



SENATE BILL 557: Various Finance Law Changes.

**This Bill Analysis
reflects the contents
of the bill as it was
presented in
committee.**

2019-2020 General Assembly

Committee:	Senate Finance	Date:	October 22, 2019
Introduced by:	Sens. Krawiec, Rabon, Lowe	Prepared by:	Nicholas Giddings Staff Attorney
Analysis of:	PCS to First Edition S557-CSBAxfr-29		

OVERVIEW: *The Proposed Committee Substitute to Senate Bill 557 would make the following finance law changes, most of which were included in House Bill 966, the 2019 Appropriations Act:*

- *Increase the standard deduction by 7.5%, from \$20,000 to \$21,500 for MFJ (House Bill 966 had a 5% increase), effective for taxable years beginning on or after January 1, 2020 (House Bill 966 had an effective date of January 1, 2021).*
- *Expand the definition of "holding company" for franchise tax purposes.*
- *Require a multistate corporation to calculate its sales factor, for apportionment purposes, based on the percentage of income attributed to the consumption of products and services in the North Carolina marketplace.*
- *Obligate a "marketplace facilitator" that meets the same threshold applicable to remote retailers to calculate, collect, and remit sales tax on a third-party seller's behalf (House Bill 966 had an effective date of September 1, 2019; the PCS pushes the date out to February 1, 2020).*
- *Direct the Revenue Laws Study Committee to review certain tax sunset provisions.*
- *Make technical changes (not included in House Bill 966).*

[As introduced, this bill was identical to H537, as introduced by Reps. Conrad, Howard, Setzer, D. Hall, which is currently in an unknown committee.]

BILL ANALYSIS AND EFFECTIVE DATES:

Section 1 would increase the standard deduction for all filing statuses by 7.5%, effective for taxable years beginning on or after January 1, 2020.

Section 2 would expand the definition of holding company, effectively capping the franchise tax on that holding company to \$150,000. The purpose of the holding company cap is to prevent the taxation of assets that are included in the net worth of the subsidiary, and indirectly in the net worth of the parent company by virtue of its investment in the holding company. The new definition of holding company is tightly drawn:

- More than 80% of the holding company's assets must be copyrights, patents, and trademarks, or more than 80% of its gross income must come from royalties and license fees.
- The holding company must be 100% directly owned by a parent corporation that includes in its net worth franchise tax base an investment in the holding company.
- The parent company must be a manufacturer who generates revenues in excess of \$5 billion from the goods it manufactures.

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This section would be effective for taxable years beginning on or after January 1, 2020, and would apply to the calculation of franchise tax reported on the 2019 and later corporate income tax returns.

Section 3 would require a multistate corporation to calculate its sales factor, for apportionment purposes, based on the percentage of income attributed to the consumption of products and services in the North Carolina marketplace. Effective for the 2019 taxable year, North Carolina will use single sales factor apportionment. A single sales factor arguably makes a state a more attractive place for a multistate company that provides products to expand its property and payroll because if those factors are ignored in calculating a state's corporate tax, then the company can hire employees or build a plant without incurring additional state tax on its corporate profits. Single sales factor does not provide the same incentive to a multistate company that provides services, because its sales factor is not based on the percentage of income derived from consumption of the company's services in a state's marketplace. Instead, its sales factor is based on the percentage of business activities conducted in a state, which is generally measured by the amount of labor costs and capital investment incurred in a state to provide the services. Consequently, states that adopt a single sales factor apportionment incentive usually adopt a market-based calculation of the sales factor for all multistate corporations, including those that provide services. At least 30 states have adopted market-based sourcing.

Subsections (a) through (d) of this section would be effective for taxable years beginning on or after January 1, 2020. The remainder of this section would become effective when law.

Section 4 would obligate a marketplace facilitator that meets the same threshold applicable to remote retailers to calculate, collect, and remit sales tax on a third party seller's behalf. A marketplace facilitator is a person that contracts with third parties to sell goods and services on its platform. The threshold is sales sourced to North Carolina for the previous or current calendar year that meet either of the following: (i) gross sales of \$100,000; or (ii) 200 or more separate transaction. For purposes of meeting the threshold, all sales made by the marketplace facilitator, including the facilitated sales, are considered.

This section would become effective February 1, 2020 and apply to sales occurring on or after that date.

Section 5 would direct the Revenue Laws Study Committee to review any tax provision set to expire within one year of the beginning of the next regular session of the General Assembly to determine whether the sunset needs to be extended.

Section 6 would make a technical correction to conform statutory language.

Section 7 would clarify that the tax changes made in Section 3.9(g) of S.L. 2019-169 (regarding property management contracts) apply to existing contracts. Many property management contracts are multi-year contracts, and this clarification ensures that those contracts do not need to be renegotiated. This section would be effective when it becomes law and apply retroactively to July 16, 2019.

Section 8 would make a technical correction to the definition of "gross sales" in G.S. 105-164.3(12) to clarify that all digital property, not just digital property subject to tax, is included in the definition of "gross sales" for purposes of determining whether a retailer must collect sales and use tax.

EFFECTIVE DATE: Except as otherwise provided, this act would be effective when it becomes law.