EXHIBIT 5
DATE 1-24-13
HB 19

HB 19 – Substantial Understatement Penalty

Section 2 - MCA §15-1-216 (3)

Individual Income Tax

There is a substantial understatement of tax if the understatement is the *greater* of 10% of the amount required to be shown on the return or $3,000.

Example 1:

- Taxpayer filed return and paid a tax liability of $1,000
- Per audit - the adjusted tax liability is $5,000

Does the understatement ($4,000) exceed the greater of 10% of the tax required to be shown on the return (10% x $5,000 = $500) OR $3,000?

Yes: Penalty is 20% of underpayment ($4,000) = $800

Example 2:

- Taxpayer filed return and paid a tax liability of $750
- Per audit - the adjusted tax liability is $1,000

Does the understatement ($250) exceed the greater of 10% of the tax required to be shown on the return (10% x $1,000 = $100) OR $3,000?

No: Penalty will not be assessed.

All Other Taxes

There is a substantial understatement of tax if the understatement exceeds the *lesser* of 10% of the amount required to be shown on the return (provided the understatement is greater than $10,000), or $500,000

Example 1:

- Taxpayer filed return and paid a tax liability of $80,000
- Per audit - the adjusted tax liability is $150,000

Does the understatement ($70,000) exceed the lesser of 10% of the tax required to be shown on the return (10% x $150,000 = $15,000) provided the understatement is > $10,000 OR $500,000?

Yes: Penalty is 20% of underpayment ($70,000) = $14,000

Example 2:

- Taxpayer filed return and paid a tax liability of $25,000
- Per audit - the adjusted tax liability is $30,000

Does the understatement ($5,000) exceed the lesser of 10% of the tax required to be shown on the return (10% x $30,000 = $3,000) provided the understatement is > $10,000 OR $500,000?

No: Penalty will not be assessed.