

Letter of Findings: 07-0212P
Withholding Tax
For the Tax Year Ending December 31, 2003

NOTICE: Under IC § 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of the document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Withholding Tax - Twenty Percent Penalty

Authority: IC § 2-5-3-1; IC § 6-3-2-2.8; IC § 6-3-4-13; IC § 6-8.1-5-1; IC § 6-8.1-10-2.1; [45 IAC 15-11-2](#).

Taxpayer seeks abatement of the twenty percent penalty for failure to file Form WH-1 and remit withholding tax on non-resident shareholders.

STATEMENT OF FACTS

Taxpayer is an S-Corporation. Taxpayer failed to file Form WH-1s and withhold tax on its non-resident shareholders for the year ending December 31, 2003. Taxpayer was assessed a twenty percent penalty pursuant to IC § 6-8.1-10-2.1(h).

I. Withholding Tax - Twenty Percent Penalty

DISCUSSION

Taxpayer believes that it is entitled to abatement of the twenty percent penalty for failure to file Form WH-1 and remit withholding tax on its non-resident shareholders.

Taxpayer claims to have paid the withholding tax by including the withholding payment with its corporate return. However, taxpayer did not file a composite return or pay the withholding for the non-resident shareholders upon filing the corporate return. Taxpayer states that its tax preparation service did not completely understand the withholding requirement and has since corrected its practices acting in compliance.

Pursuant to IC § 6-3-2-2.8(2):

Notwithstanding any provision of [IC 6-3-1](#) through [IC 6-3-7](#), there shall be no tax on the adjusted gross income of the following:

- (2) Any corporation which is exempt from income tax under Section 1363 of the Internal Revenue Code and which complies with the requirements of [IC 6-3-4-13](#). However, income of a corporation described under this subdivision that is subject to income tax under the Internal Revenue Code is subject to the tax under [IC 6-3-1](#) through [IC 6-3-7](#). A corporation will not lose its exemption under this section because it fails to comply with [IC 6-3-4-13](#) but it will be subject to the penalties provided by [IC 6-8.1-10](#).

According to IC § 6-3-4-13(a)-(j), in relevant part:

(a) Every corporation which is exempt from tax under [IC 6-3](#) pursuant to [IC 6-3-2-2.8\(2\)](#) shall, at the time that it pays or credits amounts to any of its nonresident shareholders as dividends or as their share of the corporation's undistributed taxable income, withhold the amount prescribed by the department. Such corporation so paying or crediting any nonresident shareholder:

- (1) shall be liable to the state of Indiana for the payment of the tax required to be withheld under this section and shall not be liable to such shareholder for the amount withheld and paid over in compliance or intended compliance with this section; and
- (2) when the aggregate amount due under [IC 6-3](#) and [IC 6-3.5](#) exceeds one hundred fifty dollars (\$150) per quarter, then such corporation shall make return and payment to the department quarterly, on such dates and in such manner as the department shall prescribe, of the amount of tax which, under [IC 6-3](#) and [IC 6-3.5](#), it is required to withhold.

(b) Every corporation shall, at the time of each payment made by it to the department pursuant to this section, deliver to the department a return upon such form as shall be prescribed by the department showing the total amounts paid or credited to its nonresident shareholders, the amount withheld in accordance with the provisions of this section, and such other information as the department may require. Every corporation withholding as provided in this section shall furnish to its nonresident shareholders annually, but not later than the fifteenth day of the third month after the end of its taxable year, a record of the amount of tax withheld on behalf of such shareholders on forms to be prescribed by the department.

(c) All money withheld by a corporation, pursuant to this section, shall immediately upon being withheld be the money of the state of Indiana and every corporation which withholds any amount of money under the provisions of this section shall hold the same in trust for the state of Indiana and for payment thereof to the department in the manner and at the times provided in [IC 6-3](#). Any corporation may be required to post a surety bond in such sum as the department shall determine to be appropriate to protect the state of Indiana with respect to money withheld pursuant to this section.

(d) The provisions of [IC 6-8.1](#) relating to additions to tax in case of delinquency and penalties shall apply to

corporations subject to the provisions of this section, and for these purposes any amount withheld, or required to be withheld and remitted to the department under this section, shall be considered to be the tax of the corporation, and with respect to such amount it shall be considered the taxpayer.

...

(i) If a corporation fails to withhold and pay any amount of tax required to be withheld under this section and thereafter the tax is paid by the shareholders, such amount of tax as paid by the shareholders shall not be collected from the corporation but it shall not be relieved from liability for interest or penalty otherwise due in respect to such failure to withhold under [IC 6-8.1-10](#).

(j) A corporation described in subsection (a) may file a composite adjusted gross income tax return on behalf of some or all nonresident shareholders if it complies with the requirements prescribed by the department for filing a composite return.

(Emphasis added).

IC § 6-8.1-10-2.1(d)-(h), in relevant part, provides:

(d) If a person subject to the penalty imposed under this section can show that the failure to file a return, pay the full amount of tax shown on the person's return, timely remit tax held in trust, or pay the deficiency determined by the department was due to reasonable cause and not due to willful neglect, the department shall waive the penalty.

(e) A person who wishes to avoid the penalty imposed under this section must make an affirmative showing of all facts alleged as a reasonable cause for the person's failure to file the return, pay the amount of tax shown on the person's return, pay the deficiency, or timely remit tax held in trust, in a written statement containing a declaration that the statement is made under penalty of perjury. The statement must be filed with the return or payment within the time prescribed for protesting departmental assessments. A taxpayer may also avoid the penalty imposed under this section by obtaining a ruling from the department before the end of a particular tax period on the amount of tax due for that tax period.

(f) The department shall adopt rules under [IC 4-22-2](#) to prescribe the circumstances that constitute reasonable cause and negligence for purposes of this section.

...

(h) A corporation which otherwise qualifies under [IC 6-3-2-2.8\(2\)](#) but fails to withhold and pay any amount of tax required to be withheld under [IC 6-3-4-13](#) shall pay a penalty equal to twenty percent (20 [percent]) of the amount of tax required to be withheld under [IC 6-3-4-13](#). This penalty shall be in addition to any penalty imposed by section 6 of this chapter.

(Emphasis added).

Under IC § 6-8.1-5-1(b), "The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." An assessment – including the negligence penalty – is presumptively valid.

Departmental regulation [45 IAC 15-11-2\(b\)](#) defines negligence as "the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer." Negligence is to "be determined on a case-by-case basis according to the facts and circumstances of each taxpayer." *Id.*

IC § 6-8.1-10-2.1(d) allows the Department to waive the penalty upon a showing that the failure to pay the deficiency was based on "reasonable cause and not due to willful neglect." Departmental regulation [45 IAC 15-11-2\(c\)](#) requires that in order to establish "reasonable cause," the taxpayer must demonstrate that it "exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed...."

Pursuant to IC § 2-5-3-1:

It is hereby declared to be the policy of the general assembly of the state of Indiana to promote a revenue raising structure in Indiana that will provide adequate revenues to carry on the efficient operation of the state, county, and city governments and at the same time will assure that its burdens will be shared equitably by all taxpayers. It is further declared to be the policy of the general assembly of the state of Indiana to encourage and bring about the accomplishment of enforcement policies and administrative practices that will result in maximum return from existing taxes to the state of Indiana at a minimum cost to the taxpayers.

In imposing the twenty percent penalty for failure to file Form WH-1 and remit withholding tax on non-resident shareholders the Department is enforcing a provision of the Indiana Code in order to ensure the continued compliance with Indiana law. The requirement of filing a Form WH-1 and the withholding on taxpayer's non-resident shareholders is the state's way of ensuring that the Department is provided with information it needs to carry out its objectives in the most efficient manner. The withholding requirements imposed upon the taxpayer in this instance are more efficient than the unreasonably burdensome method of the Department trying to match non-resident shareholders to their respective S-Corporations in order to ensure that voluntary compliance with the Indiana tax laws has occurred.

Taxpayer has not provided substantive evidence in support of its protest.

FINDING

Taxpayer's protest is denied.

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