



This Week in State Tax (TWIST)

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South Carolina: Credit Card Company's Income Producing Activities Occurred in South Carolina

The South Carolina Administrative Law Court recently ruled in favor of the Department of Revenue in a case involving the sourcing and apportionment of a credit card network taxpayer's income for corporate income tax purposes. The taxpayer, the operator of a worldwide credit card network, generated revenue by charging fees based on the number of credit and debit transactions from branded cards and the gross dollar volume of those transactions. The transactions were initiated when cardholders presented branded credit or debit cards to accepting merchants as payment for goods and services. Although the taxpayer had not filed any corporate tax returns for the audit period, the key issue before the court was way the gross receipts generated from transactions initiated at merchant locations in South Carolina should be sourced. The Department's position was that receipts from South Carolina initiated transactions were attributed to the state. In contrast, the taxpayer's position was that while credit card transactions occurred in South Carolina, its network was not present in the state, and it had no state-sourced income.

The court first determined that the taxpayer's payment network was present and operating in South Carolina, and the taxpayer was doing business in the state. Under South Carolina law, service receipts are sourced to the state where the income-producing activity occurs. As such, the taxpayer's income should have been sourced to South Carolina to the extent that the income-producing activity was performed in the state. In the case of the taxpayer, the court found that the relevant income-producing activity was providing access to the network, which facilitated credit card transactions between merchants and cardholders throughout the country, including South Carolina. That income-producing activity occurred in South Carolina when a transaction was initiated in the state, as the taxpayer's authorization, clearing, settlement, and assessment platforms were all used to process these transactions. The taxpayer argued that its income producing activity was the processing and delivery of information between the Issuer (cardholder's) and Acquirer (merchant's) banks which was entirely outside South Carolina and did not involve the cardholder or merchant.

While it was undisputed certain transaction processing functions occurred at locations outside South Carolina, in the court's view those functions were secondary to the activity that truly generated revenue. There was also an extensive discussion in the opinion over who was the taxpayer's customer. The court rejected the taxpayer's assertion that its income was generated solely by the service it performed for the Issuer and Acquirer banks, which were its direct customers. The taxpayer, the court noted, promoted its cards and services to both cardholders and merchants, had designed specific benefits for each, and generated income based on their activities. The merchants and cardholders who, because of the payment network, were able to consummate cashless transactions, were beneficiaries of the taxpayer's services. Having concluded that the taxpayer had receipts sourced to South Carolina, the court next addressed penalties and interest. The court upheld the Department's assessment of failure to file penalties and interest, but because of the complexity of the issues presented, the court concluded that the taxpayer exercised ordinary business care and prudence such that the majority, but not all, of the failure to pay penalties should be waived. Please contact [Jeana Parker](#) with questions on *Mastercard International Incorporated v. South Carolina Department of Revenue*.

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