Tax Policy Directive #5

May 1992

Purpose: The Policy Directives are intended to provide the general public with information concerning the Department's official position in regard to a specific issue. These directives may be relied upon by taxpayers until superseded by another policy directive, a change in statute or regulation, or a court decision that would render the policy directive void.

Subject: Withholding on Nonresident Individual Partners and Shareholders who are Domiciled in a Reverse Credit State

Reference: IC 6-3-4-12, IC 6-3-4-13.

Introduction

This policy directive is to indicate situations wherein withholding of taxes is not required, even though it would seem to be required by statute.

Discussion

IC 6-3-4-12 requires a partnership to withhold on distributions or amounts credited to nonresident partners. IC 6-3-4-13 requires certain corporations to withhold on distributions or amounts credited to nonresident shareholders. The partnership or corporation becomes liable to the State of Indiana for the payment of this tax and must report it as statutorily required. The nonresident partner or shareholder must file the appropriate tax return in order to claim credit for the taxes withheld.

A unique situation occurs when a nonresident individual partner or shareholder is domiciled in a reverse credit state with a higher tax rate than Indiana's. These individuals may claim credit on their Indiana nonresident return for taxes paid to their state of domicile on Indiana source income. Because the domiciliary state imposes a higher tax rate, such individuals will normally not owe any tax to the State of Indiana.

Conclusion

The withholding of taxes pursuant to IC 6-3-4-12 and IC 6-3-4-13 is not required when a nonresident individual partner or shareholder is domiciled for the entire year in a reverse credit state with a higher tax rate than the tax rate in force in Indiana for that tax year and the Indiana source income is actually taxed in the domiciliary state.

Kenneth L. Miller
Commissioner