

South Carolina Board of Economic Advisors

Statement of Estimated Revenue Impact

Date: February 7, 2011

Bill Number: H. 3583

Author: Cooper

Committee Requesting Impact: Ways and Means

Bill Summary


A bill to amend Section 12-6-40, as amended, Code of Laws of South Carolina, 1976, relating to the application of the Internal Revenue Code to state income tax laws, so as to update the reference to the Internal Revenue Code to the year 2010.

REVENUE IMPACT ^{1/}

This bill would decrease General Fund income tax revenue by \$5,288,658 in FY 2010-11 and increase revenue by \$6,312,069 in FY 2011-12.

Explanation

This bill updates the conformity of the South Carolina income tax statutes to the Internal Revenue Code as amended through December 31, 2010. Federal law changes were implemented in five separate tax bills enacted at the federal level in 2010. Specific federal tax modifications with significant South Carolina revenue impact include an increase in the maximum amount a taxpayer may expense under Section 179 to \$500,000 and increases the phase-out threshold amount to \$2,000,000 for tax years 2010 and 2011. The maximum deduction for Section 179 properties was \$250,000 with a phase-out threshold of \$800,000 in tax years 2008 and 2009. We expect this modification to reduce General Fund income tax revenue by \$6,109,541 in FY 2010-11 and \$1,897,818 in FY 2011-12. An increase in the amount small businesses may deduct in start-up expenses to \$10,000 from the prior \$5,000 in tax year 2010 is expected to reduce South Carolina income tax revenue by \$828,278 in FY 2010-11 and increase revenue by \$9,548 in FY 2011-12 due to fewer deductions in that tax year. Another federal change will allow retirees to rollover qualified distributions from 401(k), 403(b) and 457(b) plans to Roth designated accounts. These rollovers will be taxable at conversion, but tax free when the retirement savings are used in future years. We anticipate that this change will increase income tax revenue by \$614,210 in FY 2010-11 and \$1,437,687 in FY 2011-12. Health care reform legislation mandates that expenditures for over-the-counter medicines are no longer reimbursable from health savings accounts, Archer medical spending accounts, and health flexible spending arrangements. We anticipate that this change will increase income tax revenue by \$1,087,098 in FY 2010-11 and \$1,630,647 in FY 2011-12. The final significant revenue impact from the federal changes in 2010 is the reduction in Section 179 expensing maximum amounts to \$125,000 from \$500,000 and decreasing the phase-out threshold amount to \$500,000 from \$2,000,000 for tax year 2012. We expect that this additional modification to Section 179 expensing will increase General Fund income tax revenue by \$5,049,969 in FY 2011-12. Based on our analysis of these changes, the BEA estimates that the net revenue impact of updating IRS conformity would decrease General Fund income tax revenue by \$5,288,658 in FY 2010-11 and increase revenue by \$6,312,069 in FY 2011-12. The Board of Economic Advisors has not accounted for these projected revenue declines or increases in its forecasts of FY 2010-11 or FY 2011-12 General Fund revenues. A table summarizing the South Carolina revenue impact from all the recent federal tax changes is below.



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^{1/} This statement meets the requirement of Section 2-7-71 for a state revenue impact by the BEA, or Section 2-7-76 for a local revenue impact, or Section 6-1-85(B) for an estimate of the shift in local property tax incidence by the Office of Economic Research.

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2010 Federal Acts Affecting South Carolina Tax Revenue

Line #		Effective	FY 2010-11	FY 2011-12
1	Small Business Jobs Act of 2010			
2	A. Providing Access to Capital			
3	1. Increase in exclusion for gain from certain small business stock acquired at original issue and held for at least 5 years to 100%. The revenue gain in FY 2011 is from estimated taxes paid on gains that exceed the greater of 10 times the taxpayers' basis or \$10 million. (sunset 12/31/10)	DOE	5,435	0
4	4. Reduction in recognition period from 7 years to 5 for built-in gains tax on the sale of appreciated assets sold after conversion from a C corporation to S corporation. (sunset 12/31/11)	tyba 12/31/10	-62,759	-12,968
5	B. Encouraging Investment			
6	1. Expand definition of eligible section 179 property to include certain real property and increase maximum amount and phase-out thresholds to \$500,000 and \$2,000,000 respectively from \$250,000 maximum deduction and \$800,000 phase-out threshold that existed in tax years 2008 and 2009.	tyba 12/31/09 & before 1/1/12	-6,109,541	-1,897,818
7	C. Promoting Entrepreneurship			
8	1. Increase in amount allowed as a deduction for start-up expenditures from \$5,000 to \$10,000 and increase the deduction phase-out threshold from \$50,000 to \$60,000.	tyba 12/31/09	-828,278	9,548
9	D. Promoting Small Business Fairness			
10	3. Remove cellular telephones and similar telecommunications equipment from listed property which excludes the fair market value of personal use of a cell phone provided to an employee from gross income.	tyba 12/31/09	-40,444	-34,866
11	Total of Small Business Relief		-7,035,586	-1,936,104
12				
13	II. Revenue Provisions			
14	B. Promoting Retirement Preparation			
15	1. Allow participants in governmental 457 plans to contribute deferred amounts beginning in 2011 to designated Roth accounts.	tyba 12/31/10	32,613	46,202
16	2. Allow rollovers of qualified distributions from 401(k), 403(b) and 457(b) plans to Roth designated accounts.	DOE	614,210	1,437,687
17	3. Permit partial annuitization of a nonqualified annuity contract. The annual benefits received as an annuity payment will become taxable as income.	tyba 12/31/10	13,589	54,355
18	Total Revenue Provisions		660,412	1,538,244
19				
20	Total of Small Business Act		-6,375,174	-397,860
21				

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22		Effective	FY 2010-11	FY 2011-12
23	Education/Jobs/Medicaid Assistance Act of 2010			
24	1. Special rule with respect to certain redemptions by foreign subsidiaries. The new law requires the subsidiary's earnings to remain subject to U.S. tax when repatriated to the foreign parent as a dividend.	DOE	26,596	26,596
25				
26	Total of Education/Jobs/Medicaid Assistance Act		26,596	26,596
27				
28				
29		Effective	FY 2010-11	FY 2011-12
30	Patient Protection and Affordable Care Act and Health Care and Education Reconciliation Acts of 2010			
31	Revenue Provisions			
32	1. Conform the definition of medical expenses for health savings accounts, Archer MSAs, health flexible spending arrangements, and health reimbursement arrangements to the definition of the itemized deduction for medical expenses Therefore, over-the-counter medicines are not reimbursable from these accounts unless prescribed by a physician.	tyba 12/31/10	1,087,098	1,630,647
33	2. Limit health flexible spending arrangements in cafeteria plans to \$2,500; indexed to CPI-U after 2013 [1] [5]	tyba 12/31/12	-	-
34	4. Raise 7.5% AGI floor on medical expenses deduction to 10%; AGI floor for individuals age 65 and older (and their spouses) remains at 7.5% through 2016	tyba 12/31/12	-	-
35	5. \$500,000 deduction limitation on taxable year remuneration to officers, employees, directors, and service providers of covered health insurance providers	tyba 12/31/12	-	-
36				
37	Total Patient Protection Act		1,087,098	1,630,647
38				
39				

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40		Effective	FY 2010-11	FY 2011-12
41	The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010			
42	Section 179 expensing amounts and threshold limits reduced to \$125,000/\$500,000 for tax year 2012 from the \$500,000 maximum deduction and \$2,000,000 phase-out threshold that is law for tax years 2010 and 2011. (sunset 12/31/12) This reduction in Section 179 expensing amounts reverses the increases in tax years 2008 through 2011 as enacted in earlier legislation including the Small Business Jobs Act of 2010. The proposed \$125,000/\$500,000 levels are identical to the amounts that existed for tax year 2007 as established by the Small Business and Work Opportunity Tax Act of 2007.	tyba 12/31/11	0	5,049,969
43				
44	Total Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act		0	5,049,969
45				
46				
47		Effective	FY 2010-11	FY 2011-12
48	The Regulated Investment Company Modernization Act of 2010			
49	I. Capital loss carryovers of Regulated Investment Companies (RIC) derived from long-term capital losses will now be required to use those losses to offset long-term capital gains. This will result in a greater distribution of short-term capital gains to shareholders that will be taxed as ordinary income. As a partial offset, the RIC will be permitted to carryforward its net capital losses without limit, rather than the 8 years in previous law.	DOE	8,153	59,790
50	III.3. A RIC may pass-thru exempt interest dividends in fund of fund structure without regard to the requirement that at least 50% of the value of its total assets consist of tax-exempt State and local bonds. Previous law allowed exempt-interest dividends to be passed through by a RIC only if at least 50% of the value of the total assets consist of tax-exempt obligations.	tyba DOE	-5,435	-10,871
51	III.6. Allow distributions in redemption of stock of a RIC to be treated as an exchange if the redemption is upon the demand of the shareholder and the company issues only stock which is redeemable upon the demand of the shareholder. Otherwise, the redemption is treated as a distribution of property.	DOE	-13,589	-24,460
52	Modification of sales load basis deferred rule for RIC to allow shareholders to take capital losses for the amount of the load charges paid on the acquisition of fund shares after subsequent repurchase of shares with reinvestment rights.	tyba DOE	-16,306	-21,742
53				
54	Total Regulated Investment Company Modernization Act		-27,177	2,718
55				
56				
57	Total IRS Conformity Impact		-5,288,658	6,312,069