



SOUTH CAROLINA REVENUE AND FISCAL AFFAIRS OFFICE

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FRANK A. RAINWATER
Executive Director

September 28, 2018

Mr. W. Hartley Powell
Director
South Carolina Department of Revenue
P.O. Box 125
Columbia, SC 29214

Dear Mr. Powell:

This letter is to provide you with our estimates for the income tax credit for preventative maintenance on a motor vehicle pursuant to Section 12-6-3780. These estimates update our analysis provided in the fiscal impact statement for H. 3516 to include the latest data available.

This statute allows a resident taxpayer to claim a refundable income tax credit for preventive vehicle maintenance on private passenger motor vehicles as defined in Section 56-3-630, including motorcycles, registered in this state. The credit may not exceed the lesser of the resident's actual motor fuel user fee increase incurred as a result of the increases imposed in Section 12-28-310(D) or the amount the resident pays for vehicle maintenance. Vehicle maintenance includes, but is not limited to, costs incurred for new tires, oil changes, and regular vehicle maintenance. A taxpayer may claim the credit for up to two qualifying vehicles. Total credits are limited to a maximum by tax year, which is \$40,000,000 for 2018.

The Revenue and Fiscal Affairs Office is required to estimate the number of taxpayers expected to claim the credit for each tax year and the total amount expected to be claimed annually on or before September 30th. In the event that RFA estimates that the total credits claimed will exceed the maximum amount of the aggregate credit allowed, RFA shall certify to the Department of Revenue (DOR) the pro rata adjustment to the credit.

We have reviewed DOR's preliminary guidance for the credit and have incorporated it into our analysis. Our estimates depend on identifying the number of vehicles that will qualify for the credit, estimating the average gallons to be claimed, the total amount of

credits, and then determining the pro rata adjustment necessary to ensure that the total amount of credits does not exceed the limit.

Number of Taxpayers and Qualifying Vehicles

While we do not have sufficient data that identifies the number of resident taxpayers who own qualifying vehicles, Census data for 2016 indicate that 6.3 percent of South Carolina households have no vehicles and would be ineligible for the tax credit. Therefore, our best estimate would be to assume that 93.7 percent of all resident taxpayers, both individuals and business, would own one or more vehicles and qualify for the tax credit.

While the statute references the number of taxpayers, our analysis relies on an estimate of the expected number of qualifying vehicles. We anticipate that information will allow us to estimate more accurately the total dollar amount of credits claimed and any pro rata adjustment. Private passenger motor vehicle as defined in Section 56-3-630 includes every motor vehicle designed, used, and maintained for the transportation of ten or fewer persons and trucks with an empty weight of nine thousand pounds or less and a gross weight of eleven thousand pounds or less. This credit also specifically includes motorcycles and will include mopeds as of November 19, 2018. Based upon August 2018 data from DMV on registered vehicles, we have estimated the number of vehicles expected to qualify to be 4,166,770. We have excluded vehicles owned by governments that would not pay taxes and not be eligible for the credit, trucks that are over the weight limitations, buses, and trailers.

Further, each taxpayer may claim the credit for up to two vehicles. We have assumed based upon discussions with DOR that a joint return includes two taxpayers who may each claim the credit for two vehicles, for a total of four vehicles. Single and separate filers will be limited to a credit for two vehicles each. To account for households with more vehicles than can be claimed, we used the U.S. Census Bureau's 2016 American Community Survey data on the number of household vehicles by household size to estimate the percentage of vehicles that will be ineligible for the credit. Based upon this data, approximately 2.7 percent of vehicles will be ineligible, thereby reducing the number of motor vehicles expected to qualify to 4,054,267.

A weakness of this approach is that the DMV registration data do not indicate if owners meet the residency requirements necessary to claim the credit. Additionally, we use household vehicle ownership to estimate the number of vehicles that will be ineligible based upon the two vehicle limit, and this approach may over or under state ownership of excess vehicles, particularly for businesses. Regardless, we anticipate that the estimated 4,044,051 qualifying vehicles is the best forecast given the available data.

Total Amount of Credits Claimed

The credit may not exceed the actual motor fuel user fee increase incurred as a result of the increase in Section 12-28-310(D) or actual maintenance expenses. Section 12-28-310(D) increases the current \$0.16 per gallon motor fuel user fee by \$0.02 per gallon per year for six years for a total increase of \$0.12 per gallon of fuel. The first increase occurred July 1, 2017, and will continue each July 1 thereafter until July 1, 2023.

However, the credit must be claimed for increases incurred on a tax year basis beginning for tax year 2018 and continuing until tax year 2022. Therefore, we have estimated the motor fuel increase based upon one-half of the increase for each fiscal year. The increase was \$0.02 for January through June of 2018 and then \$0.04 for July through December, resulting in an average increase of \$0.03 in 2018.

To estimate motor fuel purchases, we use the U.S. Department of Transportation, Federal Highway Administration, Highway Statistics reports from 2012 to 2016. In the most recent 2016 report, average annual gallons usage increased slightly. When factored into our projections, this change increases our estimated number of gallons for 2018 from 513 gallons to 519 gallons. While usage has moved up and down, the average declined by 0.3 percent over the period. Based upon federal regulations requiring improvements in fuel economy under Corporate Average Fuel Economy (CAFE) standards, we expect the trend toward improvements in fuel efficiency will continue to reduce average usage long-term and have used this growth rate to project future average gasoline gallons used.

The estimated average credit is calculated by multiplying the tax year average motor fuel fee increase of \$0.03 times the estimated average annual gallons purchased of 519 to yield an average credit of amount of \$15.57. We anticipate that all taxpayers will incur maintenance expenses of at least \$15.57 annually and that the credit amount would be limited by the motor fuel increase incurred. Multiplying the average credit amount of \$15.57 by the estimated 4,054,267 vehicles yields total credits of \$63,068,000.

Pro Rata Adjustment

Based upon these projections, we anticipate that taxpayers will claim the total allowable \$40,000,000 for tax year 2018 for all qualifying vehicles. We further calculate that a pro rata adjustment of 63.4 percent must be applied to reduce the total credits claimed to the allowable \$40,000,000.

Potential General Fund Revenue Impact

In Section 12-6-3780, the Department of Transportation (DOT) is required to transfer sufficient funds to DOR by January 31st to offset the estimated total credits. If the credit claimed by all taxpayers in a tax year is less than the amounts transferred, then the excess reverts to DOT. This situation could occur if taxpayers fail to retain receipts during the year and do not claim the credit. In this case, an adjustment of 63.4 percent

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may result in fewer total credits claimed in this first year. However, the estimates provided anticipate that taxpayers will comply with the record keeping requirements of the statute and claim the appropriate credits.

Conversely, the statute does not specify a funding source if credits exceed the \$40,000,000 transfer. Since the credit is taken on income tax returns, we anticipate that any excess would reduce General Fund revenue through increased income tax refunds or decreased paid with returns.

While we have estimated a pro rata adjustment to reduce the credits claimed, with your assistance, we will monitor the total claimed during the fiscal year for any potential General Fund impact.

If I may be of further assistance, please advise.

Sincerely,



Frank A. Rainwater

FAR/lhj

cc: Mr. Meredith Cleland, Department of Revenue