to Tax
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April 2, 2014

Re: Request for Ruling: Pass-Through Entity Income Tax

Dear *****:

This will reply to your letter in which you request a ruling as to the income tax filing requirements of your client, ***** (the "Taxpayer").

FACTS

The Taxpayer, a ***** (State A) limited liability company, provides engineering services to clients in Virginia. The majority of the Taxpayer's work is performed at its main office in State A, but the Taxpayer occasionally makes site visits to Virginia. The Taxpayer has no property or payroll in Virginia. In addition, the Taxpayer would have no sales attributable to Virginia because more than 50% of the costs for providing services to Virginia customers are incurred in State A. As such, the Taxpayer has no Virginia source income.

The Taxpayer requests a ruling as to whether it is considered to be doing business in Virginia and, thus, required to file pass-through entity income tax returns. The Taxpayer also asks whether there is an income threshold for the filing of returns by pass-through entities and their owners. In addition, the Taxpayer asks whether penalties would apply if it has failed to file any required returns.

RULING

Filing Requirement

Under *Va. Code* § 58.1-392, pass-through entities (including S corporations, partnerships and limited liability companies) doing business in Virginia or having income from Virginia sources are required to file a return with the Department. Pursuant to *Va. Code* § 58.1-302, an entity has income from Virginia sources if it has any items of income, gain, loss and deduction attributable to ownership in real or tangible personal property in Virginia or resulting from a business, trade,

profession or occupation carried on in Virginia.

Generally, a pass-through entity will have income from Virginia sources if there is sufficient business activity within Virginia to make any one or more of the applicable apportionment factors positive. Pass-through entities that have income from activity both within and without Virginia are required to compute their Virginia source income in accordance with the corporate statutory formula set forth in *Va. Code* §§ 58.1-408 through 58.1-421. As such, pass-through entities must allocate dividends to the state of commercial domicile and apportion all other income. Income is apportioned using a three-factor formula based on the property, payroll and sales within Virginia. See Public Document (P.D.) 88-165 (6/29/1988) and P.D. 07-150 (9/21/2007).

A pass-through entity that does not have a positive apportionment factor would not be required to file a return. See P.D. 06-114 (10/11/2006). Based on the facts presented, the Taxpayer would not have any Virginia source income and would not be required to file a return.

Filing Threshold

Virginia Code § 58.1-392 C grants the Department the authority to establish an income threshold for the filing of returns by pass-through entities and their owners. The Department, however, has never established such a threshold. Therefore, if a pass-through entity has any Virginia source income or loss in a given taxable year, it is required to file a return.

Penalty

Virginia Code § 58.1-394.1 imposes penalties on any pass-through entity that fails to file a required return. The penalty is \$200 for each month or portion thereof the return remains unfiled after the due date, up to six months total. If the return is not filed within six months, an additional penalty is assessed equal to six percent of the entity's Virginia taxable income, reduced by the penalty imposed for the first six months and any tax already paid by the owners of the pass-through entity on such income.

This ruling is based on the facts presented as summarized above. Any change in facts or the introduction of new facts may lead to a different result.

The *Code of Virginia* sections and public documents cited are available on-line at www.tax.virginia.gov in the Laws, Rules & Decisions section of the Department's web site. If you have any questions regarding this ruling, you may contact ***** in the Office of Tax Policy, Appeals and Rulings, at *****.

Sincerely,

Craig M. Burns
Tax Commissioner

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