

Letter of Findings Number: 03-20100523
Withholding Tax
For Tax Years 2007-09

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ISSUES

I. Withholding Tax—Imposition.

Authority: IC § 6-8.1-5-1; [45 IAC 3.1-1-97](#); [45 IAC 3.1-1-102](#); Departmental Notice 1.

Taxpayer protests the imposition of withholding tax regarding specific employees.

II. Tax Administration—Negligence Penalty.

Authority: IC § 6-8.1-10-2.1; [45 IAC 15-11-2](#).

Taxpayer protests the imposition of a ten percent negligence penalty.

STATEMENT OF FACTS

Taxpayer is an Indiana corporation. As the result of an audit, the Indiana Department of Revenue ("Department") determined that Taxpayer had not withheld Indiana county income taxes on several employees for the tax years 2007, 2008, and 2009. The Department issued proposed assessments for county income tax, negligence penalty, and interest. Taxpayer protests the imposition of withholding tax on all except two of the employees who the Department included as subject to Indiana county income tax and also protests the imposition of penalty. An administrative hearing was held and this Letter of Findings results. Further facts will be supplied as required.

I. Withholding Tax—Imposition.

DISCUSSION

Taxpayer protests the imposition of Indiana county withholding tax on several employees. Taxpayer agrees that two of the employees included in the Department's calculations should have had county income tax withheld for 2008. Taxpayer withheld Indiana adjusted gross income tax for all employees but, since county income tax is imposed depending on the county of residence or employment as of January 1 for any particular tax year, did not withhold Indiana county income tax on all employees for all years. Taxpayer states that the remaining employees were out-of-state residents who were sent to jobs in Indiana after January 1, of the respective years, and that the withholding instructions listed on withholding form WH-4 state that an individual's county of residence or employment is determined on January 1 of the calendar year in which the individual's taxable year commences. Taxpayer believes that, since these employees did not start work until after January 1 of the respective years, then their counties of employment could not be determined for those years. The Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(c).

The Department refers to [45 IAC 3.1-1-97](#), which states in relevant part:

Employers who make payments of wages subject to the Adjusted Gross Income Tax Act, and who are required to withhold Federal taxes pursuant to the Internal Revenue Code (USC Title 26), are required to withhold from employees' wages Adjusted Gross and County Adjusted Gross Income Tax.

Also, [45 IAC 3.1-1-102](#) states:

The Employee's Withholding Exemption and County Residence Certificate (Form WH-4) must be refiled with the employer to show any change in residence or number of exemptions.

Change of Residence

All employees who change their county of residence or their county of principal work activity are required to file a new state Form WH-4 by January 1 of the following year.

Change in Exemptions

You may file a new WH-4 at any time if the number of your exemptions increase. You must file a new WH-4 within 10 days if the number of exemptions previously claimed by you decreases for any of the following reasons:

- (a) Your wife (or husband) for whom you have been claiming an exemption is divorced or legally separated, or claims her (or his) own exemption on a separate certificate.
- (b) The support of a dependent for whom you claim an exemption is taken over by someone else, so that you no longer expect to furnish more than half the support for the year.
- (c) You find that a dependent for whom you claim an exemption will receive \$750.00 or more of income of his own during the year.

Other decreases in exemptions such as the death of a spouse or a dependent, do not affect your withholding until the next year, but require the filing of a new WH-4 by December 1 of the year in which they occur.

(Emphasis added).

Also, the instructions included with Form WH-4 explain:

Enter your Indiana county of residence and county of principal employment as of January 1 of the current year. If you did not live of [sic] work in Indiana on January 1 of the current year, enter "not applicable" on the line(s). If you move to (or work in) another county after January 1, your county status will not change until the next calendar year.

Form WH-4 has lines to enter both the county of residence and the county of principal employment. Any individual's county of residence and/or principal employment is established on January 1 of the relevant year and is applicable throughout that year regardless of changes in residence or principal employment.

The Department determined that Taxpayer had several employees for whom Taxpayer had withheld Indiana state income tax, but did not withhold Indiana county income tax. The Department's audit workpapers listed Taxpayer's employees in each tax year at issue and indicated the state of residence and hire date where that information was available. Taxpayer was unable to provide specific work locations for all employees for all years.

The Department did not impose Indiana county income tax for the year in which an employee was hired after January 1 of that year. If an employee was hired after January 1, then the Department imposed county income tax for the following year(s). Indiana Departmental Notice 1 provides in relevant part:

The residence, principal place of business, or employment of an individual is determined on January 1 of the calendar year in which the individual's taxable year commences. An individual cannot be subject to both a resident rate and a nonresident rate at the same time. If a person resides in an adopting county on January 1, he or she is subject to that county's resident rate. If a person resides in a non-adopting county (including out-of-state), but works in an Indiana adopting county, he or she is subject to the nonresident rate corresponding to his or her county of principal employment.

Since Taxpayer was unable to provide documentation on the counties of its job site locations, and since the employees in question were out-of-state residents, the Department used the county income tax rate of Taxpayer's home Indiana county to determine the amounts of county income tax which should have been withheld. That particular county's resident and non-resident rates are identical.

Taxpayer protests that many of its employees reside in another state and that, due to the nature of its business, it did not know where those employees would be assigned when filling out the WH-4 forms for those employees. Also, Taxpayer states that these employees are paying withholding taxes in other states. As previously discussed, Taxpayer was not able to provide documentation regarding its employees' work locations or other income tax circumstances for these years.

Also as previously discussed, the burden of proving a proposed assessment wrong rests with the person against whom a proposed assessment is made, as provided by IC § 6-8.1-5-1(c). Also IC § 6-8.1-5-1(b) provides:

If the department reasonably believes that a person has not reported the proper amount of tax due, the department shall make a proposed assessment of the amount of the unpaid tax on the basis of the best information available to the department. The amount of the assessment is considered a tax payment not made by the due date and is subject to [IC 6-8.1-10](#) concerning the imposition of penalties and interest. The department shall send the person a notice of the proposed assessment through the United States mail.

In this case, the Department found employees with Indiana adjusted gross income taxes withheld, but without Indiana county income taxes withheld. It is reasonable for the Department to believe that those employees worked in an Indiana county and had Indiana county income tax due. It is the withholding agent's duty to withhold Indiana county income tax on wages paid to its employees, as provided by [45 IAC 3.1-1-97](#). While the proposed assessments may be proven incorrect, here Taxpayer has not provided documentation to prove the Department's proposed assessments incorrect, as required by IC § 6-8.1-5-1(c).

FINDING

Taxpayer's protest is denied.

II. Tax Administration–Negligence Penalty.

DISCUSSION

The Department issued proposed assessments and the ten percent negligence penalty for the tax years in question. Taxpayer protests the imposition of penalty. The Department refers to IC § 6-8.1-10-2.1(a), which states in relevant part:

If a person:

...

(3) incurs, upon examination by the department, a deficiency that is due to negligence;

...

the person is subject to a penalty.

The Department refers to [45 IAC 15-11-2\(b\)](#), which states:

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated

as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

[45 IAC 15-11-2](#)(c) provides in pertinent part:

The department shall waive the negligence penalty imposed under [IC 6-8.1-10-1](#) if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. 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 under this section.

In this case, Taxpayer incurred a deficiency which the Department determined was due to negligence under [45 IAC 15-11-2](#)(b), and so was subject to a penalty under IC § 6-8.1-10-2.1(a). While Taxpayer was denied on its protest in Issue I it has affirmatively established that its failure to withhold and remit the remaining deficiency was due to reasonable cause and not due to negligence, as required by [45 IAC 15-11-2](#)(c). The negligence penalty will be waived.

FINDING

Taxpayer's protest is sustained.

CONCLUSION

Taxpayer's protest is denied on Issue I regarding imposition of county withholding tax, as described in Issue I. Taxpayer's protest is sustained on Issue II regarding imposition of negligence penalties.

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An [html](#) version of this document.