



SOUTH CAROLINA REVENUE AND FISCAL AFFAIRS OFFICE
STATEMENT OF ESTIMATED FISCAL IMPACT
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Bill Number: H. 3147
 Author: G. M. Smith
 Requestor: House Ways and Means
 Date: February 2, 2015
 Subject: Taxable income deductions
 RFA Analyst(s): Shuford and Shealy

Estimate of Fiscal Impact

	FY 2015-16	FY 2016-17	FY 2017-18
State Expenditure			
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
State Revenue			
General Fund	(\$9,442,160)	(\$19,698,280)	(\$30,832,254)
Other and Federal	N/A	N/A	N/A
Local Expenditure	N/A	N/A	N/A
Local Revenue	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 \$9,442,160 in FY 2015-16, the first year of the three year phase-in. In FY 2016-17 when the deduction increases to 66.66 percent, the additional revenue reduction is an estimated \$10,256,119. In the final year with the 100 percent deduction, the additional revenue reduction is an estimated \$11,133,974 in FY 2017-18 for an estimated total reduction in General Fund individual income tax revenue of \$30,832,254 over the three-year phase-in.

Explanation of Fiscal Impact

State Expenditure

A bill relating to deductions from South Carolina taxable income of individuals so as to allow a deduction of 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

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 individual income tax. This deduction is phased-in over three years with the deduction being 33.33 percent in tax year 2015. The deduction rises to 66.66 percent in tax year 2016 and reaches 100 percent in tax year 2017. This proposal would also amend Section 12-6-1170(A)(2) to modify the definition of "retirement income" that is subject to the \$3,000 or \$15,000 exclusion, depending on the age of the taxpayer, to not include military retirement income for taxable years beginning after 2016. This ensures that taxpayers cannot deduct military retirement benefits twice.

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 §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% 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% 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 total 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 attached tables report the total revenue reduction by fiscal year for all military retirees and by the two age groups, age 65 and older and below age 65, discussed above.

Local Expenditure

N/A

Local Revenue

N/A



Frank A. Rainwater, Executive Director

Individual Income Tax Deduction for All Military Retirement Benefits

Department of Defense, Office of the Actuary Retirement Statistical Report Date	Fiscal Year	Total Number of Military Retirees	Growth in Number of Military Retirees	Total Annual Military Retirement Payments	Growth in Military Retirement Payments	Average Annual Military Retirement Payments	Annual Retirement Payments Deducted Under Current Law, Maximum \$3,000 or \$15,000 Depending on Age	Disability Payments (Not Taxable)	Growth in Disability Payments	Remaining Taxable Military Retirement Income	Current Tax on Remaining Taxable Military Retirement Income	Total Tax Revenue Reduction for Three Year Phase-in to 100% Military Retirement Reduction	Annual Tax Revenue Reduction for Three Year Phase-in to 100% Military Retirement Reduction
Sep-08	FY 2008-09	54,718		1,142,088,000		20,872	458,358,000	35,004,000		648,726,000	21,235,179		
Sep-09	FY 2009-10	55,433	1.31%	1,235,712,000	8.20%	22,292	466,455,000	37,020,000	5.76%	732,237,000	23,855,793		
Sep-10	FY 2010-11	55,878	0.80%	1,249,632,000	1.13%	22,364	474,306,000	36,912,000	-0.29%	738,414,000	24,039,156		
Sep-11	FY 2011-12	56,486	1.09%	1,266,108,000	1.32%	22,415	484,278,000	37,260,000	0.94%	744,570,000	24,220,305		
Sep-12	FY 2012-13	57,118	1.12%	1,323,996,000	4.57%	23,180	502,206,000	37,248,000	-0.03%	784,542,000	25,420,833		
Sep-13	FY 2013-14	57,755	1.12%	1,361,388,000	2.82%	23,572	516,729,000	38,544,000	3.48%	806,115,000	26,056,980		
Estimate	FY 2014-15	58,446	1.20%	1,411,450,000	3.68%	24,150	529,602,000	39,345,000	2.08%	842,503,000	27,165,882		
Estimate	FY 2015-16	59,167	1.23%	1,463,832,000	3.71%	24,741	542,906,000	40,180,000	2.12%	880,746,000	28,329,314	9,442,160	9,442,160
Estimate	FY 2016-17	59,918	1.27%	1,518,651,000	3.74%	25,345	556,650,500	41,050,000	2.17%	920,950,500	29,550,375	19,698,280	10,256,119
Estimate	FY 2017-18	60,702	1.31%	1,576,034,000	3.78%	25,964	570,852,000	41,956,000	2.21%	963,226,000	30,832,254	30,832,254	11,133,974

Individual Income Tax Deduction for Military Retirement Benefits for Retirees Age 65 and Older

Department of Defense, Office of the Actuary Retirement Statistical Report Date	Fiscal Year	Number of Military Retirees Age 65 and Older	Growth in Number of Military Retirees Age 65 and Older	Annual Retirement Payments	Growth in Military Retirement Payments	Average Annual Retirement Payments Age 65 and Older	Annual Retirement Payments Deducted Under Current Law, Maximum \$15,000	Disability Payments (Not Taxable)	Growth in Disability Payments	Remaining Taxable Military Retirement Income	Current Tax on Remaining Taxable Military Retirement Income	Total Tax Revenue Reduction for Three Year Phase-in to 100% Military Retirement Reduction	Annual Tax Revenue Reduction for Three Year Phase-in to 100% Military Retirement Reduction
Sep-08	FY 2008-09	24,517		550,488,000		22,453	367,755,000	18,432,000		164,301,000	4,764,729		
Sep-09	FY 2009-10	25,013	2.02%	602,592,000	9.47%	24,091	375,195,000	19,344,000	4.95%	208,053,000	6,033,537		
Sep-10	FY 2010-11	25,556	2.17%	616,116,000	2.24%	24,108	383,340,000	19,392,000	0.25%	213,384,000	6,188,136		
Sep-11	FY 2011-12	26,235	2.66%	630,888,000	2.40%	24,048	393,525,000	18,348,000	-5.38%	219,015,000	6,351,435		
Sep-12	FY 2012-13	27,571	5.09%	683,064,000	8.27%	24,775	413,565,000	18,780,000	2.35%	250,719,000	7,270,851		
Sep-13	FY 2013-14	28,622	3.81%	717,816,000	5.09%	25,079	429,330,000	18,300,000	-2.56%	270,186,000	7,835,394		
Estimate	FY 2014-15	29,522	3.14%	756,948,000	5.45%	25,640	442,830,000	18,274,000	-0.14%	295,844,000	8,579,476		
Estimate	FY 2015-16	30,450	3.14%	798,214,000	5.45%	26,214	456,756,000	18,248,000	-0.14%	323,210,000	9,373,090	3,124,051	3,124,051
Estimate	FY 2016-17	31,408	3.14%	841,729,000	5.45%	26,800	471,118,500	18,222,000	-0.14%	352,388,500	10,219,267	6,812,163	3,688,112
Estimate	FY 2017-18	32,396	3.14%	887,616,000	5.45%	27,399	485,934,000	18,196,000	-0.14%	383,486,000	11,121,094	11,121,094	4,308,931

The number of military retirees, annual retirement payments, and disability payments growth rates for FY 2014-15 to FY 2017-18 are estimated using the compound average growth rates from FY 2008-09 to FY 2013-14.

Individual Income Tax Deduction for Military Retirement Benefits for Retirees Below Age 65

Department of Defense, Office of the Actuary Retirement Statistical Report Date	Fiscal Year	Number of Military Retirees Below Age 65	Growth in Number of Military Retirees Below Age 65	Annual Retirement Payments	Growth in Military Retirement Payments	Average Annual Retirement Payments Below Age 65	Annual Retirement Payments Deducted Under Current Law, Maximum \$3,000	Disability Payments (Not Taxable)	Growth in Disability Payments	Remaining Taxable Military Retirement Income	Current Tax on Remaining Taxable Military Retirement Income	Total Tax Revenue Reduction for Three Year Phase-in to 100% Military Retirement Reduction	Annual Tax Revenue Reduction for Three Year Phase-in to 100% Military Retirement Reduction
Sep-08	FY 2008-09	30,201		591,600,000		19,589	90,603,000	16,572,000		484,425,000	16,470,450		
Sep-09	FY 2009-10	30,420	0.73%	633,120,000	7.02%	20,813	91,260,000	17,676,000	6.66%	524,184,000	17,822,256		
Sep-10	FY 2010-11	30,322	-0.32%	633,516,000	0.06%	20,893	90,966,000	17,520,000	-0.88%	525,030,000	17,851,020		
Sep-11	FY 2011-12	30,251	-0.23%	635,220,000	0.27%	20,998	90,753,000	18,912,000	7.95%	525,555,000	17,868,870		
Sep-12	FY 2012-13	29,547	-2.33%	640,932,000	0.90%	21,692	88,641,000	18,468,000	-2.35%	533,823,000	18,149,982		
Sep-13	FY 2013-14	29,133	-1.40%	643,572,000	0.41%	22,091	87,399,000	20,244,000	9.62%	535,929,000	18,221,586		
Estimate	FY 2014-15	28,924	-0.72%	654,502,000	1.70%	22,628	86,772,000	21,071,000	4.08%	546,659,000	18,586,406		
Estimate	FY 2015-16	28,717	-0.72%	665,618,000	1.70%	23,179	86,150,000	21,932,000	4.08%	557,536,000	18,956,224	6,318,109	6,318,109
Estimate	FY 2016-17	28,511	-0.72%	676,922,000	1.70%	23,743	85,532,000	22,828,000	4.08%	568,562,000	19,331,108	12,886,117	6,568,007
Estimate	FY 2017-18	28,306	-0.72%	688,418,000	1.70%	24,321	84,918,000	23,760,000	4.08%	579,740,000	19,711,160	19,711,160	6,825,043

The number of military retirees, annual retirement payments, and disability payments growth rates for FY 2014-15 to FY 2017-18 are estimated using the compound average growth rates from FY 2008-09 to FY 2013-14.