

Letter of Findings: 03-20160300
Indiana Withholding Tax
For the Years 2011, 2012, and 2013

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 This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register.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

Indiana Transportation Provider was required to withhold income tax on behalf of the drivers hired to deliver goods on behalf of the Transportation Provider; the "lease agreements" entered into with the drivers failed to establish that the drivers were independent contractors and not employees.

ISSUE

I. Withholding Tax - Employee/Independent Contractor.

Authority: IC § 6-3-4-8; IC § 6-3-4-8(g); IC § 6-8.1-5-1; Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Longmire v. Indiana Dep't of State Revenue, 638 N.E.2d 894 (Ind. Tax Ct. 1994); IRS Publication 15-A (2011); 41 Am. Jur. 2d Independent Contractors §1 (2009); Black's Law Dictionary (8th ed. 2004).

Taxpayer argues that it was not required to withhold income tax on behalf of the people who work for Taxpayer's businesses.

STATEMENT OF FACTS

Taxpayer operates Indiana businesses including a trucking company and grocery company. The trucking company pays drivers to transport steel and other materials from one location to the next. The Indiana Department of Revenue ("Department") conducted an audit review of Taxpayer's business records and tax returns. The audit resulted in an assessment of withholding tax. Taxpayer disagreed with the assessment and submitted a protest to that effect. An administrative hearing was conducted by telephone during which Taxpayer's representative explained the basis for the protest. This Letter of Findings results.

I. Withholding Tax - Employee/Independent Contractor.

DISCUSSION

The issue is whether the persons who work for and are paid by the businesses are independent contractors or employees.

The Department's audit reviewed Taxpayer's various tax returns and business records. The audit noted that Taxpayer had various persons on its trucking company and grocery company payroll. The audit found that Taxpayer "was not registered for withholding tax during the audit years of 2011, 2012, and 2013." The audit also found that "[T]axpayer paid wages to drivers employed by [trucking company]." However, the audit pointed out that Taxpayer did not issue 1099-MISC ("Miscellaneous Income") forms on behalf of the people who worked for Taxpayer.

The audit concluded that the people who worked for the grocery store and the trucking company were "employees" and that Taxpayer should have been withholding income tax on their behalf. The Department assessed Taxpayer withholding tax on behalf of the employees for the three years under review.

Taxpayer disagrees on various grounds including the argument that the drivers who work for the trucking company are "independent contractors," that the money it pays to a repair shop to repair the trucking company's vehicles is not subject to withholding, and that a portion of the money paid to one of the grocery employees

constituted payment for the purchase of real estate is also not subject to the withholding requirement.

As a threshold issue, all tax assessments are prima facie evidence that the Department's claim for the unpaid tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dept. of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

IC § 6-3-4-8 requires employers to withhold income tax on behalf employees subject to federal income tax:

(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.

IC § 6-3-4-8(g) imposes on employers personal liability for the collection and payment of the tax.

The provisions of [IC 6-8.1](#) relating to additions to tax in case of delinquency and penalties shall apply to employers subject to the provisions of this section, and for these purposes any amount deducted or required to be deducted and remitted to the department under this section shall be considered to be the tax of the employer, and with respect to such amount the employer shall be considered the taxpayer. In the case of a corporate or partnership employer, every officer, employee, or member of such employer, who, as such officer, employee, or member is under a duty to deduct and remit such taxes shall be personally liable for such taxes, penalties, and interest.

Accordingly, an employer is required to withhold Indiana state and county income taxes pursuant to IC § 6-3-4-8 and IC § 6-3-4-8(g), which piggybacks the requirement to withhold for federal tax purposes. That is, when an employer is required to withhold federal income tax for an individual because that individual is an employee of the employer - defined either by common law or by statute - the employer is also required to withhold Indiana state and county income taxes for that individual as well (provided that the wages are subject to Indiana income tax).

"Employer" is defined as "[a] person who controls and directs a worker under an express or implied contract of hire and who pays the worker's salary or wages." Black's Law Dictionary 565 (8th ed. 2004). "Employee" is defined as "[a] person who works in the service of another person (the employer) under an express or implied contract of hire, under which the employer has the right to control the details of work performance." Id. at 564. "Independent contractor" is defined as "[o]ne who is entrusted to undertake a specific project but who is left free to do the assigned work and to choose the method for accomplishing it." Id. at 785. Under law, an "independent contractor is one who, in exercising an independent employment, contracts to do certain work according to his or her own methods, without being subject to the control of the employer, except as to the product or result of the work." 41 Am. Jur. 2d Independent Contractors §1 (2009). Behavioral and financial controls are the crucial factors in determining whether an employer-employee relationship exists. An employer-employee relationship "exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished." Longmire v. Indiana Dep't of State Revenue, 638 N.E.2d 894, 897 (Ind. Tax Ct. 1994).

The Internal Revenue Service ("IRS"), in its Publication 15-A, in relevant part, states:

To determine whether an individual is an employee or an independent contractor under the common law, the

relationship of the worker and the business must be examined. In any employee-independent contractor determination, all information that provides evidence of the degree of control and the degree of independence must be considered.

The IRS publication provides that "facts that provide evidence of the degree of control and independence fall into three categories: behavioral control, financial control, and the type of relationship of the parties." The IRS publication further provides additional factors to be considered as follows:

Behavioral control. Facts that show whether the business has a right to direct and control how the worker does the task for which worker is hired include the type and degree of:

Instructions that the business gives to the worker. An employee is generally subject to the business' instructions about when, where, and how to work. All of the following are examples of types of instructions about how to do work.

- When and where to do the work.
- What tools or equipment to use.
- What workers to hire or to assist with the work.
- Where to purchase supplies and services.
- What work must be performed by a specified individual.
- What order or sequence to follow.

The amount of instruction needed varies among different jobs. Even if no instructions are given, sufficient behavioral control may exist if the employer has the right to control how the work results are achieved. A business may lack the knowledge to instruct some highly specialized professionals; in other cases, the task may require little or no instruction. The key consideration is whether the business has retained the right to control the details of a worker's performance or instead has given up that right.

Training that the business gives to the worker. An employee may be trained to perform services in a particular manner. Independent contractors ordinarily use their own methods.

Financial Control. Facts that show whether the business has a right to control the business aspects of the worker's job include:

The extent to which the worker has unreimbursed business expenses. Independent contractors are more likely to have unreimbursed expenses than are employees. Fixed ongoing costs that are incurred regardless of whether work is currently being performed are especially important. However, employees may also incur unreimbursed expenses in connection with the services that they perform for their employer.

The extent of the worker's investment. An independent contractor often has a significant investment in the facilities or tools he or she uses in performing services for someone else. However, a significant investment is not necessary for independent contractor status.

The extent to which the worker makes his or her services available to the relevant market. An independent contractor is generally free to seek out business opportunities. Independent contractors often advertise, maintain a visible business location, and are available to work in the relevant market.

How the business pays the worker. An employee is generally guaranteed a regular wage amount for an hourly, weekly, or other period of time. This usually indicates that a worker is an employee, even when the wage or salary is supplemented by a commission. An independent contractor is often paid a flat fee or on a time and materials basis for the job. However, it is common in some professions, such as law, to pay independent contractors hourly.

The extent to which the worker can realize a profit or loss. An independent contractor can make a profit or loss.

Type of relationship of the parties. Facts that show the parties' type of relationship include:

- Written contracts describing the relationship the parties intended to create.
- Whether or not the business provides the worker with employee-type benefits, such as insurance, a pension plan, vacation pay, or sick pay.

- The permanency of the relationship. If you engage a worker with the expectation that the relationship will continue indefinitely, rather than for a specific project or period, this generally considered evidence that you intent was to create an employer-employee relationship.
- The extent to which services performed by the worker are a key aspect of the regular business of the company. If a worker provides services that are a key aspect of your regular business activity, it is more likely that you will have the right to direct and control his or her activities. For example, if a law firm hires an attorney, it is likely that it will present the attorney's work as its own and would have the right to control or direct that work. This would indicate an employer-employee relationship.

A. Truck Drivers.

Taxpayer explains that its trucking company primarily arranges for the transportation of steel from one location to the next and that it does so by means of lease agreements with its drivers.

Taxpayer argues that the company drivers are "independent contractors" who operate pursuant to "leasing agreements." According to Taxpayer, the agreements "state that these individuals are responsible for any and all taxes that would be due from income generated from these agreements."

Under the terms of the agreements, Taxpayer agreed to rent certain equipment from the drivers, that Taxpayer had exclusive use of the equipment for the duration of the agreement, that it would compensate the drivers for fuel and mileage expenses, that Taxpayer would be responsible for liability and property insurance costs, that Taxpayer would - on occasion - furnish the driver with trailers and/or tractors, and that the owner/driver would guarantees Taxpayer "quiet and peaceful useful use and possession of the equipment" during the term of the lease.

The "lease agreements" necessarily specified the obligations and responsibilities of both Taxpayer and the drivers, but the Department is unable to agree with Taxpayer that it has met its burden of establishing that the drivers are independent contractors free to come-and-go as they please, that it lacked the ability to control the delivery of goods from one location to the next, or lacked the right to control the actions and performance of the drivers who were hired by Taxpayer to fulfill its obligation to the steel manufacturer. As explained in the audit report, "Taxpayer . . . had complete control of the activities of the business." Taxpayer took upon itself the responsibility of delivering steel on behalf of the steel manufacturer and - in order to fulfill that responsibility - it necessarily directed and controlled the timing, location, means, and method by which it accepted delivery of the steel from the manufacturer and then deliver that steel to the location specified by the manufacturer. In summary, the drivers were not entirely free to perform the assigned work in a manner that the drivers chose or to choose the method by which the steel would be delivered.

B. Repair Shop.

Taxpayer argues that it was not required to withhold tax on payments made to a truck repair facility. To that end, it attached copies of invoices issued by the repair facility. Taxpayer maintains that the amount it paid for these repairs was not subject to withholding tax. To the extent that Taxpayer provided six invoices charging Taxpayer for the repair of vehicles, Taxpayer is correct. The invoices plainly specify repair and parts charges which are not subject to withholding tax.

C. Trucking Company.

Taxpayer states that it entered into an agreement with Trucking Company "to haul freight for this Company." Taxpayer presented a Department of Transportation permit issued to Trucking Company. That permit granted Trucking Company "authority to engage in transportation as a contract carrier of property by motor vehicle"

Unlike the drivers addressed in Part A above, Taxpayer has provided no written agreement detailing Taxpayer and Trucking Company's mutual responsibilities and duties. It is unclear whether Trucking Company was or was not an "employee" or a true "independent contractor." Other than the DOT permit and invoices issued by the Trucking Company, there is nothing that delineates the parties' relationship or whether Taxpayer was paying Trucking Company as a business entity or an individual. Under IC § 6-8.1-5-1(c), Taxpayer has failed to meet its responsibility of establishing that the assessment of withholding tax was "wrong."

D. Grocery Employee.

Taxpayer hired a Family Member to work in its grocery business. The Department's audit assessed withholding

tax on the amount of money paid to this Family Member. Taxpayer admits that this Family Member is an employee of the grocery business but argues that a portion of the amount paid the Family Member is not subject to tax. Taxpayer explains that it entered into an agreement with the Family Member for the purchase of real estate. Under that agreement, Taxpayer was required to pay Family Member an installment payment of \$674 each month. Taxpayer provided a copy of the purchase agreement detailing the real estate purchase and Taxpayer's obligation to pay the specified monthly installment. The Department agrees that the \$674 monthly payment is unrelated to the wages paid the Family Member and that the Department's original audit should be adjusted to reflect that determination.

FINDING

Taxpayer's protest is denied in part and sustained in part.

SUMMARY

With the exception of monthly installment payments made to an employee/Family Member and specific payments made for the repair of Taxpayer's vehicles, Taxpayer's protest is respectfully denied.

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