THE STATE OF SOUTH CAROLINA
In The Court of Appeals

U.S. Bank National Association, Appellant,

v.

South Carolina Department of Revenue, Respondent.

Appellate Case No. 2024-001577

Appeal From The Administrative Law Court
Milton G. Kimpson, Administrative Law Judge
Robert Lawrence Reibold, Administrative Law Judge

Opinion No. 6168
Heard June 10, 2026 – Filed October 21, 2026

AFFIRMED AS MODIFIED

Bryson Moore Geer, of Nelson Mullins Riley & Scarborough, LLP, of Charleston; Nicole L. Johnson and Craig B. Fields, both of Blank Rome, LLP, of New York, New York; all for Appellant.

Marcus Dawson Antley, III and Wayne Allen Myrick, Jr., both of the South Carolina Department of Revenue, of Columbia, for Respondent.

KONDUROS, J.: U.S. Bank National Association appeals the administrative law court's (ALC's) order affirming the South Carolina Department of Revenue's (the Department's) assessment of additional bank tax, interest, and penalties on excluded receipts from U.S. Bank's mortgage and credit card operations from 2011

through 2016.[1] On appeal, U.S. Bank argues the Department's assessment misapplies section 12-6-2295 of the South Carolina Code (2014 & Supp. 2025) and that the Department's imposition of substantial penalties is unwarranted. We affirm the ALC's order as modified.

FACTS/PROCEDURAL HISTORY

I. U.S. Bank's Business Operations

U.S. Bank operates across the country and maintains its headquarters and principal place of business in Minnesota. It has no banking branches in South Carolina but operates a trust office within the state. During the disputed time, it employed a range of forty to fifty-four employees in South Carolina and filed an average of around 1,500 property tax returns per year.

A. Mortgage Activity

U.S. Bank earns income on three distinct mortgage operations: (1) interest, (2) mortgage servicing fees, and (3) gains on the sale of pooled mortgages. It generally sells the mortgages it holds in South Carolina, selling 95% of those mortgages to government-sponsored entities, such as the Federal Home Loan Mortgage Corporation, the Federal National Mortgage Association, and the Government National Mortgage Association.[2] In turn, the government-sponsored entities pay a mortgage servicing fee for U.S. Bank's management of those mortgages. U.S. Bank operates its application processing, funding, management, and servicing for its mortgages outside of South Carolina, primarily at its office in Kentucky. U.S. Bank also purchases mortgages from third parties, some of which are used to secure property located in South Carolina. Lastly, U.S. Bank earns interest income from the approximately 5% of mortgages it chooses not to sell to a third party. It apportioned no interest income, gains from the sale of mortgages, or mortgage servicing income to South Carolina in its original returns.

B. Credit Card Activity

---

[1] Administrative Law Judge Milton G. Kimpson heard and decided the case, but the case was reassigned to Administrative Law Judge Robert Lawrence Reibold after Judge Kimpson's election to the circuit court bench.

[2] These government-sponsored entities are also commonly known as Freddie Mac, Fannie Mae, and Ginnie Mae respectively.

U.S. Bank also offers credit cards throughout the United States, earning income from two aspects of its credit card operations: (1) credit card fees, including interest, late fees, and annual fees, and (2) interchange fees.[3] Both consumers and small merchants pay the first category of interest, late fees, and annual fees directly to U.S. Bank. For the second category of income, businesses and larger commercial entities pay U.S. Bank interchange fees to facilitate the processing of a transaction, including U.S. Bank's decision to accept or decline the payment and settlement of the payment. In both instances, U.S. Bank performs its consumer and commercial credit card operations all outside of South Carolina, primarily in North Dakota, Missouri, Wisconsin, and Kansas.

II. U.S. Bank's Tax Returns and the Department Audit

U.S. Bank timely filed South Carolina bank tax returns for this period, originally excluding the three types of income from its mortgage operations and the two types of income from its credit card operations as described above. U.S. Bank included income solely from its rental of tangible personal property and trust custody fees for South Carolina customers. In September of 2018, the Department issued a proposed notice of adjustment based on its audit of U.S. Bank for this period, including all receipts relating to U.S. Bank's mortgage and credit card receipts from South Carolina borrowers. U.S. Bank appealed the proposed notice, and the Department upheld the notice in its entirety. U.S. Bank then appealed to the ALC. In July of 2023, U.S. Bank amended its bank tax returns for the years at issue to reflect its own market sourcing analysis.

III. The ALC's Decisions

The ALC's initial order primarily upheld the Department's assessment, but the ALC removed the penalties from U.S. Bank's failure to report interchange fees and the sale of Visa stock. The initial order determined U.S. Bank's mortgage receipts from interest, fees, and gains on the sale of mortgages to government-sponsored entities are all classified as receipts from intangibles and apportionable to South Carolina if the borrower is located within the state. The ALC also determined U.S. Bank's receipts from credit card fees, interest, and interchange fees are receipts from intangibles and apportionable to South Carolina if used within the state. In modifying the penalties from U.S. Bank's failure to report interchange fees as sourced to South Carolina, the ALC determined that reasonable cause existed to

---

[3] U.S. Bank earns both interchange and merchant fees depending on its role in a transaction. For the purposes of our analysis, interchange fees refer to both.

justify U.S. Bank's actions because the Department failed to point to any policy guidance it has issued to assist taxpayers with the Department's interpretation of income-producing activity. In ruling upon U.S. Bank's motion to reconsider the order, the ALC modified its classification of mortgage servicing fees after U.S. Bank sells the mortgage to a government-sponsored entity as a receipt from U.S. Bank's services. Additionally, the ALC excluded U.S. Bank's sale of Visa stock as apportionable to South Carolina, and the Department did not appeal this ruling.

In sum, the combined orders of the ALC determined U.S. Bank must include each of the five income streams in its gross receipts and apportion that income to South Carolina. Applying section 12-6-2295(A) to U.S. Bank's mortgage activities, the ALC determined (1) mortgage servicing fees are receipts from services, finding the income-producing activity is performed in South Carolina; (2) gains on the sale of mortgages are receipts from the sale of intangibles used in the trade or business of U.S. Bank, finding South Carolina mortgages are used within the state; and (3) mortgage interest is a receipt from the use of an intangible, finding U.S. Bank's South Carolina mortgages are used within the state. Applying the same section to U.S. Bank's credit card operations, the ALC concluded (1) receipts from credit card interest and fees are receipts from intangibles, finding the use of the customer's credit card is use of an intangible within the state and (2) interchange fee income is a receipt from a service, finding the income-producing activity occurs at the location of the merchant at which a credit card is used and occurs when processing and approval messages are transmitted to merchants located within South Carolina. The total amount at issue is $4,970,518.15, comprised of $2.8 million in additional tax, $1.5 million in interest, and $582,864.72 in penalties. This appeal follows.

STANDARD OF REVIEW

In an appeal from an ALC decision, the appellate court may only reverse or modify if the decision is

> (a) in violation of constitutional or statutory provisions;
>
> (b) in excess of the statutory authority of the agency;
>
> (c) made upon unlawful procedure;
>
> (d) affected by other error of law;

> (e) clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record; or
>
> (f) arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion.

S.C. Code Ann. § 1-23-610(B) (Supp. 2025).

The reviewing court "may not substitute its judgment for the judgment of the [ALC] as to the weight of the evidence on questions of fact." *Rent-A-Ctr. E., Inc. v. S.C. Dep't of Revenue*, 425 S.C. 582, 586, 824 S.E.2d 217, 219 (Ct. App. 2019) (alteration in original) (quoting § 1-23-610(B)). Judicial review of the ALC's findings of fact is limited to determining if the findings are supported by "substantial evidence." *MRI at Belfair, LLC v. S.C. Dep't of Health & Env't Control*, 379 S.C. 1, 6, 664 S.E.2d 471, 474 (2008). Substantial evidence is evidence which, when considering the record as a whole, would allow reasonable minds to reach the conclusion that the ALC reached. *Books-A-Million, Inc. v. S.C. Dep't of Revenue*, 430 S.C. 388, 391, 844 S.E.2d 399, 400-01 (Ct. App. 2020). When the evidence conflicts on an issue, the court's substantial evidence standard of review defers to the findings of the factfinder and the possibility of drawing two inconsistent conclusions from the evidence does not prevent a finding from being supported by substantial evidence. *Risher v. S.C. Dep't of Health & Env't Control*, 393 S.C. 198, 210, 712 S.E.2d 428, 435 (2011).

"[Q]uestions of statutory interpretation are questions of law, which [the appellate court is] free to decide without any deference to the court below." *DIRECTV Inc. & Subs. v. S.C. Dep't of Revenue*, 421 S.C. 59, 69, 804 S.E.2d 633, 638 (Ct. App. 2017) (second alteration in original) (quoting *Centex Int'l, Inc. v. S.C. Dep't of Revenue*, 406 S.C. 132, 139, 750 S.E.2d 65, 69 (2013)). "The cardinal rule of statutory interpretation is to ascertain and effectuate the intention of the legislature." *Sloan v. Hardee*, 371 S.C. 495, 498, 640 S.E.2d 457, 459 (2007). "Whe[n] the statute's language is plain and unambiguous, and conveys a clear and definite meaning, the rules of statutory interpretation are not needed and the court has no right to impose another meaning." *Media Gen. Commc'ns, Inc.*, 388 S.C. 138, 148, 694 S.E.2d 525, 530 (quoting *Hodges v. Rainey*, 341 S.C. 79, 85, 533 S.E.2d 578, 581 (2000)).

"[I]n the enforcement of tax statutes, the taxpayer should receive the benefit in cases of doubt." *Alltel Commc'ns, Inc. v. S.C. Dep't of Revenue*, 399 S.C. 313, 321,

731 S.E.2d 869, 873 (2012) (quoting *S.C. Nat'l Bank v. S.C. Tax Comm'n*, 297 S.C. 279, 281, 376 S.E.2d 512, 513 (1989)).

LAW/ANALYSIS

I. U.S. Bank's Business Activity in the State

South Carolina imposes a "bank tax" of 4.5% on the entire net income of every bank doing business in the state. S.C. Code Ann. § 12-11-20 (2014).[4] The bank tax is separate from the income tax imposed in Chapter 6 of Title 12. But some provisions related to income tax are adopted by the bank tax statutes. "For the purpose of . . . allocation and apportionment . . . [and] penalties, . . . all of the provisions of Chapter 6 of this title that may be appropriate or applicable are adopted and made a part of this chapter for the enforcement and administration of this chapter . . . ." S.C. Code Ann. § 12-11-40 (2014). Ultimately, banks pay their apportionable tax through the same gross-receipts formula as corporations, but at a 4.5% rate rather than the 5% corporate tax rate. *See* § 12-11-20; S.C. Code Ann. § 12-6-530 (2014).

The receipts included in the denominator as "South Carolina Gross Receipts" are sourced through section 12-6-2295:

> The term[] . . . "gross receipts" as used in [s]ection 12-6-2290 include[s], but [is] not limited to, the following items if they have not been separately allocated:
>
> > (1) receipts from the sale or rental of property maintained for sale or rental to customers in the ordinary course of the taxpayer's trade or business including inventory;
> >
> > . . .
> >
> > (3) receipts from the use of intangible property in this [s]tate including, but not limited to, royalties

[4] § 12-11-20 ("A tax is imposed upon every bank engaged in business in the [s]tate which shall be levied, collected[,] and paid annually with respect to the entire net income of the taxpayer . . . computed at the rate of [4.5%] . . . .").

> from patents, copyrights, trademarks, and trade names;
>
> (4) net gain from the sale of property used in the trade or business. For purposes of this subsection, property used in the trade or business means property subject to the allowance for depreciation, real property used in the trade or business, and intangible property used in the trade or business which is:
>
> > (a) not property of a kind that properly would be includible in inventory of the business if on hand at the close of the taxable year; or
> >
> > (b) held by the business primarily for sale to customers in the ordinary course of the trade or business;
>
> (5) receipts from services if the entire income-producing activity is within this [s]tate. If the income-producing activity is performed partly within and partly without this [s]tate, sales are attributable to this [s]tate to the extent the income-producing activity is performed within this [s]tate . . . .

§ 12-6-2295(A)(1), (3) to (5).

"[T]he apportionment formula is a reasonable basis for establishing the income tax of corporations which . . . do business on a multistate level." *Eastman Kodak v. S.C. Tax Comm'n*, 308 S.C. 415, 419, 418 S.E.2d 542, 544 (1992) (citing *Covington Fabrics Corp. v. S.C. Tax Comm'n*, 264 S.C. 59, 212 S.E.2d 574 (1975)). "The obvious purpose of the apportionment formula is the determination of income from business activities within this [s]tate and is a proper subject for legislative action." *Covington Fabrics*, 264 S.C. at 66, 212 S.E.2d at 577. "The method of apportionment applicable to any particular taxpayer depends upon the nature of the taxpayer's business in this state." *DIRECTV*, 421 S.C. at 71, 804 S.E.2d at 639. "Although exactness in apportionment is desirable, all that is

required is a reasonable approximation." *Covington Fabrics*, 264 S.C. at 66, 212 S.E.2d at 577.

A. Mortgage Receipts

1. Mortgage Servicing Fees

The ALC determined U.S. Bank's mortgage servicing fees generated income from services and found its income-producing activities are performed in South Carolina. U.S. Bank argues its income-producing activities consist of processing monthly payments, facilitating the payment of taxes and insurance, and managing collection activities, all of which it performs entirely outside of the state.

U.S. Bank only earns mortgage servicing fees when it sells a mortgage to a third party. In this relationship, its customer is the government-sponsored entity and U.S. Bank provides assistance to manage the mortgage. U.S. Bank insists the plain language of section 12-6-2295(A)(5) requires looking directly at the activity of the taxpayer, so the location it operates within determines its apportionment. We disagree and hold the ALC's finding that the income-producing activity for these fees takes place within South Carolina is supported by substantial evidence.

When examining income-producing activity in *DIRECTV*, this court first interpreted section 12-6-2295, applying a de novo standard of review. 421 S.C. at 72-73, 804 S.E.2d at 640. This court then evaluated DIRECTV's income-producing activity and determined "substantial evidence support[ed] the ALC's finding that DIRECTV's [income-producing activity wa]s the delivery of [its] signal to its customers nationwide." *Id.* at 75, 804 S.E.2d at 641. Thus, we follow suit in reviewing the ALC's application of section 12-6-2295 de novo. And we review the ALC's finding as to U.S. Bank's income-producing activities to determine whether it is supported by substantial evidence. *See* § 1-23-610(B).

Here, U.S. Bank's attempt to pose this question as a matter of statutory interpretation is misguided. No aspect of section 12-6-2295(A)(5) is in dispute with respect to U.S. Bank's mortgage servicing fees. Thus, the only issue left for us to review is whether its income-producing activity is performed within South Carolina. In ruling on U.S. Bank's motion to reconsider, the ALC found that each of the income-producing activities related to mortgage servicing fees is performed by U.S. Bank employees located outside of South Carolina but that its conduct is directed into South Carolina and relies on an inextricable nexus with the South Carolina-based mortgage. Substantial evidence supports this finding. U.S. Bank's

classification of its income-producing activity as "processing monthly payments, facilitating the payment of taxes, and managing any necessary collections activities" demonstrates that each activity produces income because the activity is directed into the state. At the end of each activity performed by U.S. Bank is real property located in South Carolina owned by South Carolina borrowers, and this determination is supported by the testimonies of U.S. Bank's and the Department's experts. Thus, the apportionment of receipts by the Department reasonably represents U.S. Bank's business activity from mortgage servicing within the state and substantial evidence supports the ALC's finding. *See DIRECTV*, 421 S.C. at 77, 804 S.E.2d at 643 (noting the policy behind South Carolina's apportionment statutes is to include a fraction of the taxpayer's income *reasonably attributable* to its business activity in the state).

2. Mortgage Interest

U.S. Bank argues its mortgage interest income should be sourced as a service and it only produces income from mortgage interest for lending funds and performing ongoing financial services for its loans. The Department agreed with the ALC that mortgage interest income results from the use of an intangible and should be sourced to the extent that intangible is used within the state. The ALC found the intangible is used within the state because income is generated when U.S. Bank extends a loan to South Carolina borrowers. We agree.

Initially, U.S. Bank contends that we must look to the usual dictionary meaning of the terms "service" and "intangible property" to apply section 12-6-2295. It relies on *Jack's Custom Cycles, Inc. v. South Carolina Department of Revenue*, to assert that "[w]here a word is not defined in a statute, our appellate courts have looked to the usual dictionary meaning to supply its meaning." 439 S.C. 35, 43, 885 S.E.2d 433, 437 (Ct. App. 2023) (quoting *Lee v. Thermal Eng'g Corp.*, 352 S.C. 81, 91-92, 572 S.E.2d 298, 303 (Ct. App. 2002)). But in that case, the term at issue was undefined in the relevant title. *See id.*

The sourcing statute includes "receipts from the use of intangible property in this [s]tate including, but not limited to, royalties from patents, copyrights, trademarks, and trade names" as apportionable income. § 12-6-2295(A)(3). Article 1 of Title 12, Chapter 6, "Definitions," defines intangible property and tangible property: tangible property "includes real property and corporeal personal property but does not include, money, bank deposits, shares of stock, bonds, credits, evidences of debt, choses in action, or evidences of an interest in property" while intangible property "means all property other than tangible property." S.C. Code Ann.

§ 12-6-30(11) to (12) (2014). "Service" is not specifically defined, so the dictionary definition may aid in determining the proper application of the statute. The dictionary defines service as "useful labor that does not produce a tangible commodity."[5]

Examining the language of the statute in conjunction with the definitions of Title 12, we conclude the legislature intended section 12-6-2295(A)(3) to encompass mortgage interest as income from the use of an intangible. Thus, U.S. Bank's South Carolina mortgage interest income is properly sourced as income from the use of intangible property.

U.S. Bank additionally argues that the ALC erred in finding its mortgage interest income resulted from use within the state. We disagree. The ALC found a mortgage is used at the location of the real property it secures. U.S. Bank failed to show substantial evidence supported finding its mortgage interest income resulted from the use of an intangible outside of the state. Further, substantial evidence from the Department's experts and U.S. Bank's records detailing the mortgages, in fact, were extended to secure property located in South Carolina supports the ALC's finding.

3. Gains on the Sale of Mortgages

U.S. Bank similarly argues the ALC erred by sourcing its gain on the sale of mortgages through subsection (A)(4) of section 12-6-2295 instead of subsection (A)(1). It asserts that to earn income from selling pooled mortgages, it merely performs services like pricing the loans and selecting loans to pool into mortgage-backed securities or bonds. Given that U.S. Bank sold approximately 95% of its South Carolina loans to government-sponsored entities and each government-sponsored entity is located outside the state, U.S. Bank submits that applying subsection (A)(4) using the Department's method would render subsection (A)(1) superfluous.

The Department argues that the gain from the sale of South Carolina mortgages should be sourced to South Carolina because the real property securing the mortgage loan is located in the state. The ALC concluded that for income tax purposes, and therefore, the bank tax, a mortgage is intangible property. The applicable provision of section 12-6-2295 includes as sales and gross receipts:

---

[5] *Service*, *Merriam-Webster's Collegiate Dictionary* (12th ed. 2026).

> net gain from the sale of property used in the trade or business. For purposes of this subsection, property used in the trade or business means property subject to the allowance for depreciation, real property used in the trade or business, and intangible property used in the trade or business which is:
>
> > (a) not property of a kind that properly would be includible in inventory of the business if on hand at the close of the taxable year; or
> >
> > (b) held by the business primarily for sale to customers in the ordinary course of the trade or business . . . .

§ 12-6-2295(A)(4).

Here, U.S. Bank's mortgage interest income is produced by the use of intangible property. The plain language of section 12-6-30(11) through (12) includes a mortgage as intangible property within Title 12. U.S. Bank uses this intangible property in its business by servicing and collecting interest income on its originated and actively held mortgages, and in most cases, by the sale of the mortgage. A mortgage is not of a kind properly included in inventory, such as merchandise or other personal property. U.S. Bank holds its South Carolina mortgages primarily for sale to customers in the ordinary course of business, as evidenced by its sale of 95% of mortgages to government-sponsored entities. Thus, the plain language of subsection (A)(4) of section 12-6-2295 includes receipts from U.S. Bank's gains on the sale of mortgages, provided the mortgages are used in the state. We hold substantial evidence supports the ALC's finding that a mortgage is "used" by U.S. Bank at the location of the real property securing the mortgage. The Department's experts' testimonies combined with U.S. Bank's substantial records detailing its business activity within the state support this conclusion.

B. Credit Card Receipts

1. Credit Card Interest and Fees

U.S. Bank similarly asserts the ALC erred in sourcing its credit card interest and fees as a receipt from intangibles. It argues the ALC erred by concluding its credit

card income was earned by creating "accounts receivables that fall into the definition of intangible property for purposes of South Carolina's income tax." Additionally, U.S. Bank maintains the ALC erred by using the *Black's Law Dictionary* definition of accounts receivable to arrive at that conclusion. We agree.

The ALC used a definition of "accounts receivable" from *Black's Law Dictionary* (5th ed. 1979). The ALC's reliance on the usual dictionary definition of accounts receivable is misplaced. The term "accounts receivable" is absent from the statute the ALC applied to source U.S. Bank's income. *See* § 12-6-2295(A)(3). The canons of statutory interpretation permit using the dictionary meaning when presented with an undefined term. *See Jack's Custom Cycles*, 439 S.C. at 43, 885 S.E.2d at 437. But applying a usual dictionary definition to work backwards into the language of a statute does not comport with our canons of statutory interpretation. Further, applying this interpretation of accounts receivable to subsection (A)(3) of section 12-6-2295 would both lead to an absurd result and render subsection (A)(5) of section 12-6-2295 superfluous.[6] *See Senate ex rel. Leatherman v. McMaster*, 425 S.C. 315, 322, 821 S.E.2d 908, 912 (2018) ("[W]e must read the statute so 'that no word, clause, sentence, provision or part shall be rendered surplusage, or superfluous' . . . ." (quoting *CFRE, LLC v. Greenville Cnty. Assessor*, 395 S.C. 67, 74, 716 S.E.2d 877, 881 (2011))). Therefore, we modify this portion of the ALC's order to exclude treatment of U.S. Bank's income from credit card interest and fees as receipts from intangibles because the plain language of the statute and our canons of statutory interpretation cannot support this conclusion.

We further conclude subsection (A)(5) encompasses U.S. Bank's receipts from credit card interest and fees. U.S. Bank's income earned from credit card interest and fees derives from its services rendered within a network of financial institutions to offer its cards to customers. We, however, agree with the ALC's alternate determination that the income-producing activity resulting from its service takes place within the state. *See* Rule 220(c), SCACR ("The appellate court may affirm any ruling, order, decision or judgment upon any ground(s) appearing in the Record on Appeal.").

---

[6] U.S. Bank aptly pointed out this interpretation would include all accounts receivable on the books of any business. Additionally, the definition would include any service rendered in advance of payment, a category encompassed by the plain language of subsection (A)(5).

In *DIRECTV*, this court rejected the argument the activities that corporate taxpayer engaged in "for the production of its programming and marketing" were the activities that generated its income for the purposes of subsection (A)(5). 421 S.C. at 77, 804 S.E.2d at 643. This court held these activities were preparatory activities that it performed "'in anticipation' of customers signing up for [its] services" and were therefore income-anticipatory rather than income-producing activities. *Id.* at 77-78, 804 S.E.2d at 643. This court thus concluded substantial evidence supported the ALC's conclusion that the taxpayer's primary income-producing activity was "the delivery of the signal to the customer *because this activity actually generates income for DIRECTV*." *Id.* at 78, 804 S.E.2d at 643 (emphasis added).

U.S. Bank incorrectly characterizes its income-anticipatory activities as income-producing activities. Arranging the payment of late fees, operating a rewards program, and facilitating balance transfers are not the services U.S. Bank's customers pay for and that ultimately generate income. Substantial evidence supports the ALC's determination that when a customer pays interest and fees related to a credit card, the customer is paying for the extension of credit and thus, the ability to spend money now and pay later. Ultimately, a consumer's use of a credit card in the state is the activity that produces income for U.S. Bank. Its activities above and beyond facilitating card payments, or to remain competitive within the industry, are merely preparatory or ancillary to its income-producing activity. *See DIRECTV*, 421 S.C. at 78, 804 S.E.2d 643 ("While the other activities occurring prior to the delivery of signal are important for DIRECTV in that it can lead to income, section 12-6-2295(A)(5) requires activities that actually produce income.").

2. Interchange Fees

U.S. Bank argues that its income-producing activities to earn interchange fees are the routing, processing, and funding of transactions. It maintains that its performance of these activities occurs entirely outside of South Carolina. It asserts the ALC's conclusion that U.S. Bank sends approval or disapproval decisions to the merchant's location is unsupported by substantial evidence because those decisions are sent to merchant processors, not the location of the actual transaction. Thus, its only income-producing activities are performed entirely out of state. We disagree.

Substantial evidence supports the ALC's finding that "[t]o the extent U.S. Bank's merchants are located in South Carolina, therefore, the primary income-producing

activity as it relates to merchant interchange fees occurs in South Carolina." The record reflects the initiation of a credit card transaction combined with the ultimate funding of the transaction is the activity that generates income for U.S. Bank. Although the routing, processing, and funding activities that take place outside the state may help facilitate this process, the merchants located in this state, prompted by consumers acting in the state, generate U.S. Bank's interchange and merchant fee income. U.S. Bank's characterization of its income-producing activities stops the analysis short of its activities that produce income. The true income-producing activity occurs from the ultimate effect of U.S. Bank enabling each credit card transaction in South Carolina.

II. Penalties

U.S. Bank argues the ALC upheld the substantial understatement penalties in error because the exclusion of receipts from its mortgage and credit card operations is based on substantial authority and alternatively, is based upon a reasonable cause construction reached in good faith. U.S. Bank asserts it relied on substantial authority by operating from a "well-reasoned construction of the applicable statutory provision." U.S. Bank asserts the ALC erred in relying on the Department's "longstanding administrative practice of sourcing receipts to the borrower's location" because none of the administrative guidance the Department points to was issued until after the enactment of the sourcing statute in 2007.

The Department claims U.S. Bank produced no authority supporting its contention the penalty amounts should be reduced. The Department submits U.S. Bank never contacted the Department to request guidance on sourcing, amended its returns, or complied with existing law provided by *DIRECTV*. The Department asserts U.S. Bank's treatment of income did not reasonably represent its business activity within the state, regardless of the sourcing statute's application. We agree. The assessed penalties are both proper and required by statute.

The penalty provisions apply equally to the bank tax and are mandatory in situations of an understatement greater than 25% of the taxpayer's amount owed under the following provisions:

> (A) Except as otherwise provided, the civil penalties imposed by this penalty section apply to every revenue or tax law of the [s]tate that provides for the filing with the department of a return or statement of the tax or the amount taxable.

> (B) The penalties described in this section *must be added to* and become a part of and collected as the tax imposed by the revenue or tax laws of this [s]tate.
>
> (C)(1) In the case of failure to file a return on or before the date prescribed by law, determined with regard to any extension of time for filing, *there must be added* to the amount required to be shown as tax on the return, *a penalty* of five percent of the amount of the tax if the failure is for not more than one month, with an additional five percent for each additional month or fraction of the month during which the failure continues, not exceeding twenty-five percent in the aggregate.

S.C. Code Ann. § 12-54-43(A) to (C)(1) (2014) (emphases added). "Unless otherwise specifically prohibited, the department may waive, dismiss, or reduce penalties provided for in this chapter." S.C. Code Ann. § 12-54-160 (2014).

When examining the apportionment statutes, "the statutory policy is designed to apportion to South Carolina a fraction of the taxpayer's total income *reasonably attributable* to its business activity in this [s]tate." *Duke Energy Corp. v. S.C. Dep't of Revenue*, 415 S.C. 351, 356, 782 S.E.2d 590, 592 (2016) (quoting *Emerson Elec. Co. v. S.C. Dep't of Revenue*, 395 S.C. 481, 485-86, 719 S.E.2d 650, 652 (2011)).

The record contains substantial evidence demonstrating U.S. Bank's exclusion of all receipts from its mortgage and credit card operations was an unreasonable approximation of its business activity in the state. Like *DIRECTV*, U.S. Bank's customers pay to use its mortgages to secure property in the state, maintain mortgage requirements in the state, or to conduct transactions in the state and its returns were required to include a reasonable approximation of such business activities. U.S. Bank failed to identify substantial authority or reasonable cause for its initial exclusion of the disputed receipts or that its amended returns represented a reasonable approximation of its business activity within the state. At any point, U.S. Bank could have requested clarification from the Department regarding its apportionment method instead of facing mandatory penalties that may only be waived or reduced at the discretion of the Department.

Accordingly, although the ALC found U.S. Bank acted in good faith, the ALC did not find a reasonable cause for U.S. Bank's underpayment. Therefore, in accordance with our standard of review, we affirm the ALC's amended order regarding substantial understatement penalties.

CONCLUSION

Based on the above, we conclude substantial evidence in the record supports the ALC's findings that U.S. Bank's income-producing activities performed for its mortgage and credit card receipts took place within South Carolina. Although we modify which subsection of section 12-6-2295 applies to U.S. Bank's credit card interest and fees, the ALC correctly apportioned the six income streams into U.S. Bank's gross-receipts ratio. Additionally, we affirm the ALC's assessment of underpayment penalties because U.S. Bank failed to demonstrate a reasonable cause for underpayment. Accordingly, the ALC's decision is

AFFIRMED AS MODIFIED.

WILLIAMS, C.J., and VINSON, J., concur.