



SOUTH CAROLINA REVENUE AND FISCAL AFFAIRS OFFICE
STATEMENT OF ESTIMATED FISCAL IMPACT
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This fiscal impact statement is produced in compliance with the South Carolina Code of Laws and House and Senate rules. The focus of the analysis is on governmental expenditure and revenue impacts and may not provide a comprehensive summary of the legislation.

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|------------------------|--|------------------------------------|
| Bill Number: | H. 3247 | Signed by Governor on May 13, 2022 |
| Author: | G.M. Smith | |
| Subject: | Workforce Enhancement and Military Recognition Act | |
| Requestor: | House of Representatives | |
| RFA Analyst(s): | Jolliff | |
| Impact Date: | June 21, 2022 | |

Fiscal Impact Summary

This bill amends 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 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

Signed by Governor on May 13, 2022

State Expenditure

This bill increases 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 amends 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

Local Expenditure

N/A

Local Revenue

N/A

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