

Letter of Findings: 03-20140647
Withholding Tax
For the Years 2011, 2012, and 2013

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 requires 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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

Employer improperly relied on a payroll service to adjust withholding taxes for out-of-state employees, therefore, the penalty is abated but the tax liability and interest were still due.

ISSUES

I. Withholding Tax-State and Non-Resident County Imposition.

Authority: IC § 6-3-4-8; IC § 6-3-4-13; IC § 6-8.1-5-1; IC § 6-8.1-7-1; Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); [45 IAC 3.1-1-97](#).

Taxpayer protests the assessment of withholding tax on wages it paid to its employees.

II. Tax Administration-Penalty and Interest.

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

STATEMENT OF FACTS

Taxpayer is a company operating in Indiana. Taxpayer employs out-of-state employees. Taxpayer's payroll service company did not properly advise Taxpayer on how to withhold for out-of-state employees for payroll taxes. The Indiana Department of Revenue ("Department") conducted an audit review of Taxpayer's business records and withholding tax returns for the 2011, 2012, and 2013 tax years. Taxpayer did not withhold Indiana state tax from its employees for the above stated years, and Taxpayer did not withhold Non-Resident County Tax for the year 2013. As a result, the Department issued proposed assessments for the withholding taxes as well as interest and penalty. Taxpayer protested the assessments. An administrative hearing was conducted, and this Letter of Findings results. Additional facts will be provided as necessary.

I. Withholding Tax-State and Non-Resident County Imposition.

DISCUSSION

Taxpayer protests the assessment of withholding taxes on wages it paid to its employees for the 2011, 2012, and 2013 tax years. Taxpayer stated that it relied on faulty advice from their payroll service company.

As a threshold issue, it is the taxpayer's responsibility to establish that the existing tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

IC § 6-3-4-8(a) provides that employers must "withhold, collect, and pay over income tax on wages paid to . . . employees." The relevant regulation [45 IAC 3.1-1-97](#), states that employers must "withhold [F]ederal taxes pursuant to the Internal Revenue Code", and are also "required to withhold from employees' wages Adjusted Gross and County Adjusted Gross Income Tax."

Taxpayer maintains that when it fails to withhold the tax, the Department should seek the tax from its employees as individual taxpayers.

IC § 6-3-4-8 provides, in part, as follows:

(a) Except as provided in subsection (d), every employer making payments of wages subject to tax under this article, regardless of the place where such payment is made, who is required under the provisions of the Internal Revenue Code to withhold, collect, and pay over income tax on wages paid by such employer to such employee, shall, at the time of payment of such wages, deduct and retain therefrom the amount prescribed in withholding instructions issued by the department. The department shall base its withholding instructions on the adjusted gross income tax rate for persons, on the total rates of any income taxes that the taxpayer is subject to under [IC 6-3.5](#), and on the total amount of exclusions the taxpayer is entitled to under [IC 6-3-1-3.5\(a\)\(3\)](#) and [IC 6-3-1-3.5\(a\)\(4\)](#). However, the withholding instructions on the adjusted gross income of a nonresident alien (as defined in Section 7701 of the Internal Revenue Code) are to be based on applying not more than one (1) withholding exclusion, regardless of the total number of exclusions that [IC 6-3-1-3.5\(a\)\(3\)](#) and [IC 6-3-1-3.5\(a\)\(4\)](#) permit the taxpayer to apply on the taxpayer's final return for the taxable year. Such employer making payments of any wages:

(1) shall be liable to the state of Indiana for the payment of the tax required to be deducted and withheld under this section and shall not be liable to any individual for the amount deducted from the individual's wages and paid over in compliance or intended compliance with this section; and

(2) shall make return of and payment to the department monthly of the amount of tax which under this article and [IC 6-3.5](#) the employer is required to withhold.

(Emphasis added).

Accordingly, IC § 6-3-4-8(a) specifically requires an employer to "withhold, collect, and pay over income tax on wages paid by such employer to such employee . . . [in] the amount prescribed in withholding instructions issued by the department." IC § 6-3-4-8(a)(1) specifically provides that the employer is "liable to the state of Indiana for the payment of the tax required to be deducted and withheld." (Emphasis added). IC § 6-3-4-8 specifically provides that the employer is liable for the amount that it was required to withhold. These statutory requirements for the employer to withhold the amount prescribed in the Department's withholding instructions and for the employer to become liable for the amount it is required to withhold are restated in [45 IAC 3.1-1-97](#). "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." *Id.* The regulation then goes on to state, "In the case of delinquency or nonpayment of withholding tax, the employer is liable for such tax, penalties, and interest." *Id.*

Taxpayer asks for a reduction in its withholding tax liability by the actual amount that its employees paid in the employees' respective individual income tax returns attributable to the employees' given county. Taxpayer asks for the Department to look beyond the W-2s and look at the individual employee's tax return information.

In effect, Taxpayer is requesting that the Department perform individual income tax audits of each of its employees to determine if the tax that it was required to pay was paid by the individuals and then relieve Taxpayer of its responsibility for withholding tax if individual employees did in fact report and pay the tax. For the Department to do what the Taxpayer requests, the Department would have to schedule individual audits with each of Taxpayer's employees, request copies of the employee's federal tax returns and other records, and then provide this employee's information about how much of the income was reported with the tax paid to Indiana to Taxpayer. However, there is nothing in Indiana law which allows such treatment. Moreover, if the Department attempted to do as Taxpayer suggests, the Department would be violating the tax confidentiality requirements found in IC § 6-8.1-7-1(a) that prohibits the Department from sharing one taxpayer's information—i.e., the employee's tax information—with another taxpayer—i.e., the employer. Unlike the S-corporation withholding statute where the legislature has given the Department express authority, in IC § 6-3-4-13(i), for the shareholder's tax information to be shared with the S-corporation and to relieve the S-corporation of its withholding tax liability when the adjusted gross income tax has been paid by the shareholder, the Indiana legislature has not provided this remedy for employers with withholding tax liabilities.

FINDING

For the reasons stated above, Taxpayer's protest is respectfully denied.

II. Tax Administration-Penalty and Interest.

Taxpayer protests the impositions of penalty and interest. Taxpayer asserts that the Department should abate the negligence penalty and interest.

A. Interest.

Taxpayer requests the abatement of interest imposed on the withholding tax assessment. Indiana imposes interest on overdue tax pursuant to IC § 6-8.1-10-1(a), which provides:

If a person fails to file a return for any of the listed taxes, fails to pay the full amount of tax shown on the person's return by the due date for the return or the payment, or incurs a deficiency upon a determination by the department, the person is subject to interest on the nonpayment.

In the case of the interest assessed, the Department has no discretion to abate or adjust the amount of interest owed. IC § 6-8.1-10-1(e). Taxpayer's request to abate interest is denied.

B. Penalty.

Taxpayer requests the penalty be abated. Taxpayer maintains that penalty waiver is warranted because it has a quality compliance record with regard to other tax filings, and that the mistake made was reasonable.

IC § 6-8.1-10-2.1(a)(2) requires a ten-percent penalty if the taxpayer "fails to pay the full amount of tax shown on the person's return on or before the due date for the return or payment."

The regulation which controls the application of penalty is [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.

Generally, the Department will waive penalty in the event of an unusual error and a good compliance record. [45 IAC 15-11-2\(c\)](#) explains that:

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. Factors which may be considered in determining reasonable cause include, but are not limited to:

- (1) the nature of the tax involved;
- (2) judicial precedents set by Indiana courts;
- (3) judicial precedents established in jurisdictions outside Indiana;
- (4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc.;
- (5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

In the instant case, Taxpayer relied on purportedly bad advice from its payroll service company. They had no reason to know that the service was wrong. Furthermore, this is Taxpayer's first and only liability. Taxpayer's history is favorable.

Taxpayer has provided sufficient information to establish that its failure to pay the deficiency in this instance was not due to Taxpayer's negligence, but was due to reasonable cause as required by [45 IAC 15-11-2\(c\)](#). Furthermore, Taxpayer has taken steps to insure that this action does not occur again. Therefore, the Department sustains the Taxpayer's penalty protest.

FINDING

For the reasons stated above, Taxpayer's protest to abate the penalty is sustained, and Taxpayer's protest to abate the interest is denied.

SUMMARY

Taxpayer's protest is denied in part and sustained in part. Taxpayer's protest of the imposition of penalty is sustained as discussed in Issue II, B. The remainder of Taxpayer's protest is denied as discussed in Issues I and II, A.

Posted: 06/24/2015 by Legislative Services Agency
An [html](#) version of this document.