

DRAFT FORM — NOT FOR FILING

This draft form has been updated to include the most recent changes effective for Tax Year 2026 Virginia returns. If legislative changes or issues arise, we will post a new version of this draft form.

Please continue to monitor tax.virginia.gov/early-release-forms for future drafts of this form. Once forms are final, we will post them on our website at tax.virginia.gov/forms.

Instructions for Forms 502FED-1 and 502FED-2

Virginia Partnership-Level Federal Adjustments Reports

General Information

Effective on and after July 1, 2020, Virginia procedures have been updated for reporting certain partnership adjustments to the Department of Taxation (the Department) that result from federal tax changes and other changes to federal taxable income. The updated procedures require partnerships to report federal adjustments to the Department within 90 days after the federal determination date (“the 90-day requirement”). Payments associated with the adjustments must be submitted within 1 year of the final determination date.

There are two ways to report adjustments and pay the tax due. The Virginia default “push-out” method requires that the adjustments pass through to the partnership’s owners. Virginia also allows partnerships to elect an alternative “partnership pays” method in which the partnership agrees to pay the amount of additional tax, penalty, and interest that results from partnership-level federal adjustments in lieu of requiring the partners to file amended Virginia returns and pay the additional amount due.

Partnerships with 100 or fewer partners that have validly opted out of the federal audit rules under the Bipartisan Budget Act of 2015 (opting out partnerships) are exempt from these partnership-level reporting requirements. However, please note that partner-level reporting may still be necessary. Partners of opting out partnerships should review information at www.tax.virginia.gov regarding amending their return to report federal changes.

Definitions

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

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

Direct – with respect to a partner, that such partner holds a direct interest in a partnership or a pass-through entity and that such interest is not held indirectly through another partnership or pass-through entity.

Federal adjustment – 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.

Final determination date –

- If the federal adjustment arises from an IRS audit or other action by the IRS, the final determination date is defined as the first day on which no federal adjustments arising from that audit or other action remain to be finally determined, whether by IRS decision with respect to which all rights of appeal have been waived or exhausted, by agreement, or, if appealed or contested, by a final decision with respect to which all rights of appeal have been waived or exhausted. For agreements required to be signed by the IRS and the taxpayer, the final determination date is defined as the date on which the last party signed the agreement.
- For federal adjustments arising from an IRS audit or other action by the IRS, if the taxpayer filed as a member of a Virginia combined or consolidated return, the final determination date is defined as the first day on which no related federal adjustments arising from that audit remain to be finally determined for the entire group.
- If the federal adjustment results from filing an amended federal return, a federal refund claim, or an administrative adjustment request or if it is a federal adjustment reported on an amended federal return or other similar report, the final determination date is defined as the day on which the amended return, refund claim, administrative adjustment request, or other similar report was filed.

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

Partnership-level audit – 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.

Reviewed year – the taxable year of a partnership that is subject to a partnership-level audit from which federal adjustments arise.

State partnership representative – the person identified as the representative of a partnership pursuant to the provisions of Va. Code § 58.1-398:

- The state partnership representative has the sole authority to act on behalf of a partnership. The actions of the state partnership representative shall be binding on the direct partners and indirect partners of the partnership.
- The state partnership representative for a reviewed year is the partnership’s federal partnership representative unless the partnership designates in writing another person as its state partnership representative.

Partnership-Level Reporting Forms

Form 502FED-1

Form 502FED-1 is used to report partnership-level federal adjustments. This report is due within 90 days after the IRS final determination date. Partnerships must file this form regardless of the reporting method or payment election.

Form 502FED-2

Form 502FED-2 is used by a partnership that is electing to pay any additional income tax, penalties, and interest on behalf of its partners in lieu of requiring partners to file amended returns. This election must be made within the 90-day requirement in order to be valid. Check the box on the top of Form 502FED-2 to indicate the partnership is making this election.

Reporting and Paying Tax

Default Method — Push Out

Under the default push-out method, a partnership passes the federal adjustments through to the owners. The partnership is only required to report federal adjustments to the Department and direct partners under the 90-day requirement. The obligation to pay generally remains with the partners. However, the partnership is required to make nonresident withholding payments and, if a Form 765 was filed, composite return income tax payments associated with the federal adjustments.

Partnership Responsibilities

Within **90 days** of the final determination date, the partnership must:

- File Form 502FED-1.
- File an amended Form 502 along with all associated forms and schedules.
- Pay any additional withholding tax due.
- Send a copy of the Form 502FED-1 along with amended federal Schedules K-1 and Schedules VK-1 to each partner. See the Form 502 Instructions for more information on completing the amended return.

Note: The requirement to provide amended Schedules K-1 to partners applies, even if they were not required to provide amended Schedules K-1 to their partners at the federal level.

- File an amended Form 765 and pay any additional income tax due. (Only applicable if the partnership had previously filed a Form 765 on behalf of nonresident owners.)

Partner Responsibilities

Within **1 year** of the final determination date, the owner(s) must:

- File an amended return along with a copy of the 502FED-1 received from its partnership.

- Pay any tax resulting from the partner's distributive share of partnership-level federal adjustments.

Partnership Pays Election

A partnership may elect to pay Virginia income tax, interest, and penalties attributable to any partnership-level adjustments in lieu of requiring the partners to do so. An amended return is not required for a partnership or any of its partners where the partnership selects the "election to pay" option in Form 502FED-2.

Partnership Responsibilities

Within **90 days** of the final determination date, the partnership must:

- File Form 502FED-1.
- File Form 502FED-2 to summarize the partnership-level adjustments. If the partnership fails to indicate on the Form 502FED-2 that it is electing to pay any income tax due on behalf of its partners, or the Form 502FED-2 is not filed within 90 days of the final determination date, the election is invalid and such partnership must use the default method to report and pass the adjustments through to its partners.

Within **1 year** of the final determination date, the partnership must:

- Pay any tax, interest, or penalties that result from the adjustments to Virginia taxable income.

Partner Responsibilities

The partners are not required to take any action if the partnership elects to file and pay at the entity level and the partnership actually pays the full amount due at the entity level. They do not need to file an amended Virginia return.

Modified Reporting

A partnership may request to use a modified reporting and payment method by writing to the Department within 90 days of the final determination date.

All requests must be submitted in writing to:

**Virginia Department of Taxation
Office of Compliance
P.O. Box 5771
Richmond, Virginia 23220-0771**

The partnership is required to indicate in its request whether, in the event its request is denied, it would like to make a partnership pays election. If the partnership would like to make a partnership pays election in the event that its request is denied but does not indicate so in its request, the partnership must submit a letter in writing to the address above within 90 days of the final determination date indicating this. Before using a modified method to calculate the amount due, the partnership must receive approval from the Department.

Filing Information

Due Dates

Form 502FED-1 Due Date

The partnership must notify the Department of the partnership-level adjustments within 90 days of the IRS final determination date by filing Form 502FED-1.

Form 502FED-2 Due Date

If a partnership elects to pay any additional tax on behalf of its partners, it must complete Form 502FED-2 within 90 days of the IRS final determination date in lieu of submitting an amended return along with all associated filings and payments.

Amended Return Due Date

Amended returns are due only under the default push-out method.

Partnership Responsibilities

Under the default push-out method, partnerships must file an amended Form 502 and Form 765, if applicable, along with all associated forms and schedules, including updated Schedules VK-1, within 90 days of the final determination date.

Partner Responsibilities

Under the default push-out method, partners must file the appropriate amended return, and pay any tax due, within 1 year of the final determination date. The Form 502FED-1 and amended Schedule VK-1 must be submitted with the partner's amended return.

Payment Due Date

Payments, whether they are made on the level of the partner or the partnership, are due within 1 year of the IRS final determination date.

Penalties and Interest

Late File

- **A partnership** that fails to report federal adjustments within 90 days of the final determination date is subject to a penalty of \$200 per month (or fraction of a month) that the partnership is late. If the partnership is more than 6 months late, the penalty is the greater of \$1,200 or 6% of the amount by which the partnership's Virginia taxable income is required to be adjusted.
- **A partner** that fails to report federal adjustments within 1 year of the final determination date is subject to a penalty of \$200 per month (or fraction of a month) that the partner is late. If the partner is more than 6 months late, the penalty is the greater of \$1,200 or 6% of the amount by which the partner's Virginia taxable income is required to be adjusted.

Late Payment

The failure to pay penalty for electing partnerships is 6% of the elective payment amount for each month or fraction thereof from the date the Form 502 for the reviewed taxable year originally was due until paid, not exceeding 30% in the aggregate.

In addition to the 6% late payment penalty, if the understatement is false or fraudulent with intent to evade the tax, a penalty of 100% of the elective payment from the date the Form 502 for the reviewed taxable year originally was due until paid.

If Form 502 was made in good faith and the understatement of the amount in the return was not due to any fault of the electing partnership, then no penalty is due as long as payment is made within one year of the final determination date. A partnership that selects the "election to pay" method and fails to pay within 1 year of the final determination date is subject to a penalty of 6% per month, up to a maximum of 30% of the elective payment due but left unpaid.

Interest

Interest is due on any unpaid tax at the underpayment rate under IRC § 6621, plus 2%, from the due date until the tax is paid.

Electronic Payments

To make payments electronically, use the eForms application on the Department's website, www.tax.virginia.gov. Select Form 502V from the eForms list and complete the form and payment information online.

A PTE may also make its tax payments using an ACH credit transaction through its bank. Some banks may charge a fee for this service. For information on how to submit ACH credit payments to the Department, see the Electronic Payment Guide available at www.tax.virginia.gov.

Where to File

Form 502FED-1 Filing Information

Form 502FED-1 must be filed as a PDF attachment to the electronically-filed amended Form 502.

Form 502FED-2 Filing Information

Submit Form 502FED-2 to the following address:

**Virginia Department of Taxation
Office of Compliance
P.O. Box 5771
Richmond, Virginia 23220-0771**

Where to Get Help

- Visit our website at www.tax.virginia.gov.
- Write to the Department of Taxation at:
Virginia Department of Taxation
P.O. Box 1115
Richmond, VA 23218-1115
- Call us at (804) 367-8037.
- Fax us at (804) 254-6111.

Form 502FED-1 Instructions

All taxpayers must complete the Taxpayer Information Section and Section I – Summary of Partnership-Level Income and Adjustments. Only taxpayers who apportion their income must complete Section II – Partnership-Level Adjusted Virginia Apportionment.

Taxpayer Information Section

Complete all fields in this section.

State partnership representative information – The state partnership representative has the sole authority to act on behalf of a partnership.

Enter the name and contact information of the partnership's state partnership representative. Such person must meet the qualifications required by the IRS to be a federal partnership representative. If no state partnership representative is designated, the state partnership representative will automatically be the partnership's federal partnership representative.

The actions of the state partnership representative shall be binding on the direct partners and indirect partners of the partnership. See the Definitions section above for more information about the state partnership representative.

Final Federal Determination Date – enter the date on which the federal determination became final. See the Definitions section above for more information about the final determination date.

Taxable Year of Federal Adjustment – enter the year that is subject to a partnership-level audit from which federal adjustments arise.

Section I – Summary of Partnership-Level Adjustments

All filers must complete this section to summarize the changes between the original Form 502 and the adjusted amounts.

Enter the figures from the original Form 502 in Column A. Enter the net changes arising from the federal partnership audit in Column B. In Column C, enter the corrected amounts.

When referring to the Form 502, use this chart to transfer amounts to the corresponding line on the Form 502FED-1:

Line Description	Form 502FED-1	Form 502, Page 1
Total taxable income	Line 1	Line 1
Total deductions	Line 2	Line 2
Tax-exempt interest income	Line 3	Line 3
Total Virginia additions	Line 4	Line 13
Total Virginia subtractions	Line 5	Line 18
Income allocated to Virginia	Line 6	Line 4
Apportionable income	Line 7	Line 6
Income allocated outside of Virginia	Line 8	Line 5
Virginia apportionment percentage	Line 9	Line 7
Total nonrefundable credits	Line 10	Line 19
Total refundable credits	Line 11	Line 20

See the Form 502 Instructions for more information about each line.

Section II – Partnership-Level Adjusted Virginia Apportionment

Complete this section if the partnership's income is derived from sources both within and without Virginia. This section only needs to be completed by companies that must apportion their income to Virginia.

The lines on the Form 502FED-1 correspond to Schedule 502A, Section B – Apportionment Percentage. See the instructions for Schedule 502A for more information about apportionment factors and calculations.

Form 502FED-2 Instructions Partnership Pays Election Computation

Use Form 502FED-2 if the audited partnership is electing to pay additional tax, penalties, and interest at the partnership level. This form is used to calculate amounts due on partnership-level adjustments attributable to partners that the partnership is paying on their behalf.

Important Information Regarding the Election to Pay on the Partnership Level

Any audited partnership who wants to report adjustments and pay tax on the partnership level must check the box at the top of the page to consent to the election. If this box is not checked, the election will be invalid and tax must be calculated and paid using the default method of reporting (push-out method).

Additionally, if this form is not filed within 90 days of the final determination date, the election to pay on the partnership level will be invalid. The partnership will be required to report and pay taxes using the default method.

If a partnership makes a partnership pays election, such election is irrevocable by the partnership, and all partners

of the partnership must be included on the report, including those that were originally included in a composite return.

Section I – Calculation of Adjusted Taxable Income

Complete only the lines that apply to the type(s) of partners included in the partnership-level federal adjustments report.

Change in Virginia Taxable Income Allocated to Virginia: Line 1

Transfer the amount of net change from Form 502FED-1, Line 6, Column B.

Resident Direct Partners: Lines 2-4

Complete these lines if the electing partnership has Virginia resident direct partners (individuals, estates, and trusts). Enter the resident direct partners' distributive share of adjustments on Line 3. On Line 4, multiply the amount on Line 3 by the 5.75% individual income tax rate to calculate the tax owed on direct partners' distributive shares.

Nonresident Direct Partners: Lines 5-8

Complete these lines if the electing partnership has nonresident direct partners (individuals, estates, and trusts). A nonresident partner is any individual, estate, or trust partner that is not a resident partner. The allocation and apportionment is a partnership-level computation.

On Line 6, enter the nonresident direct partners' distributive share of adjustments and on Line 7, enter the amount of distributive shares that are sourced to Virginia. Multiply the amount on Line 7 by the 5.75% individual income tax rate and enter this amount on Line 8. This is the tax owed on nonresident direct partners' shares.

Corporation and Tax-Exempt Partners: Lines 9-12

Complete these lines if the electing partnership has direct corporate or tax-exempt partners.

A "tax-exempt partner" is a partner exempt from Virginia income taxation. If such partner has unrelated business taxable income but otherwise is exempt from Virginia income taxation, such partner will be considered a "tax-exempt partner." For the portion of federal adjustments that are to unrelated business income or other taxable income to which a tax-exempt partner would be subject to tax under *Va. Code* § 58.1-400, the elective payment amount is the distributive share of such adjustments that are apportioned or allocated to Virginia.

On Line 10, enter the corporate or tax-exempt partners' distributive share of adjustments. On Line 11, enter the corporate or tax-exempt partners' shares that are apportioned or allocated to Virginia. Multiply this amount by the 6% corporate tax rate and enter the result on Line 12. This is the tax owed on corporate or tax-exempt partners' shares.

Tiered Partners: Lines 13-18

Complete these lines if the electing partnership has partners that are themselves partnerships (tiered partners). Enter the tiered partners' distributive share of adjustments on Line 14. On Line 15, enter the amount of distributive shares that are not sourced to Virginia.

For most electing partnerships, Line 16 will be zero. However, if your electing partnership is properly using an alternative method of apportionment or is considered an investment pass-through entity under Public Document 15-240, you may have adjustments included on Line 14 that are of a type that would not be subject to sourcing in Virginia. If so, you can exclude such adjustments when computing tax owed on tiered partner distributive shares if you can show that they are:

- Allocable to a nonresident indirect partner,
- Allocable to a partner that is not subject to tax on such amount,
- Excludable under procedures for alternative reporting and payment as specified in *Va. Code* § 58.1-399.3.

Enter these excluded distributive shares, if any, on Lines 16. If you enter any amount other than zero on Line 16, you must submit documentation with the Form 502FED-2 to establish that you are entitled to exclude such distributive shares. Documentation can include a copy of a resident tax return filed by the nonresident indirect partner in another state and, if filed, a copy of a nonresident tax return filed by the nonresident indirect partner in Virginia. Note that any amount included on Line 15 may not also be included on Line 16.

On Line 17, enter the net tiered partner distributive shares. Calculate the net tiered partner distributive share by subtracting Lines 15 and 16 from Line 14. Multiply the net distributive shares on Line 17 by the 5.75% individual income tax rate and enter the result on Line 18. This is the tax owed on tiered partners' distributive shares.

Section II – Tax, Penalty, and Interest Calculation

The amount of tax, penalty, and interest calculated in this section must be paid by the partnership within one year of the IRS final determination date. The payment of tax by the partnership is made in lieu of taxes owed by the partners included in the federal adjustment report.

Line 19: Total Virginia Tax Due

The total amount of tax due is the sum of the tax owed on Virginia distributive shares of all partners included in the federal adjustments report. Add the amounts on 4, 8, 12, and 18 to calculate the tax owed by the partnership on behalf of the partners.

Line 20: Penalty

Refer to the "Penalty and Interest" section above to determine whether you owe a Late File or Late Pay penalty. Enter the penalty amount on this line.

The failure to pay penalty for electing partnerships is 6% of the elective payment amount for each month or fraction

thereof from the date the Form 502 for the reviewed taxable year originally was due until paid, not exceeding 30% in the aggregate. In addition, if the understatement is false or fraudulent with intent to evade the tax, a penalty of 100% of the elective payment from the date the Form 502 for the reviewed taxable year originally was due until paid. Enter the sum of the failure to pay penalty and, if applicable, the 100% penalty, on this line.

However, if the Form 502 was made in good faith and the understatement of the amount in the return was not due to any fault of the electing partnership, enter zero on this line. Note that even if zero is properly entered on this line, if the full amount of elective payment reported on this form is not made within 1 year of the final determination date, the Department will assess such partnership with a penalty of 6% of the unpaid amount per month from the date that is one year from the final determination date until paid, not exceeding 30% in the aggregate.

Line 21: Interest

Interest on the elective payment begins accruing from the date the original Form 502 was due until the date the tax is paid. If you are submitting payment with the Form 502FED-2, enter the amount of interest on this line. If you are paying at a later date, leave this line blank and submit payment, with interest, using the electronically filed Form 502V within the one year payment due date.

Line 22: Total Amount Due from Partnership

Add Lines 19-21 to compute the amount of tax, penalty, and interest owed by the partnership and enter the result on Line 22. This is the amount of the elective payment due from the partnership. See the "Electronic Payments" section above for instructions on how to submit payments.

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