

## DEPARTMENT OF STATE REVENUE

03-20140295P.LOF

**Letter of Findings Number: 03-20140295P**  
**Tax Administration**  
**For Tax Years 2010, 2011, and 2012**

**NOTICE:** IC §6-8.1-3-3.5 and IC § 4-22-7-7 require the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective as of its date of publication and remains in effect until the date it is superseded by the publication of another document in the Indiana Register.

**ISSUE****I. Tax Administration - Penalty.**

**Authority:** IC § 6-3-2-2.8; IC § 6-3-4-13; IC § 6-8.1-10-2.1; Income Tax Information Bulletin 72 (September 2007); Income Tax Information Bulletin 72 (May 2012); [45 IAC 15-11-2](#).

Taxpayer protests the imposition of a twenty percent penalty.

**STATEMENT OF FACTS**

Taxpayer is an Indiana S corporation selling software products. The Indiana Department of Revenue ("Department") conducted an audit and issued a proposed assessment for a twenty percent penalty based on Taxpayer's failure to withhold state income tax on nonresident shareholder's distributive share of income. Taxpayer protested the imposition of the penalty. An administrative hearing was held, and this Letter of Findings results. Further facts will be supplied as required.

**I. Tax Administration - Penalty.****DISCUSSION**

The Department issued a proposed assessment for a twenty percent penalty for each tax year based on Taxpayer's failure to withhold state income tax on nonresident shareholder's share of income. Taxpayer protested the imposition of the penalties.

IC § 6-3-4-13(a) requires corporations which are exempt from tax under IC § 6-3 pursuant to IC § 6-3-2-2.8(2) (i.e. S corporations) to "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." See Income Tax Information Bulletin 72 (September 2007), 20071003 Ind. Reg. 045070632NRA, Income Tax Information Bulletin 72 (May 2012), 20120627 Ind. Reg. 045120371NRA. If an S corporation fails to withhold pursuant to this section, it is subject to a "penalty equal to twenty percent (20[percent]) of the amount of tax required to be withheld under [IC 6-3-4-12](#), [IC 6-3-4-13](#), or [IC 6-3-4-15](#)." IC § 6-8.1-10-2.1(h). This is true even if the amount required to be withheld is paid by the nonresident shareholders. IC § 6-3-4-13(i) (stating that "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](#).").

The Department has the power to waive the penalty if the taxpayer demonstrates its failure to withhold "was due to reasonable cause and not due to willful neglect." IC § 6-8.1-10-2.1(d); see also [45 IAC 15-11-2](#). A taxpayer may demonstrate reasonable cause by showing affirmatively that it used "ordinary business care and prudence" in not paying the outstanding taxes. Whether a taxpayer demonstrates reasonable cause for penalty purposes is a fact-sensitive question and determined on a case-by-case basis. [45 IAC 15-11-2](#)(b) and (c).

In this case, Taxpayer has affirmatively established that it acted reasonably in its efforts to comply with Indiana's tax filing and payment requirements, as required by [45 IAC 15-11-2](#)(c). The penalty will be waived. However, the Department takes this opportunity to notify Taxpayer that it is now aware of its withholding tax obligations and that penalties shall be imposed if this scenario occurs again. Taxpayer's protest is sustained.

**FINDING**

Taxpayer's protest is denied.

*Posted: 10/29/2014 by Legislative Services Agency*  
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