

Income/Franchise:

Virginia: Pass-Throughs May Have to Withhold Tax on Nonresidents Whose Ownership Interests are Held by IRAs

Public Document No. 22-118, Va. Dept. of Tax. (7/21/22). Responding to an inquiry made by a pass-through entity taxpayer (PTE taxpayer) on whether it must withhold tax from a nonresident individual whose ownership interest in the PTE taxpayer is held by an Individual Retirement Account (IRA), the Virginia Department of Taxation (Department) held that the PTE taxpayer may have to withhold tax from the nonresident owner of the IRA if the IRA has either unrelated business taxable income (UBTI) or unrelated debt-financed income (UDFI) as determined under federal law. In doing so, the Department explained that pass-through entities are generally not required to withhold tax from nonresident owners that are exempt from federal and Virginia income tax; however, pursuant to Internal Revenue Code (IRC) section 408(e), while IRAs are *not* generally subject to federal income tax, they may be subject to income tax on UBTI. Moreover, the Department explained that a portion of any capital gains realized from a sale of real estate that was financed with debt may be reported as UDFI under IRC section 514, thus requiring the PTE taxpayer to withhold Virginia tax from the nonresident owner of the IRA if the IRA has UBTI or UDFI under federal law. Please contact us with any questions.

URL: <https://www.tax.virginia.gov/laws-rules-decisions/rulings-tax-commissioner/22-118>

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