



SOUTH CAROLINA REVENUE AND FISCAL AFFAIRS OFFICE
STATEMENT OF ESTIMATED FISCAL IMPACT
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Bill Number:	H. 3247	Amended by House Ways and Means on February 10, 2022
Author:	G.M. Smith	
Subject:	Workforce Enhancement and Military Recognition Act	
Requestor:	House of Representatives	
RFA Analyst(s):	Jolliff	
Impact Date:	February 15, 2022	

Fiscal Impact Summary

This bill would amend Section 12-6-1171 to allow taxpayers to deduct all military retirement income from state taxable income.

We anticipate that the Department of Revenue (DOR) will implement the change with existing staff and resources. Therefore, the bill is not expected to impact expenditures for the agency.

The bill as amended will decrease General Fund individual income tax revenue by an estimated \$7,972,000 beginning in FY 2022-23 by allowing taxpayers to deduct all military retirement income.

Explanation of Fiscal Impact

Amended by House Ways and Means on February 10, 2022

State Expenditure

This amended bill would increase the current income tax deduction for military retirement income to allow taxpayers to deduct all military retirement from state taxable income without regard to earned income. We anticipate that DOR will implement the changes with existing staff and resources. Therefore, the bill is not expected to impact expenditures for the agency.

State Revenue

This bill would amend Section 12-6-1171 to allow taxpayers to deduct all military retirement income from state taxable income. Currently, Section 12-6-1171 provides an individual income tax deduction of up to \$17,500 of earned income for taxpayers that also have military retirement income. The deduction is equal to the amount of military retirement income included in taxable income, not to exceed \$17,500. Taxpayers age 65 and over may also deduct up to \$30,000 of military retirement income without regard to earned income.

Please be advised that in SC Revenue Ruling 21-13 issued in late 2021, the Department of Revenue stated that a taxpayer age 65 and over is eligible for both the earned income deduction of \$17,500 and a military retirement deduction of up to \$30,000, as opposed to only the military retirement deduction. DOR's guidance that taxpayers age 65 and over may claim both the earned income and military retirement deductions was not addressed in the tax return instructions

for 2021 or in prior years. As such, we do not anticipate that the impact is currently reflected in our revenue collections for FY 2021-22. The Board of Economic Advisors (BEA) accounted for this change in its revised forecast for FY 2022-23 on February 15, 2022. Our analysis is based upon the impact of this new guidance.

Based upon the latest data provided by the SC Department of Veterans Affairs from the Department of Defense, Office of the Actuary through September 2021, the estimated revenue impact in FY 2022-23 for the deduction under current law totals \$22,914,000 with the new guidance.

The first row of the table below reports the estimated revenue impact of the current deductions and proposed full deduction of all military retirement income for taxpayers under age 65 in tax year 2022. We estimate that the individual income tax revenue impact of a fully implemented military retirement income deduction in FY 2022-23 will total \$18,714,000 for taxpayers under age 65. The BEA forecast for individual income tax revenue includes the impact of the current deductions, which is estimated to be \$11,025,000. Therefore, the proposed complete deduction of the remaining military retirement for taxpayers under age 65 will reduce individual income tax revenue by an additional \$7,689,000 in FY 2022-23.

The second row of the table below reports the estimated revenue impact of the current and proposed deduction for taxpayers age 65 and older in tax year 2022. We estimate that the individual income tax revenue impact of the fully implemented military retirement income deduction in FY 2022-23 will total \$12,172,000 for taxpayers age 65 and over. For these taxpayers, the BEA forecast includes the reduction in the individual income tax revenue for the current deduction estimated to be \$10,036,000. Therefore, the proposed complete deduction of the remaining military retirement for taxpayers age 65 and older will reduce individual income tax revenue by an additional \$2,136,000 in FY 2022-23.

Our estimate of the earned income deduction for taxpayers age 65 and over with military retirement is based upon data from the Census Bureau and the Bureau of Labor Statistics. Using 2021 figures, approximately 18.5 percent of the estimated U.S. population age 65 and over is employed. The code section allows a taxpayer to deduct up to \$17,500 of earned income equal to military income. Based upon an average tax rate of 2.88 percent for a deduction of \$17,500, this deduction will reduce income tax by approximately \$504 per qualifying taxpayer. The average tax rate for this deduction amount accounts for the fact that many returns are already reduced to zero before the additional deduction. Multiplying 18.5 percent by the 19,869 individuals with military retirement, we estimate that approximately 3,676 will be eligible for the \$504 deduction totaling \$1,853,000.

The net change for taxpayers age 65 and over will be an additional reduction of \$283,000. This change is shown in the fourth row of the table below.

Combining the revenue impacts of the deduction for all military retirees results in an estimated total reduction in General Fund individual income tax revenue of \$30,886,000. Of this total, the current revenue forecast includes an estimated reduction of \$22,914,000. Therefore, the

proposed complete deduction of all remaining military retirement income beginning in tax year 2022 will reduce General Fund individual income tax revenue by an additional \$7,972,000 in FY 2022-23.

**Estimated Number and Tax Revenue Reduction for
Military Retirees FY 2022-23**

Age of Military Retirees	Total Estimated Number of Active Duty Military Retirees	Total Tax Revenue Reduction from Full Military Retirement Deduction	Total Revenue Reduction from Act 272 of 2016	Additional Revenue Reduction from Full Military Retirement Deduction
Under Age 65	17,603	(\$18,714,000)	(\$11,025,000)	(\$7,689,000)
Age 65 and Older (Retirement)	19,869	(\$12,172,000)	(\$10,036,000)	(\$2,136,000)
Age 65 and Older (Earned Income) ¹	3,676	\$0	(\$1,853,000)	\$1,853,000
Age 65 and Older (Total)	19,869	(\$12,172,000)	(\$11,889,000)	(\$283,000)
Total	37,471	(\$30,886,000)	(\$22,914,000)	(\$7,972,000)

¹ Reflects guidance issued by the S.C. Department of Revenue in SC Revenue Ruling 21-13

Introduced on January 12, 2021

State Expenditure

This bill would increase the current income tax deductions for military retirement income. We anticipate that DOR will implement the changes with existing staff and resources. Therefore, the bill is not expected to impact expenditures for the agency.

State Revenue

This bill would amend the military retirement income deductions in Section 12-6-1171 by increasing the deduction amounts each year from tax year 2022 through 2027. Currently, taxpayers are allowed an individual income tax deduction of up to \$17,500 of earned income for taxpayers under age 65 that receive military retirement income for tax year 2021. The deduction is equal to the amount of military retirement income, not to exceed \$17,500. When a taxpayer reaches age 65, the taxpayer may deduct up to \$30,000 of military retirement income.

The bill would increase the current allowable deduction amount for earned income of individuals under age 65 of \$17,500 by \$2,900 beginning in tax year 2022 through 2027. Beginning in tax year 2027, the amount of the deduction is expanded to the full amount of earned income. For individuals 65 and over, the current \$30,000 deduction is increased by \$3,000 per year beginning

in tax year 2022 through 2027. Beginning in tax year 2028, the deduction is the full amount of military retirement income for taxpayers 65 and over.

For this analysis, we used the latest data from the Department of Defense, Office of the Actuary as of September 2020 provided by the SC Department of Veterans Affairs. Since Section 12-6-1171 allows different amounts of retirement income deductions by taxpayers depending on their age, we used these data to segregate taxpayers with military retirement income into two categories: under age 65 and age 65 and older.

Table 1 reports the estimated revenue impact of increasing the earned income deduction for military retirement income for taxpayers under age 65 beginning in tax year 2022. By full implementation, the deduction for taxpayers under 65 will reduce General Fund individual income tax revenue by up to \$9,037,000 in FY 2028-29. Because a taxpayer under age 65 must have earned income equal to the amount of military retirement, the deduction may be less than the full amount estimated, particularly in FY 2028-29 when the military retirement income deduction amount is only limited by the amount of earned income. However, the income tax returns do not provide sufficient information to determine the amount that will not be deducted. Therefore, we have included the maximum potential deduction.

Table 1: Tax Revenue Reduction from Phased-in Deduction for Military Retirees Under Age 65

Fiscal Year	Total Number of Active Duty Military Retirees	Maximum Earned Income Deduction Amount	Annual Revenue Reduction	Annual Additional Revenue Reduction
FY 2022-23	17,646	\$20,400	(\$1,475,000)	
FY 2023-24	17,402	\$23,300	(\$2,910,000)	(\$1,435,000)
FY 2024-25	17,162	\$26,200	(\$4,305,000)	(\$1,395,000)
FY 2025-26	16,925	\$29,100	(\$5,661,000)	(\$1,356,000)
FY 2026-27	16,691	\$32,000	(\$6,978,000)	(\$1,317,000)
FY 2027-28	16,461	\$34,900	(\$8,258,000)	(\$1,280,000)
FY 2028-29	16,233	all earned income	(\$9,037,000)	(\$779,000)

Table 2 reports the estimated revenue impact of increasing the military retirement income deduction for taxpayers age 65 and over beginning in tax year 2022. By full implementation, the deduction for taxpayers age 65 and over will reduce General Fund individual income tax revenue by up to \$3,852,000 in FY 2028-29.

Table 2: Tax Revenue Reduction from Phased-in Deduction for Military Retirees Age 65 and Older

Fiscal Year	Total Number of Active Duty Military Retirees	Maximum Retirement Income Deduction Amount	Annual Revenue Reduction	Annual Additional Revenue Reduction
FY 2022-23	19,959	\$33,000	(\$1,488,000)	
FY 2023-24	20,316	\$36,000	(\$2,243,000)	(\$755,000)
FY 2024-25	20,680	\$39,000	(\$2,537,000)	(\$294,000)
FY 2025-26	21,051	\$42,000	(\$2,844,000)	(\$307,000)
FY 2026-27	21,428	\$45,000	(\$3,165,000)	(\$321,000)
FY 2027-28	21,812	\$48,000	(\$3,501,000)	(\$336,000)
FY 2028-29	22,203	no limit	(\$3,852,000)	(\$351,000)

Combining the revenue impacts of the retirement income tax deduction for all military retirees, the bill will reduce General Fund individual income tax revenue by up to \$12,889,000 in FY 2028-29. The estimated impact by fiscal year is outlined in Table 3 below.

Table 3: Summary of Tax Revenue Reduction from Phased-in Military Retirement Deductions

Fiscal Year	Annual Revenue Reduction	Annual Additional Revenue Reduction
FY 2022-23	(\$2,963,000)	
FY 2023-24	(\$5,153,000)	(\$2,190,000)
FY 2024-25	(\$6,842,000)	(\$1,689,000)
FY 2025-26	(\$8,505,000)	(\$1,663,000)
FY 2026-27	(\$10,143,000)	(\$1,638,000)
FY 2027-28	(\$11,759,000)	(\$1,616,000)
FY 2028-29	(\$12,889,000)	(\$1,130,000)

Local Expenditure

N/A

Local Revenue

N/A

Frank A. Rainwater, Executive Director