~~Indicates Matter Stricken~~

Indicates New Matter

COMMITTEE REPORT

April 23, 2015

**H. 3147**

Introduced by Reps. G.M. Smith, G.R. Smith, Huggins, Weeks, Taylor, Pope, Collins, Johnson, Stavrinakis and Yow

S. Printed 4/23/15--H.

Read the first time January 13, 2015.

**THE COMMITTEE ON WAYS AND MEANS**

To whom was referred a Bill (H. 3147) to amend Section 12‑6‑1140, as amended, Code of Laws of South Carolina, 1976, relating to deductions from South Carolina taxable income of individuals for purposes, etc., respectfully

**REPORT:**

That they have duly and carefully considered the same and recommend that the same do pass:

W. BRIAN WHITE for Committee.

**STATEMENT OF ESTIMATED FISCAL IMPACT**

**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.

**Individual Income Tax Deduction for All Military Retirement Benefits**

**Department**

**of Defense,**

**Office of the**

**Actuary Growth Growth Average**

**Retirement Total in Total Annual in Annual**

**Statistical Number Number Military Military Military**

**Report of Military of Retirement Retirement Retirement**

**Date Fiscal Year Retirees Military Payments Payments Payments**

Sep-08 FY 2008-09 54,718 **Retirees**  1,142,088,000   20,872

Sep-09 FY 2009-10 55,433 1.31% 1,235,712,000 8.20% 22,292

Sep-10 FY 2010-11 55,878 0.80% 1,249,632,000 1.13% 22,364

Sep-11 FY 2011-12 56,486 1.09% 1,266,108,000 1.32% 22,415

Sep-12 FY 2012-13 57,118 1.12% 1,323,996,000 4.57% 23,180

Sep-13 FY 2013-14 57,755 1.12% 1,361,388,000 2.82% 23,572

Estimate FY 2014-15 58,446 1.20% 1,411,450,000 3.68% 24,150

Estimate FY 2015-16 59,167 1.23% 1,463,832,000 3.71% 24,741

Estimate FY 2016-17 59,918 1.27% 1,518,651,000 3.74% 25,345

Estimate FY 2017-18 60,702 1.31% 1,576,034,000 3.78% 25,964

**Annual**

**Retirement**

**Payments**

**Deducted Total Tax Annual Tax**

**Under Revenue Revenue**

**Current Current Reduction Reduction**

**Law, Tax on for Three Year for Three Year**

**Maximum Remaining Remaining Phase-in Phase-in**

**$3,000 or Growth Taxable Taxable to 100% to 100%**

**$15,000 Disability in Military Military Military Military**

**Depending Payments Disability Retirement Retirement Retirement Retirement**

**on Age (Not Taxable) Payments Income Income Reduction Reduction**

458,358,000 35,004,000 648,726,000 21,235,179

466,455,000 37,020,000 5.76% 732,237,000 23,855,793

474,306,000 36,912,000 -0.29% 738,414,000 24,039,156

484,278,000 37,260,000 0.94% 744,570,000 24,220,305

502,206,000 37,248,000 -0.03% 784,542,000 25,420,833

516,729,000 38,544,000 3.48% 806,115,000 26,056,980

529,602,000 39,345,000 2.08% 842,503,000 27,165,882

542,906,000 40,180,000 2.12% 880,746,000 28,329,314 9,442,160 9,442,160

556,650,500 41,050,000 2.17% 920,950,500 29,550,375 19,698,280 10,256,119

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**

**Growth**

**Department in**

**of Defense, Number**

**Office of the Number of Average**

**Actuary of Military Military Growth Annual**

**Retirement Retirees Retirees in Retirement**

**Statistical Age 65 Age 65 Annual Military Payments**

**Report and and Retirement Retirement Age 65 and**

**Date Fiscal Year Older Older Payments Payments Older**

Sep-08 FY 2008-09 24,517   550,488,000   22,453

Sep-09 FY 2009-10 25,013 2.02% 602,592,000 9.47% 24,091

Sep-10 FY 2010-11 25,556 2.17% 616,116,000 2.24% 24,108

Sep-11 FY 2011-12 26,235 2.66% 630,888,000 2.40% 24,048

Sep-12 FY 2012-13 27,571 5.09% 683,064,000 8.27% 24,775

Sep-13 FY 2013-14 28,622 3.81% 717,816,000 5.09% 25,079

Estimate FY 2014-15 29,522 3.14% 756,948,000 5.45% 25,640

Estimate FY 2015-16 30,450 3.14% 798,214,000 5.45% 26,214

Estimate FY 2016-17 31,408 3.14% 841,729,000 5.45% 26,800

Estimate FY 2017-18 32,396 3.14% 887,616,000 5.45% 27,399

**Annual Total Tax Annual Tax**

**Retirement Revenue Revenue**

**Payments Current Reduction Reduction**

**Deducted Tax on for Three Year for Three Year**

**Under Remaining Remaining Phase-in Phase-in**

**Current Growth Taxable Taxable to 100% to 100%**

**Law, Disability in Military Military Military Military**

**Maximum Payments Disability Retirement Retirement Retirement Retirement**

**$15,000 (Not Taxable) Payments Income Income Reduction Reduction**

367,755,000 18,432,000   164,301,000 4,764,729

375,195,000 19,344,000 4.95% 208,053,000 6,033,537

383,340,000 19,392,000 0.25% 213,384,000 6,188,136

393,525,000 18,348,000 -5.38% 219,015,000 6,351,435

413,565,000 18,780,000 2.35% 250,719,000 7,270,851

429,330,000 18,300,000 -2.56% 270,186,000 7,835,394

442,830,000 18,274,000 -0.14% 295,844,000 8,579,476

456,756,000 18,248,000 -0.14% 323,210,000 9,373,090 3,124,051 3,124,051

471,118,500 18,222,000 -0.14% 352,388,500 10,219,267 6,812,163 3,688,112

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 Growth**

**of Defense, in**

**Office of the Number Average**

**Actuary Number of Growth Annual**

**Retirement of Military Military in Retirement**

**Statistical Retirees Retirees Annual Military Payments**

**Report Below Below Retirement Retirement Below**

**Date Fiscal Year Age 65 Age 65 Payments Payments Age 65**

Sep-08 FY 2008-09 30,201   591,600,000   19,589

Sep-09 FY 2009-10 30,420 0.73% 633,120,000 7.02% 20,813

Sep-10 FY 2010-11 30,322 -0.32% 633,516,000 0.06% 20,893

Sep-11 FY 2011-12 30,251 -0.23% 635,220,000 0.27% 20,998

Sep-12 FY 2012-13 29,547 -2.33% 640,932,000 0.90% 21,692

Sep-13 FY 2013-14 29,133 -1.40% 643,572,000 0.41% 22,091

Estimate FY 2014-15 28,924 -0.72% 654,502,000 1.70% 22,628

Estimate FY 2015-16 28,717 -0.72% 665,618,000 1.70% 23,179

Estimate FY 2016-17 28,511 -0.72% 676,922,000 1.70% 23,743

Estimate FY 2017-18 28,306 -0.72% 688,418,000 1.70% 24,321

**Annual Total Tax Annual Tax**

**Retirement Revenue Revenue**

**Payments Current Reduction Reduction**

**Deducted Tax on for Three Year for Three Year**

**Under Remaining Remaining Phase-in Phase-in**

**Current Growth Taxable Taxable to 100% to 100%**

**Law, Disability in Military Military Military Military**

**Maximum Payments Disability Retirement Retirement Retirement Retirement**

**$15,000 (Not Taxable) Payments Income Income Reduction Reduction**

90,603,000 16,572,000   484,425,000 16,470,450

91,260,000 17,676,000 6.66% 524,184,000 17,822,256

90,966,000 17,520,000 -0.88% 525,030,000 17,851,020

90,753,000 18,912,000 7.95% 525,555,000 17,868,870

88,641,000 18,468,000 -2.35% 533,823,000 18,149,982

87,399,000 20,244,000 9.62% 535,929,000 18,221,586

86,772,000 21,071,000 4.08% 546,659,000 18,586,406

86,150,000 21,932,000 4.08% 557,536,000 18,956,224 6,318,109 6,318,109

85,532,000 22,828,000 4.08% 568,562,000 19,331,108 12,886,117 6,568,007

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.

Frank A. Rainwater, Executive Director

Revenue and Fiscal Affairs Office

**A** **BILL**

TO AMEND SECTION 12‑6‑1140, AS AMENDED, CODE OF LAWS OF SOUTH CAROLINA, 1976, RELATING TO DEDUCTIONS FROM SOUTH CAROLINA TAXABLE INCOME OF INDIVIDUALS FOR PURPOSES OF THE SOUTH CAROLINA INCOME TAX ACT, SO AS TO ALLOW THE DEDUCTION OF RETIREMENT BENEFITS ATTRIBUTABLE TO SERVICE ON ACTIVE DUTY IN THE ARMED FORCES OF THE UNITED STATES; AND TO AMEND SECTION 12‑6‑1170, AS AMENDED, RELATING TO THE RETIREMENT INCOME DEDUCTION, SO AS TO CONFORM THIS DEDUCTION TO THE MILITARY RETIREMENT DEDUCTION ALLOWED BY THIS ACT.

Be it enacted by the General Assembly of the State of South Carolina:

SECTION 1. This act may be cited as the “South Carolina Giving Back to Our Veterans Act”.

SECTION 2. Section 12‑6‑1140 of the 1976 Code is amended by adding a new item at the end to read:

“(12) for taxable years beginning after 2016, military retirement benefits attributable to service on active duty in the armed forces of the United States.”

SECTION 3. Section 12‑6‑1170(A)(2) of the 1976 Code is amended to read:

“(2) The term ‘retirement income’, as used in this subsection, means the total of all otherwise taxable income not subject to a penalty for premature distribution received by the taxpayer or the taxpayer’s surviving spouse in a taxable year from qualified retirement plans which include those plans defined in Internal Revenue Code Sections 401, 403, 408, and 457, and all public employee retirement plans of the federal, state, and local governments, including military retirement. After taxable year 2016, military retirement is not included as retirement income for purposes of the deduction allowed by this section.”

SECTION 4. In addition to amounts allowed as a deduction pursuant to Section 12‑6‑1170 of the 1976 Code, there is allowed as a deduction from South Carolina taxable income of individuals for purposes of the South Carolina Income Tax Act a portion of otherwise taxable military retirement benefits attributable to service on active duty in the armed forces of the United States according to the following schedule:

Taxable Year Deduction Percentage

2015 33.33 percent

2016 66.67 percent.

SECTION 5. This act takes effect upon approval by the Governor and applies for taxable years beginning after 2014.

‑‑‑‑XX‑‑‑‑