



COMMONWEALTH of VIRGINIA

Department of Taxation

July 28, 2010

To: Craig M. Burns
Acting Tax Commissioner

Through: William J. White
Assistant Commissioner for Tax Policy

From: Mark C. Haskins
Director, Policy Development Division

Re: Statute of Limitations for Income Taxes and Refund Match Situations

The Policy Development Division ("Policy") has received several inquiries regarding the statute of limitations for various tax types and actions undertaken by the Department of Taxation ("TAX") or the taxpayer. As the statute of limitations for the withholding tax was discussed in an earlier memorandum dated May 1, 2009, this memorandum will describe the applicable statute of limitations for the income taxes and for refund match situations.

Income Tax

Because of recent changes in the law regarding extensions to file pass-through entity and individual, fiduciary, and corporate income tax returns, there has been some confusion regarding the applicable statute of limitations in terms of allowing taxpayers to file amended income tax returns or to receive refunds. In addition, there is some confusion regarding the time limitations for TAX to issue assessments for these tax types.

Prior to 2005, income taxpayers were required to request an extension to file their income tax returns. The maximum extension of time was six months from the due date of the return. Taxpayers could request the automatic four-month Virginia extension if they had chosen the automatic extension of time to file their federal returns; or they could request a Virginia extension which ended no later than six months from the original due date of their returns. Thus, the "last day for the timely filing" of a return for taxable years before 2005 will vary depending on whether or not a taxpayer requested and received an extension and, if so, whether the return was filed during the extension period.



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Effective for taxable years beginning on and after January 1, 2005, taxpayers are allowed to elect to take a six month extension to file their returns. In order to elect an extension, the taxpayer must (i) file the return within the extended period, and (ii) on or before the original due date for the filing of the return, pay the full amount properly estimated as the balance of the tax due for the taxable year. See *Va. Code* §§ 58.1-344, 58.1-393.1, and 58.1-453. If the taxpayer intends to take the extension but then does not file a return or pay the full amount of the tax due by the extended due date, the taxpayer is treated as if no extension had been granted. As a result, the "last day for the timely filing" of a return will vary depending on whether or not a taxpayer a taxpayer filed a return during the extension period.

Assessments

For the purposes of the income tax, an assessment may be made at any time if no return has been filed. See *Va. Code* § 58.1-312. When a return has been filed on or before the original due date, an assessment must be made within three years of the original due date. If a return has been filed on or before the extended due date, whether such extension was granted by TAX or automatically, an assessment must be made within three years of the extended due date. This is because, under *Va. Code* § 58.1-1812, returns filed before "the last day prescribed by law for the timely filing thereof shall be considered as filed on the last day." Finally, when a return has been filed after the extended due date, TAX has three years after the submitted date of the return to make an assessment. See *Va. Code* § 58.1-1812.

Refund/Amended Returns

Taxpayers who do not file a return have three years from the original due date to file a return requesting a refund. See *Va. Code* § 58.1-499. When a return has been filed on or before an original or extended due date, whether such extension was granted by TAX or automatically, an amended return must be filed within three years of the original or extended due date, as applicable. See *Va. Code* § 58.1-1823.

Finally, when an original return has been filed after the due date, whether original or extended, the taxpayer has from three years after the original due date to file an amended return. This is because, under the provisions of *Va. Code* § 58.1-499 (D), an original return and, under *Va. Code* § 58.1-1823, an amended return must be filed within three years from the last day prescribed by law for the timely filing of a return. If a

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return is not filed within an extension period, the extension is negated and the last day allowed for the timely filing of the return reverts to the original due date.

Attached below are two charts presenting various scenarios for the filing of income tax returns and the applicable statute of limitations for each one. For the purposes of the chart, the individual income tax is used as an example. The first chart applies to returns for taxable years prior to 2005, while the second chart is applicable to taxable years beginning on and after January 1, 2005.

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Returns for Taxable Years Prior to 2005
(Extensions, If Any, Must Have Been Requested)

| Return Type | Scenario | SOL to Receive Refund/Amend Return | SOL for TAX to Issue Assessment |
|--------------------|---|--|--|
| Original | The due date to file the original return is May 1. No extension requested. The taxpayer does not file. | The taxpayer has until three years from the original May 1 due date to file the original return before the SOL expires. See § 58.1-499. | If taxpayer does not file a return, there is no SOL. See § 58.1-312. |
| Amended | The original return was due May 1 and filed by the May 1 due date. | The taxpayer has until May 1, three years from the original due date to file an amended return before the SOL expires. See § 58.1-1823. | TAX has until May 1, three years from the original due date to issue an assessment. See § 58.1-1812 |
| Amended | The original return was due May 1 and filed within a requested and approved 6-month extension period. | Because, under § 58.1-1823, the taxpayer has from last day prescribed by law to file an amended return, he would have until three years from the end of the extension, i.e. until November 1, to file an amended return. | A return filed before the last day prescribed by law is treated as being filed on the last day under § 58.1-1812. Therefore, TAX would have three years from the end of the extension, i.e. until November 1, to bill. |
| Amended | The original return was due May 1 and filed after the due date and after the approved 6-month extension period. | The taxpayer has until three years from the original May 1 due date to file an amended return before the SOL expires. The extension is void because the return was filed after it ended. | Under § 58.1-1812, TAX has until three years from the submitted date of the original return to issue an assessment. |

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Returns for Taxable Year 2005 and Beyond
(Automatic, "Paperless" Extensions)

| Return Type | Scenario | SOL to Receive Refund/Amend Return | SOL for TAX to Issue Assessment |
|--------------------|--|---|---|
| Original | The due date to file the original return was May 1. The 6-month automatic extension applies. The taxpayer does not file. | If the taxpayer never files a return, the extension is void and he has to file within three years of May 1. | If taxpayer never filed, there is no SOL. |
| Amended | The original return was due May 1 and filed by the May 1 due date. | The taxpayer has until three years from the original May 1 due date to file an amended return before the SOL expires. | TAX has until three years from the original May 1 due date to issue an assessment. |
| Amended | The original return was due May 1 and filed within the automatic extension period. | The taxpayer has three years from November 1 to file amended return. He elected to take the extension, so the November 1 date is the last day prescribed by law for filing the return. | TAX has three years from last day prescribed by law to file the return to bill the taxpayer. As taxpayer elected to take the extension, TAX has until November 1 to bill. |
| Amended | The original return was due May 1 and filed after the automatic extension period. | The taxpayer has until three years after the original May 1 due date to file an amended return before the SOL expires. The extended due date is void because the original return was not filed within the extension period. | TAX has three years after the submitted date to issue an assessment. |

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Refund Match

Policy has also been questioned regarding the statute of limitations for situations in which a refund has been applied to an outstanding assessment and the assessment is later reduced or abated. In such situations, TAX must first determine whether or not the refund return was timely filed. If not, no refund may be issued to the taxpayer regardless of the timing of the assessment reduction or abatement. If the refund return was timely filed, TAX must then refer to the two-year statute of limitations related to bill payments that is provided in *Va. Code* § 58.1-1823. Consider the following examples:

Example 1: Taxpayer A files a 2004 income tax return on May 15, 2007. Although the return is late, it is filed within three years of the due date, so TAX could issue a refund.

On November 10, 2007, TAX applies the 2004 refund of \$3,500 to an outstanding nonfiler bill for 2002.

On June 17, 2008, Taxpayer A provides information that allows TAX to abate the 2002 assessment.

RESULT: Because Taxpayer A provided information allowing for the abatement of the assessment within two years of the refund match, the refund may be released to Taxpayer A.

Example 2: Taxpayer B files a 2006 income tax return on May 1, 2007. The return is timely filed.

On July 25, 2007, TAX applies the 2006 refund of \$5,000 to an outstanding bill for 2005.

On February 10, 2010, Taxpayer B provides information that allows TAX to abate the 2005 assessment.

RESULT: Because Taxpayer B did not provide information allowing for the abatement of the assessment within two years of the refund match, the refund may not be released to Taxpayer B. This is true even though the information was provided within three years of the timely filing of the 2006 return.

Example 3: Taxpayer C files a 2004 income tax return on May 15, 2007. Although the return is late, it is filed within three years of the due date, so TAX could issue a refund.

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On November 10, 2007, TAX applies the 2004 refund of \$3,500 to an outstanding nonfiler bill for 2002.

On June 17, 2008, Taxpayer C files an amended return for 2002 that shows that the assessment should be abated and that the taxpayer should have received a \$500 refund for that taxable year.

RESULT: Because the amended return for 2002 allows TAX to abate the assessment within two years of the refund match, TAX may refund the \$3,500 to Taxpayer C. However, the additional \$500 refund from 2002 may not be paid to the taxpayer. While the amended return was filed within two years of the payment as required by *Va. Code* § 1823, the refund amount may not exceed the amount of the payment. Therefore, Taxpayer C may only receive \$3,500.

Approved:

A handwritten signature in black ink, appearing to read 'CMB', is written over a solid horizontal line.

Craig M. Burns
Acting Tax Commissioner

CMB/ams