



TaxNewsFlash

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North Carolina: Market-based sourcing and marketplace-facilitator legislation enacted

North Carolina's governor on November 8, 2019, signed into law Senate Bill 557 that:

- Increases the standard deduction for individuals
- Adopts market-based sourcing effective for tax years beginning on or after January 1, 2020
- Requires marketplace facilitators to collect and remit sales and use tax effective February 1, 2020
- Expands the definition of a holding company for franchise tax purposes

The governor vetoed a separate bill (Senate Bill 587) to reduce the franchise tax rate and modify film credits.

Read [Senate Bill 557](#) [PDF 259 KB]

Market-based sourcing

Senate Bill 557 adopts market-based sourcing rules for sales of other than tangible personal property effective for tax years beginning on or after January 1, 2020.

Receipts will be attributed to North Carolina if the taxpayer's market for the receipts is in the state. If the market for a receipt cannot be determined, the state or states of assignment must be reasonably approximated. If a taxpayer cannot ascertain the state or states to which receipts of a sale are to be assigned through the use of a method of reasonable approximation, the receipts must be excluded from the denominator of a taxpayer's sales factor.

The new law establishes the following rules for assigning a taxpayer's receipts to North Carolina:

- In the case of a sale, rental, lease or license of real property—if and to the extent the real property is located in North Carolina.
- In the case of a rental, lease or license of tangible personal property—if and to the extent the property is located in North Carolina.

- In the case of a sale of a service—if and to the extent the service is delivered to a location in North Carolina.
- In the case of a rental, lease or license of intangible property—if and to the extent the intangible property is used in North Carolina. Intangible property used in marketing a good or service to a consumer is “used in” North Carolina if that good or service is purchased by a consumer in the state.
- In the case of intangible property that is sold—if and to the extent the property is used in North Carolina. A contract right, government license or similar intangible property that authorizes the holder to conduct a business activity in a specific geographic area is “used in” North Carolina if the geographic area includes all or part of North Carolina. Receipts from a sale of intangible property that is contingent on the productivity, use or disposition of the intangible property are to be treated as receipts from the rental, lease or licensing of the intangible property.

All other receipts from a sale of intangible property must be excluded from the numerator and denominator of the sales factor.

Apportionment rules

Senate Bill 557 has special provisions for a taxpayer with a state net loss balance as of the end of its 2019 tax year. These taxpayers may elect to apportion receipts from services based on the percentage of the income-producing activities performed in North Carolina (i.e., using the prior method of apportionment). The election must be made on the 2020 tax year return and in the form required by the Secretary, including any supporting documentation. The election is binding and irrevocable until the earlier of the tax year in which the existing state net loss balance is fully used or all of the existing state net loss balance has expired. A taxpayer must apportion receipts from services in accordance with the market-based sourcing rules for tax years beginning on and after the tax year that the existing state net loss is fully utilized. The “state net loss balance” is the total amount of state net losses for tax years beginning before January 1, 2020, and available for carryforward to tax years beginning on or after January 1, 2020. A state net loss created in a tax year beginning on or after January 1, 2020, must be determined using the market-based sourcing rules.

Senate Bill 557 also adopts specific apportionment rules for various industries, including pipeline companies, electric power companies, wholesale content distributors, and banks:

- For pipeline companies subject to regulation by the Federal Energy Regulatory Commission—receipts from the transportation and transmission of petroleum-based liquids and natural gas are apportioned based on the number of “traffic units” in state versus traffic units everywhere. A “traffic unit” is defined as a “barrel mile” or “cubic foot mile,” depending on the natural state of the property.
- For electric power companies—the apportionment factor is based on the average value of the real and tangible personal property owned or rented and used by the electric power company. Senate Bill 557 provides rules for determining the average value of the real or tangible personal property.
- For wholesale content distributors—these distributors (as defined) must apportion receipts using the sum of gross receipts from transactions and activities in the regular course of its trade and business in North Carolina compared to gross receipts from transactions and activities in the regular course of business everywhere. Transactions and activities (including advertising, licensing, and distribution activities as well as subscriptions of individual consumers) are attributed to North Carolina under specific rules. Receipts from the sale of real or tangible personal property are specifically excluded from the apportionment calculation. In no event may the amount of income

apportioned to North Carolina be less than 2% of the total domestic gross receipts of the wholesale content distributor from advertising and licensing activities.

- For banks—Senate Bill 557 adopts an extensive list of rules for sourcing various types of receipts received by banks, including but not limited to, receipts from the sales, lease or rental of property; receipts from interest, fees, and penalties from cardholders; receipts from ATM fees; net gains from sales of credit card receivables; and other “miscellaneous receipts.” Specific types of receipts (e.g., dividends subtracted or excluded and the portion of receipts realized from the sale or maturity of securities or other obligations that represent a return of principal) are excluded entirely from the receipts factor.

Marketplace (and other) facilitator provisions

Senate Bill 557 requires marketplace facilitators (as defined) to collect and remit sales tax on sales they facilitate, effective February 1, 2020 if in the previous or current calendar year, the marketplace facilitator exceeds \$100,000 in gross sales or has 200 or more separate transactions. A marketplace facilitator that meets the threshold is considered to be the retailer of each marketplace-facilitated sale it makes and is liable for collecting and remitting the sales and use tax on all such sales.

A marketplace facilitator is required to collect and remit sales tax regardless of whether a marketplace seller for whom it makes a marketplace-facilitated sale has a physical presence in North Carolina or otherwise is required to register with the Department of Revenue.

A marketplace facilitator and a marketplace seller may enter into an agreement with each other regarding the fulfillment of the requirements under the marketplace law, except that an agreement may not require a marketplace seller to collect and remit sales and use tax on marketplace-facilitated sales.

A marketplace facilitator is defined as:

A person that, directly or indirectly and whether through one or more affiliates, ... [l]ists or otherwise makes available for sale a marketplace seller's items through a marketplace owned or operated by the marketplace facilitator [and] ... [c]ollects the sales price or purchase price of a marketplace seller's items or otherwise processes payment [and/or] [m]akes payment processing services available to purchasers for the sale of a marketplace seller's items.

Senate Bill 557 also:

- Provides for relief for marketplace facilitators under certain circumstances and requires a marketplace facilitator to provide monthly reports to a marketplace seller on gross sales volume and number of transactions facilitated.
- Excludes accommodation facilitators, admission facilitators, and service contract facilitators (as defined) from the marketplace-facilitator requirements. These other facilitators have preexisting and separate obligations to collect on their sales, and Senate Bill 557 requires these facilitators to comply with certain reporting requirements.
- Amends the definition an accommodation facilitator to mean a person that markets and accepts payment for the rental of accommodations or lists the accommodation for rental on a platform for a fee or other consideration. “Accommodation” is defined as a hotel room, a motel room, a residence, a cottage, or a similar lodging facility for occupancy by an individual. An accommodation facilitator is deemed the retailer of the accommodation rental and is required to collect and remit tax on the portion of the gross receipts derived from the rental that the facilitator collects.
- Provides that certain accommodation facilitators are not considered to be retailers if they are “operated by or on behalf of a hotel or a hotel corporation, that facilitates the rental of hotel accommodations solely for the hotel or the hotel corporation's owned or managed hotels and

franchisees, and that collects payment, or a portion of the payment, for the rental of an accommodation.” In this instance, the accommodation facilitator must send to the hotel operator (or retailer) the tax collected on the sales price or the portion of the sales price that the facilitator collected, and the retailer is responsible for remitting the applicable tax to the Department. Accommodation facilitators are also required to file an annual report with the Department of Revenue on the rentals it makes and the gross receipts for such rentals.

- Revises the current law provisions that address facilitators that facilitate sales of admissions and service contracts. An admission facilitator is “[a] person who accepts payment of an admission charge to an entertainment activity and who is not the operator of the venue where the entertainment activity occurs.” A service contract facilitator is “[a] person who contracts with the obligor of a service contract to market the service contract and accepts payment from the purchaser for the service contract.” Senate Bill 557 imposes new reporting requirements on these entities.

Expanded holding company definition

Under North Carolina law, franchise tax payable by a corporation that is classified as a “holding company” is limited to \$150,000, when the company is paying on its net worth base. If the “holding company” definition is not met, there is no limitation.

Senate Bill 557 adds a third condition to the definition of a holding company for franchise tax purposes effective for tax years beginning on or after January 1, 2020, and applicable to the calculation of franchise tax reported on the 2019 and later corporate income tax returns.

Under prior law, a company had to meet at least one of two conditions to be considered a holding company. Under the new law (as revised), a holding company will also include an entity that owns copyrights, patents or trademarks that represent more than 80% of its total assets, or receives royalties and license fees that represent more than 80% of its gross income, if it is 100% directly owned by a corporation that meets all of the following conditions: (1) it is a manufacturer, as defined by NAICS codes 31 through 33; (2) it generates revenues in excess of \$5 billion for income tax purposes from goods that it manufactures; and (3) it includes, in its net worth, an investment in a subsidiary that owns copyrights, patents or trademarks.

Various other miscellaneous changes

Dual notices: The Department must update its electronic tax systems to store and recognize power of attorney registrations so that notices generated by the Department are simultaneously sent to both the taxpayer and the person designated in the taxpayer's power of attorney registration. By January 31, 2020, the Department is to report to the Joint Legislative Oversight Committee on General Government on its progress in updating its electronic tax systems.

Review of expiring tax provisions: The Revenue Laws Study Committee may review any tax provision set to sunset within one year of the beginning of the next regular session of the General Assembly to determine whether the sunset needs to be extended.

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