

# Statement of Estimated State Revenue Impact

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**Date:** May 22, 2012

**Bill Number:** S.1409 as amended May 16, 2012 by Ways and Means Economic Development, Capital Improvement, and Other Taxes Subcommittee

**Author:** Alexander

**Committee Requesting Impact:** Ways and Means

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## Bill Summary

TO AMEND SECTION 6-34-40, AS AMENDED, CODE OF LAWS OF SOUTH CAROLINA, 1976, RELATING TO TAX CREDITS FOR REHABILITATION EXPENSES, SO AS TO CLARIFY THAT THE CREDIT MAY BE TAKEN AGAINST FRANCHISE TAXES ON BANKS; TO AMEND SECTION 12-4-320, AS AMENDED, RELATING TO POWERS AND DUTIES OF THE DEPARTMENT OF REVENUE, SO AS TO ALLOW THE DEPARTMENT TO GRANT RELIEF PERIODS GRANTED BY THE INTERNAL REVENUE SERVICE; TO AMEND SECTION 12-6-50, AS AMENDED, RELATING TO INTERNAL REVENUE CODE SECTIONS SPECIFICALLY NOT ADOPTED, SO AS TO NOT ADOPT SECTION 7508; TO AMEND SECTION 12-6-590, RELATING TO THE TREATMENT OF "S" CORPORATIONS FOR TAX PURPOSES, SO AS TO IMPOSE A TAX ON CERTAIN INCOME IF THE INTERNAL REVENUE CODE IMPOSES A SIMILAR TAX; TO AMEND SECTION 12-6-3360, AS AMENDED, RELATING TO THE JOBS TAX CREDIT, SO AS TO AMEND THE DEFINITION OF "NEW JOB"; TO AMEND SECTION 12-6-3535, AS AMENDED, RELATING TO THE INCOME TAX CREDIT FOR REHABILITATION EXPENSES, SO AS TO CLARIFY THAT THE CREDIT MAY BE TAKEN AGAINST FRANCHISE TAXES ON BANKS; TO AMEND SECTION 12-6-3630, RELATING TO INCOME TAX CREDITS FOR HYDROGEN RESEARCH CONTRIBUTIONS, SO AS TO CLARIFY THAT THE CREDIT MAY BE TAKEN AGAINST FRANCHISE TAXES ON BANKS; TO AMEND SECTION 12-6-4910, AS AMENDED, RELATING TO THE REQUIREMENT TO FILE AN INCOME TAX RETURN, SO AS TO INCREASE THE STANDARD DEDUCTION FOR INDIVIDUALS OVER SIXTY-FIVE AS PROVIDED IN THE INTERNAL REVENUE CODE; TO AMEND SECTION 12-37-220, AS AMENDED, RELATING TO PROPERTY TAX EXEMPTIONS, SO AS TO CORRECT A CROSS-REFERENCE; TO AMEND SECTION 12-43-260, RELATING TO COUNTIES WILFUL FAILURE TO COMPLY WITH THE ASSESSMENT PROGRAM, SO AS TO PROVIDE THAT THE DEPARTMENT SHALL MAKE A DETERMINATION THAT IS SUBJECT TO REVIEW BY THE ADMINISTRATIVE LAW COURT; TO AMEND SECTION 12-44-110, AS AMENDED, RELATING TO FEE IN LIEU OF TAX, SO AS TO UPDATE A TERM; TO AMEND SECTION 12-54-240, AS AMENDED, RELATING TO THE DISCLOSURE OF RECORDS FILED WITH THE DEPARTMENT, SO AS TO PROVIDE THAT IN ORDER FOR A CONVICTION FOR UNLAWFULLY DIVULGING RECORDS, A PERSON MUST WILFULLY DIVULGE, AND TO PROVIDE THAT PRIOR TO DISMISSING AN EMPLOYEE FOR A VIOLATION, THE EMPLOYEE MUST BE CONVICTED; TO AMEND SECTION 12-60-50, AS AMENDED, RELATING TO THE OCCURRENCE OF A FILING PERIOD ENDING ON A HOLIDAY, SO AS TO RECOGNIZE A HOLIDAY RECOGNIZED BY THE INTERNAL REVENUE SERVICE; TO AMEND SECTION 12-60-90, AS AMENDED, RELATING TO THE ADMINISTRATIVE TAX PROCESS, SO AS TO CORRECT CROSS-REFERENCES AND FURTHER DEFINE TERMS; TO AMEND SECTION 12-65-30, AS AMENDED, RELATING TO THE CREDIT FOR EXPENSES RELATED TO THE REHABILITATION OF A TEXTILE MILL, SO AS TO CLARIFY THAT THE CREDIT MAY BE TAKEN AGAINST FRANCHISE TAXES ON BANKS; AND TO AMEND SECTION 44-43-1360, AS AMENDED, RELATING TO ADMINISTRATIVE EXPENSES FOR DONATE LIFE SOUTH CAROLINA, SO AS TO CORRECT A CROSS-REFERENCE.

# Statement of Estimated State Revenue Impact

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## REVENUE IMPACT <sup>1/</sup>

We expect this bill, S. 1409 as amended by Ways and Means Subcommittee, will reduce General Fund revenue by \$4,875,514 in FY 2012-13 and by an additional \$1,284,500 in FY 2013-14. Other fund revenue allocated to the State Energy Office will increase by \$17,000 in FY 2012-13.

### **Explanation of Bill as Amended on May 16, 2012 by Ways and Means Economic Development, Capital Improvement, and Other Taxes Subcommittee**

**Amendment 1.** The first amendment adds an unnumbered section that expands the current 5% investment credit for qualified plastic and rubber products manufacturers to include employers committing to hire 1,200 full-time employees by January 1, 2022 and investing \$400,000,000 in capital investments between September 1, 2011 and January 1, 2022. The current investment tax credit pursuant to §12-14-80 requires plastic and rubber manufacturers to employ 5,000 full-time employees, have a total capital investment in South Carolina of not less than \$2,000,000,000, and commit to investing \$500,000,000 in capital investments in South Carolina between January 1, 2006 and July 1, 2011.

This amendment also clarifies that a taxpayer can include any intermediaries controlled by or under common control with the taxpayer. The amendment further defines "capital investment in this state" to include property capitalized, subject to a capital lease, or an operating lease with the taxpayer. The proposed investment tax credit cannot be utilized until the taxpayer has invested \$200,000,000 of the \$400,000,000 required investment, commits to the Department in a statement to invest a total of \$400,000,000 in this state before January 1, 2022, and commits to employing 1,200 full-time employees in the state by January 1, 2022. If a taxpayer fails to meet these requirements, they must refund any credit received with interest.

Taxpayers qualifying for the current and proposed expanded investment tax credit may claim the credit against income or withholding taxes. The credit ranges from 0.5% for 3 year recovery property to 2.5% for 15 year recovery property under Section 168(e) of the Internal Revenue Code. We anticipate that the investment credit will average 2% for the mix of property investments made by these manufacturers. Based on recent economic development announcements totaling \$1,700,000,000 by tire manufacturers, we believe that the proposed legislation could create corporate income tax credits of \$3,400,000 per year during the ten-year period.

However, we anticipate that the plastic and rubber products manufacturers qualifying for this proposed credit are eligible for the single sales factor apportionment method, which excludes payroll and property in calculating South Carolina taxable income. This income allocation method would limit the amount of taxable income attributed to South Carolina and likely result in qualifying taxpayers claiming the proposed investment tax credit against withholding tax.

## Statement of Estimated State Revenue Impact

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We expect that withholding liabilities will exceed the proposed investment tax credit and allow the manufacturers to utilize this credit. From publicized employment projections in recent economic development announcements, we anticipate that between September 1, 2011 and January 1, 2022 qualifying taxpayers will increase employment by 2,550 jobs at an average annual salary of \$52,000 per year based on U.S. Census Bureau data for these manufacturers. We estimate that employee payroll for these additional workers will total \$132,600,000 annually and withholding tax will total \$9,282,000 per year. Under current law, the proposed investment tax credit may not exceed 50% of the withholding tax due before the application of job tax, job development, and job retraining credits. Multiplying the expected \$9,282,000 in withholding tax by 50% results in \$4,641,000 of withholding liabilities per year that manufacturers can utilize for the investment credit against during the ten-year life of the proposed credit. This amendment will reduce General Fund income tax revenue by \$3,400,000 per year during the ten-year life of the proposed credit. By tax year 2022, we expect that the General Fund income tax revenue reduction will total \$34,000,000 at which time the credits are anticipated to expire.

**Amendment 2.** This amendment allows taxpayers to claim discounts, which are currently allowed for timely filed returns, on delinquent returns when the Department of Revenue waives all penalties for late filing due to reasonable cause. At this time, the Department cannot provide the number or amount of discounts this amendment would affect. The Department's general guidelines for a complete penalty waiver require the taxpayer to exercise ordinary care and prudence. The burden is on the taxpayer to prove the existence of a reasonable cause. Examples of reasonable cause include unavoidable absence of the taxpayer from South Carolina, death or incapacitating illness of the taxpayer, unavailability of the taxpayer's records, and reliance on erroneous written or oral advice given by the Department or other competent tax advisor. Based on the difficulty of showing reasonable cause, we expect that this amendment will reduce General Fund revenue from many tax categories by \$25,000 in FY 2012-13.

**Amendment 3.** This amendment revises Section 12-6-3360(M)(13) and (14) relating to Qualifying Service-Related Facilities and Technology Intensive Facilities by adjusting the number of jobs necessary to qualify for the job tax credit and expanding the types of facilities deemed to be technology intensive. The amendments to section (M) (13) would likely only apply to a select group of industries not already covered by existing laws. Very few industries will likely meet one of the five requirements to qualify for the tax credit: 1) have net increases of 175 jobs at a single location, or 2) create 150 jobs at a single location in a building that has been vacant for at least 12 months prior, or 3) create 100 jobs at a single location paying on average at least 1.5 times the state per capita income, or 4) create 50 jobs paying on average at least double the state per capita income, or 5) create 25 jobs paying on average at least 2.5 times the state per capita income.

The industry most likely to qualify that is not already included under another code section would be Management of Companies (NAICS code 55). Specifically, call centers would be the most likely sub-industry capable of generating sufficient new jobs to qualify for the credit.

## **Statement of Estimated State Revenue Impact**

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Over the past six years, according to the Census Bureau's County Business Patterns data, on average one new call center per year with more than 100 employees has opened in South Carolina. Based on an average \$3,500 in job tax credits and the creation of 175 new jobs, this section of the amendment will reduce General Fund individual and corporate income tax revenue by an estimated \$612,500 in FY 2013-14, which accounts for the one-year lag to claim the credit from when the jobs are created.

This amendment also amends Section 12-6-3360(M) (14) to include data processing, hosting and related services facilities (NAICS code 518210 to the definition of "technology intensive facility", expanding the jobs tax credit to this sector. Based upon data from the SC Department of Employment and Workforce, this qualifying sector (NAICS code 518210) added an average of 192 jobs each year over the latest four fiscal years even without the credit. We expect that this pace of new jobs creation in this sector will continue in FY 2012-13, but with these new hires receiving the credit. We estimate that the 192 new jobs multiplied by an average job tax credit of \$3,500 per new job created will reduce General Fund individual and corporate income tax revenue by an estimated \$672,000 in FY 2013-14, which accounts for the one-year lag to claim the credit from when the jobs are created.

This amendment also exempts the purchases of computers, computer equipment, computer hardware, computer software, and electricity used by a datacenter from the state sales and use tax. Datacenters are defined as facilities in which at least fifty million dollars are invested in real or personal property or both over a five-year period by a taxpayer or where one or more taxpayers invests a minimum aggregate capital investment of at least seventy-five million dollars in real or personal property or both over a five year period and that provide infrastructure for hosting or data processing services. The datacenter must also be certified by the Department of Commerce and create and maintain for three consecutive years at least twenty-five full-time jobs at the facility with an average cash compensation level of one hundred fifty percent of the per capita income of the state or of the county in which the facility is located, whichever is lower.

The state has not attracted hosting or data processing datacenters with this level of capital investment. In the absence of this proposed legislation, this trend is expected to continue. Since the revenue projection does not anticipate tax revenue from these projects, these tax exemptions will have no impact on the revenue forecast for FY2012-13. As a result, the revenue forecast for the General Fund, EIA fund, and the Homestead Exemption fund would not be impacted.

In total, this amendment will reduce General Fund individual and corporate income tax revenue by \$1,284,500 in FY 2013-14.

**Amendment 4.** This amendment adds Section 12-6-3586 granting a tax credit equal to thirty-five percent of the costs of solar energy equipment used for water heating, space heating or cooling, generating electricity, distillation, desalination, detoxification, or the production of industrial or commercial process heat placed into service by a taxpayer. The credit may be claimed against a taxpayer's individual income, corporate income, bank tax,

## **Statement of Estimated State Revenue Impact**

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license fees, or insurance premiums taxes, or any combination of these taxes. In no case may the credit claimed by a taxpayer exceed one-half of the taxpayer's tax liability for a taxable year.

This bill also provides ceilings on the amount of credit that can be claimed per installation. For solar energy equipment placed into service for residential purposes, the ceiling per dwelling is \$3,500 for domestic water heating or active space heating and \$10,500 for any other solar energy equipment. Any unused residential credit may be carried forward to the five succeeding taxable years.

For solar energy systems placed into service for any purpose except residential, the ceiling amount equals \$2,500,000 and must be taken in three equal annual installments. Any unused credits may be carried forward for five succeeding taxable years.

The total amount of credits allocated may not exceed \$8,000,000 in tax years 2012 and 2013, \$7,000,000 in tax year 2014, and \$6,000,000 in tax years 2015 and 2016. Of these annual amounts, 15% must be allocated for single-family residential equipment, 35% for equipment with less than one megawatt of installed capacity for purposes other than single-family homes, and 50% must be allocated for equipment with one megawatt or more of installed capacity for purposes other than single-family homes. The amendment would allow large, commercial installations that have at least one megawatt of installed capacity to be exempted from the aggregate credit caps in each year.

The amendment also provides for a new, nonrefundable application fee equal to one percent of the credit applied for with a cap of \$2,500. The application fee will be credited to the State Energy Office to administer the tax credit. Finally, the amendment clarifies that taxpayers applying for the credit may not resell electricity generated by the solar energy equipment to any other person or entity unless it is to an electric supplier or electrical utility, an electric cooperative, the SC Public Service Authority, a city or town or board of public works or a commission of public works, or a joint agency.

Section 12-6-3587, which is in current law, allows an income tax credit equal to 25 percent for the costs of purchasing and installing certain solar energy systems. The income tax credit pursuant to Section 12-6-3587 is capped at \$3,500 per facility.

Based on analysis of the solar installations in South Carolina, provided by the State Energy Office, and using average costs of solar energy equipment, it is estimated that 30 percent of taxpayers that purchase and install solar energy equipment would benefit more from the 35 percent income tax credit allowed under this amendment compared to the existing 25 percent income tax credit. According to data from the Department of Revenue, approximately 240 taxpayers claimed the existing solar energy tax credit for a total of \$696,300, or approximately \$2,900 per taxpayer, in 2010. The four-year average growth in the number of individuals claiming the existing credit is 51.4 percent per year. Assuming this growth rate holds over the next few years, the projected number of taxpayers claiming the existing 25 percent credit in 2012 would be 555. Assuming that 30 percent of these individuals would benefit more from the new credit, there would be 167 individuals claiming

## **Statement of Estimated State Revenue Impact**

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the 35 percent credit in 2012 at an average credit of \$8,200 per taxpayer (based on an analysis of solar installations from the State Energy Office). This would result in total credits of approximately \$1,365,461, which would be capped at \$1,200,000 per the restrictions in the bill. If this amendment did not pass, these individuals could take the smaller \$3,500 credit already offered in existing law, which would reduce the total impact, by \$582,819. Based on this analysis, the residential solar energy equipment tax credit would reduce General Fund income tax revenue by an estimated \$617,181 in FY2012-13.

Regarding non-residential installations, approximately nine commercial firms claimed a similar renewable energy equipment income tax credit in North Carolina in 2010, which also includes wind, hydroelectric, biomass, and geothermal equipment installations. We estimate that three of the nine commercial firms that claimed the similar renewable energy equipment income tax credit in North Carolina installed solar energy equipment. We anticipate that two commercial taxpayers will place into service solar energy equipment in South Carolina in FY2012-13, for a total of \$5,000,000 in credits. Adjusting for the fact that the tax credit is to be taken in three equal annual installments and applying the fifty percent tax liability limitation, it is estimated that this bill would reduce state General Fund income tax, bank tax, license fees, or insurance premium tax revenue by an estimated \$833,333 in FY2012-13 for commercial installations. As we do not expect to reach the aggregate credit cap in the upcoming fiscal years, the provision exempting certain commercial installations of one megawatt or larger from the cap does not affect the revenue estimate.

The amendment provided a new tax credit application fee that will provide other funds revenue for the State Energy Office. The application fee is equal to one percent of the credits, but no more than \$2,500 per installation. We expect taxpayers installing residential solar energy equipment to remit approximately \$12,000 in FY 2012-13. For non-residential installations, we expect that the application fee cap will generate \$5,000 in other funds revenue. The application fee will generate a total of \$17,000 in other fund revenue for the State Energy Office in FY 2012-13.

In total, this amendment will reduce General Fund income tax revenue by an estimated \$1,450,514 in FY2012-13 and increase other fund revenues allocated to the State Energy Office by \$17,000 in FY2012-13.

**Amendment 5.** This amendment revises code sections relating to the appeal of property assessment values. Under current law, a taxpayer may appeal the assessed value of owner-occupied property based upon the value as it existed in the year of the most recent reassessment program. Under this amendment, taxpayers may appeal the assessment of owner-occupied residential property based upon the fair market value as of December thirty-first of the tax year under appeal. Beginning with tax bills due January 15, 2013, this would allow taxpayers to appeal based upon a lower fair market value if home values have declined since the most recent reassessment. Based upon the county reassessment schedule, 15 counties have undergone reassessment since the decline in the housing market and would not likely be affected by this change. The remaining 31 counties may experience some impact from a decline in the owner-occupied property tax base if appeals are based upon a

## **Statement of Estimated State Revenue Impact**

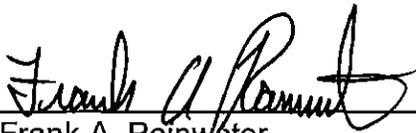
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lower value than existed as of the last reassessment. The impact would only exist in the remaining years until the county's next reassessment. We anticipate a reduction in local property tax revenue; however, the impact is indeterminable since it will be dependent upon the number of appeals, the timing of the last property reassessment, current home values in the affected counties and the difference between assessed value and market value.

The amendment also revises property tax assessment notice requirements to provide that in a year in which an assessable transfer of interest occurs due to a conveyance, if the assessor determines that fair market value is more than the purchase price, the assessor shall state with particularity, the basis for the increase in fair market value. Additionally, the amendment provides that the taxpayer at least has 30 days following receipt of the tax notice to appeal, and requires the assessor to include a property tax refund assignment contract in certain cases. These changes are not expected to impact local revenues.

### **Explanation of Bill filed April 10, 2012**

This bill implements a number of technical or clarifying amendments to various tax statutes administered by the Department of Revenue. The Department affirms that these proposed changes reflect current administrative practices and will not affect revenue collections. We expect that this bill will have no revenue impact on the General Fund or other agency funds.



Frank A. Rainwater  
Chief Economist

**Analysts:** Shuford, Martin, and Jolliff

<sup>11</sup> 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.