

FEDERAL TAX CONFORMITY

TAX YEAR 2017 AND 2018

PRESENTED TO

HOUSE WAYS AND MEANS
INCOME TAX SUBCOMMITTEE

April 17, 2018

South Carolina Revenue and Fiscal Affairs Office

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CONFORMITY

Tax Year 2017 and 2018

- Conformity is more complicated due to major federal tax reform
- Winners and losers
 - Detailed RFA report on federal tax changes:
Estimated South Carolina Impact of Federal “Tax Cuts and Jobs Act” of 2017 (<http://rfa.sc.gov/econ/reports/econanalysis>)
- Taxpayers, tax professionals, and DOR need time for implementation of tax changes



CONFORMITY - RETROACTIVE Tax Year 2017 (April 2018 filings)

- Conforming to federal tax changes for tax year 2017 will allow taxpayers under 65 to claim higher medical deductions: \$3.5 million revenue reduction
- Twelve tax provisions extended in the Bipartisan Budget Act affect taxpayers for 2017
 - Total of \$11.8 million including:
 - Medical deductions for taxpayers over 65 (\$4.8 M)
 - Qualified tuition and related expenses (\$2.8 M)
- Current filers will have to file amended returns if these provisions are adopted



CONFORMITY

Tax Year 2018 (April 2019 Filings)

Adopt Federal Income Tax Changes

- Simplest for taxpayers and least likely to result in non-compliance
- No changes to tax processing or revenue flow

BUDGET/REVENUE ISSUES

**\$205 Million Revenue Increase*
(\$180 Individ.; \$25 Corp.)**

For Individual Tax Filers:

- **Decreased Tax Liability:
31%**
- **Increased Tax Liability:
27%**
- **Unchanged Tax Liability:
42%**

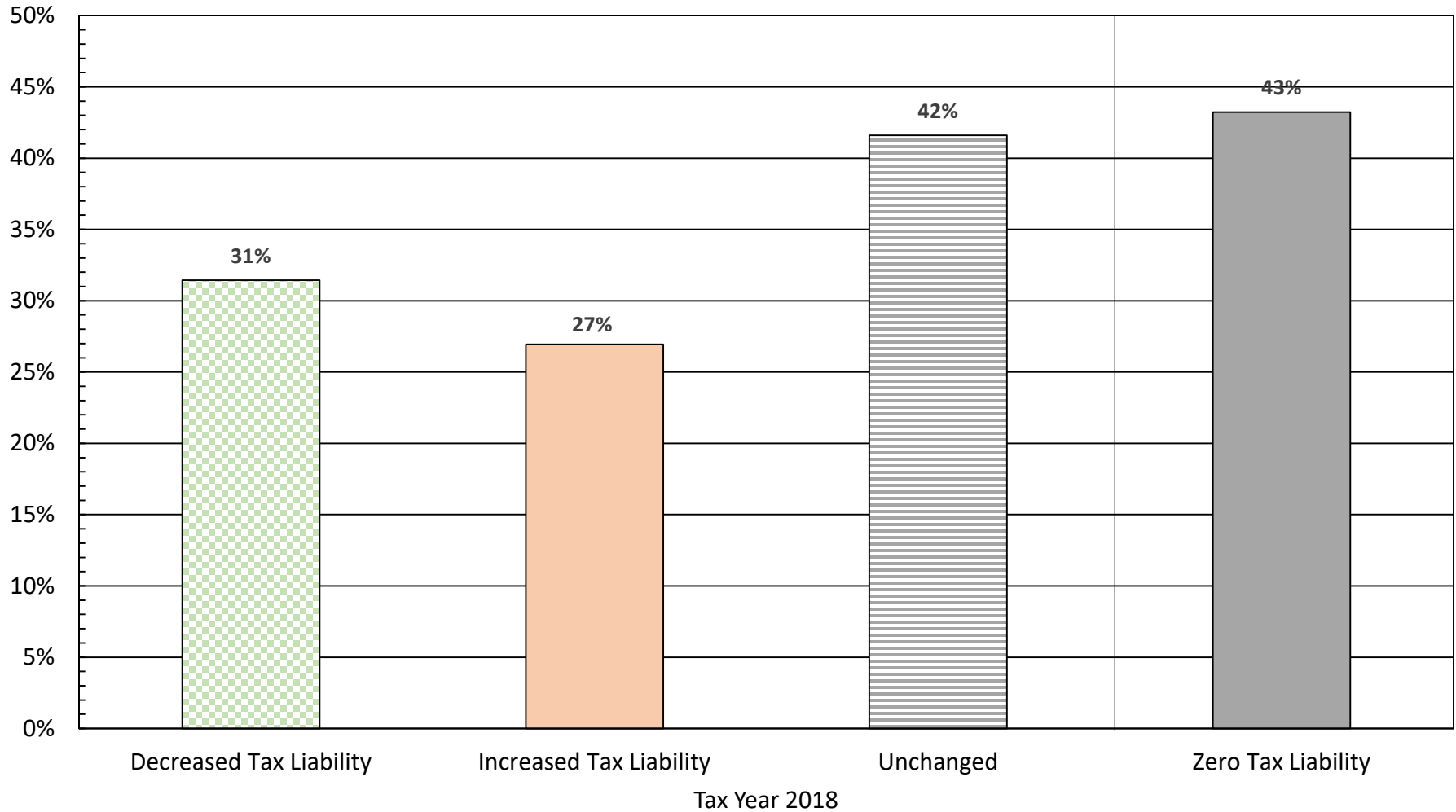
***Before any state tax reform**



SOUTH CAROLINA STATE INDIVIDUAL INCOME TAX LIABILITY IMPACT

Tax Year 2018 - Projected Impact of Federal Tax Changes

Percentage of Returns



NONCONFORMITY

No Action (Maintain 2016 Tax Code)

Decouple from Federal Tax Code

- Significant change for taxpayers, tax professionals, and DOR
- Potential for unintended tax liability impacts
- Taxpayers must follow two sets of tax laws

BUDGET/REVENUE ISSUES

Unknown Impacts on Compliance

- Voluntary Compliance
 - Taxpayer confusion may have unintended revenue effects
- Involuntary Compliance
 - Tens of millions in audit revenue affected
- Short Time for Implementation
 - Processing Delays - revenue timing and budget cash flow would be affected, especially if electronic filings are affected



NONCONFORMITY - SPECIFIC CONCERNS

Tax Year 2018 Issues for Taxpayers

- Federal and state tax law differences
 - Significant differences between federal and state standard deductions and personal exemptions may affect compliance
 - Different thresholds for medical deductions
- Taxpayers will need to follow two sets of tax rules and complete another set of forms to duplicate federal returns under old law
 - Individuals and business may have much higher tax preparation expenses. For example, Indiana estimates their businesses' expenses will increase by \$100 million.¹
- Delays in processing would mean taxpayers would have to wait to receive refunds

¹ *Indianapolis Business Journal*, March 23, 2018 <https://www.ibj.com/articles/68093-without-state-fix-federal-tax-change-could-cost-indiana-firms-100m>



EFFECTS OF TAX CONFORMITY OR NONCONFORMITY

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ISSUES FOR TAXPAYERS

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