



**SOUTH CAROLINA REVENUE AND FISCAL AFFAIRS OFFICE**  
**STATEMENT OF ESTIMATED FISCAL IMPACT**  
 (803)734-0640 • RFA.SC.GOV/IMPACTS

---

Bill Number: H. 3147 Updated for Revised Analysis and Additional Revenue Impact  
 Author: G. M. Smith  
 Requestor: House Ways and Means  
 Date: May 14, 2015  
 Subject: Taxable income deductions  
 RFA Analyst(s): Shuford and Shealy

---

**Estimate of Fiscal Impact**

	<b>FY 2015-16</b>	<b>FY 2016-17</b>	<b>FY 2017-18</b>
<b>State Expenditure</b>			
General Fund	Minimal	N/A	N/A
Other and Federal	N/A	N/A	N/A
Full-Time Equivalent Position(s)	0.00	0.00	0.00
<b>State Revenue</b>			
General Fund	(\$11,241,160)	(\$23,447,280)	(\$36,692,254)
Other and Federal	N/A	N/A	N/A
<b>Local Expenditure</b>	N/A	N/A	N/A
<b>Local Revenue</b>	N/A	N/A	N/A

**Fiscal Impact Summary**

This legislation will have a minimal expenditure impact from revising forms and instructions. The Department of Revenue will have some additional General Fund expenditures that can be absorbed within their current funding.

This bill would reduce General Fund individual income tax revenue by an estimated \$11,241,160 in FY 2015-16, the first year of the three-year phase-in. The total reduction in General Fund individual income tax revenue in FY 2016-17 with the 66.66 percent deduction is an estimated \$23,447,280. In the final year with the 100 percent deduction, the total reduction in General Fund individual income tax revenue is an estimated \$36,692,254 for FY 2017-18.

**Explanation of Fiscal Impact**

**State Expenditure**

This bill provides a deduction from South Carolina taxable income of individuals for retirement benefits attributable to service on active duty in the Armed Forces of the United States.

The Department of Revenue estimates that this legislation will have a minimal expenditure impact on the department from revising forms and instructions. The department will have some additional General Fund expenditures that can be absorbed within their current funding.

## State Revenue

### **Updated on May 14, 2015 to Include Revised Analysis and Additional Revenue Impact**

Sections 2 and 4 of this bill allows a deduction of military retirement benefits attributable to service on active duty in the Armed Forces of the United States for taxable years beginning after 2014 from South Carolina taxable income. This deduction is phased-in over three years, with the deduction being 33.33 percent in tax year 2015. The deduction increases to 66.66 percent in tax year 2016 and reaches 100 percent in tax year 2017.

Based on the latest data from the U.S. Department of Defense, Office of the Actuary, there were 57,755 military retirees in South Carolina as of September 2013 receiving \$1,361,388,000 in annual military retirement benefits. This equates to an average annual retirement benefit of \$23,572 for each retiree in South Carolina.

Since Section 12-6-1170 allows different amounts of retirement income deductions by taxpayers depending on their age, we use Department of Defense data to segregate these taxpayers into two categories: age 65 and older and under age 65. Taxpayers age 65 and older may deduct retirement income of up to \$15,000 per year, while taxpayers under age 65 may deduct retirement income up to \$3,000 per year.

Adjusting the number of South Carolina military retirees and their retirement income in tax year 2013 to tax year 2015, or FY 2015-16, we anticipate 30,450 taxpayers age 65 or older with military retirement income totaling \$798,214,000. This results in an average \$26,214 annual military retirement benefit. After accounting for the current \$15,000 deduction and any non-taxable retirement income such as disability payments, we estimate that the remaining \$323,210,000 in taxable retirement benefits at an average tax rate of 2.9 percent would generate \$9,373,090 in individual income tax revenue in FY 2015-16. Adjusting this amount for the 33.33 percent deduction allowed in tax year 2015 results in an estimated \$3,124,051 reduction in General Fund individual income tax revenue in FY 2015-16.

We also anticipate 28,717 taxpayers under age 65 with military retirement income totaling \$665,618,000, resulting in an average \$23,179 annual military retirement benefit. After accounting for the current \$3,000 deduction and any non-taxable retirement income such as disability payments, we estimate that the remaining \$557,536,000 in taxable retirement benefits multiplied by an average tax rate of 3.4 percent will generate \$18,956,224 in individual income tax revenue in FY 2015-16. Adjusting this amount for the 33.33 percent deduction allowed in tax year 2015 results in an estimated \$6,318,109 reduction in General Fund individual income tax revenue in FY 2015-16.

The average tax rates used in this analysis are based on a re-calculation of the income tax for each return after the proposed deduction is applied. This method takes into account the large number of returns that have zero taxable income, returns that are reduced to zero taxable income by the deduction, and returns that do not benefit from the full amount of the proposed deduction. The tax rates for the two age groups are different because the larger deduction for age 65 and older further reduces remaining South Carolina income subject to tax.

Combining the revenue impact for these two age groups results in an estimated \$9,442,160 reduction in General Fund individual income tax revenue in FY 2015-16, the first year of the three-year phase-in. The total reduction in General Fund individual income tax revenue in FY 2016-17 with the 66.66 percent deduction is an estimated \$19,698,280. In the final year with the 100 percent deduction, the total reduction in General Fund individual income tax revenue is an estimated \$30,832,254 for FY 2017-18.

The revised analysis and additional revenue impact in this updated fiscal impact statement is from our reexamination of Section 3 that amends Section 12-6-1170(A)(2) for taxable years after 2016 to exclude military retirement income for purposes of the deduction allowed by this section. Section 12-6-1170 allows different amounts of retirement income deductions by taxpayers depending on their age. Significant to this analysis is Section 12-6-1170(B), which states that a taxpayer aged 65 and older is allowed a \$15,000 deduction from South Carolina taxable income reduced by the \$10,000 retirement income deduction. This proposed amendment in Section 12-6-1170(A)(2) would allow taxpayers aged 65 and older to deduct up to the \$15,000 amount allowed without subtracting \$10,000 of military retirement income that will no longer be taxable. This results in an increase in the revenue impact of this bill from our original estimate. Based on data compiled by the Revenue and Fiscal Affairs Office from a Department of Revenue sample of 2012 federal and state matched returns, we estimate that the 30,450 taxpayers age 65 or older with military retirement income in tax year 2016 would be allowed to deduct an additional \$186,088,000 of South Carolina taxable income compared to the current statute. At an average tax rate of 2.9 percent, this would reduce General Fund individual income tax revenue by \$5,397,000. Adjusting this amount for the 33.33 percent deduction allowed in tax year 2015 results in an estimated \$1,799,000 reduction in General Fund individual income tax revenue in FY 2015-16. By FY 2017-18, these additional deductions are expected to total \$202,064,413 and reduce General Fund individual income tax revenue by \$5,860,000 when the deduction reaches 100 percent.

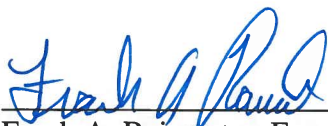
Combining the revenue impacts of the military retirement deduction and the revision to the maximum \$15,000 deduction allowed in Section 3 of the bill results in an estimated \$11,241,160 reduction in General Fund individual income tax revenue in FY 2015-16, the first year of the three-year phase-in. The total reduction in General Fund individual income tax revenue in FY 2016-17 with the 66.66 percent deduction is an estimated \$23,447,280. In the final year with the 100 percent deduction, the total reduction in General Fund individual income tax revenue is an estimated \$36,692,254 for FY 2017-18.

**Local Expenditure**

N/A

**Local Revenue**

N/A



Frank A. Rainwater, Executive Director