



#### OUR MISSION

*is to educate members and all South Carolinians about state and local public policy based on the traditional South Carolina values of individual liberty and responsibility, free enterprise, and limited government*

## SCPC Issue Analysis

### The House Tax Plan: True Reform or Something Else?

As we've reported in the past, South Carolina's tax rates are among the least competitive in the nation. Middle class families pay an inordinately high top rate, manufacturers are crippled by the state's property tax (one of the highest in the nation), and our state's byzantine system of exemptions keeps sales tax artificially high. And yet, instead of taking serious action to reform the state's anti-competitive and job-destroying tax structure, state politicians spend millions upon millions of dollars on failed "economic development" plans and other harebrained debacles.

Recently, a package of bills were filed in the House as an attempt at tax reform. Below is a brief review of this plan.

#### Income Tax Reform: H. 4997

##### The Problem:

Under South Carolina's current income tax system, middle class families pay an extremely high top marginal rate (*i.e.*, they pay taxes at the top tax rate). Anyone making over \$14,000 in taxable income falls under the top marginal rate of 7 percent. Since a middle class family of four falls well into the top tax bracket, it's not just the rich paying big taxes in South Carolina. By comparison, in Connecticut, not even millionaires pay 7 percent of their income to the state. That middle class citizens in South Carolina are paying a top 7 percent marginal rate (the 13th highest in the nation) is unconscionable.

##### The Proposed Bill:

This bill would reduce the number of tax brackets from six to three, making the income tax structure flatter. A flatter tax code is a better one given that it results in a simpler tax structure. However, the problem isn't just the number of tax brackets: it's also (and more importantly) the tax rates.

Supporters of the legislation claim the bill would reduce taxes for most South Carolinians. That's true, but not by much. Currently, a median family of four pays \$2,089 in state income tax. If this bill were to pass as is, that family would pay \$1,911 in state income tax, a savings of \$178 (\$45 dollars per household member). While any money returned to taxpayers is good, \$178 for a family of four is hardly the bold and ambitious relief taxpayers deserve. Even if this income tax relief was passed, it would return less than 0.3 percent of a median family's income back to them.

The proposed bill does set the rates slightly lower than [the governor's proposed tax reform](#). Under the governor's plan, the three brackets would be 0 percent, 3.75 percent, and 7 percent. Under the House, the three brackets would be 0 percent, 3 percent, and 7 percent.

### **Best Plan for the State:**

We believe the best tax plan for the state is one that is low and an equitable. As long as middle class South Carolinians are paying one of the highest state tax rates in the nation, the state tax system is neither. Instead of simply tinkering around with brackets, the state should be focusing on cutting as much waste out of the budget as possible, and using those “savings” to make our state’s tax rates as low as possible. 7% is too high, especially considering the amount of dollars that go towards funding waste. Unfortunately, neither the proposed plan nor the governor’s do anything about this top rate.

## **Sales Tax Reform: H. 4995**

### **The Problem:**

South Carolina’s sale tax code is a testament to the power of special interest in our states. Over the years, the code has been so riddled with exemptions carved out at the request of industry lobbyists that the state now exempts more in sales tax than it collects. However, by handing out exemptions, the state keeps the sales tax rate artificially high –higher than both North Carolina and Georgia. This is because if the state were to eliminate all the exemptions, they could reduce the overall sales tax rate without decreasing revenue. By keeping our rates high, state lawmakers put South Carolina businesses at a competitive disadvantage compared to businesses in neighboring states.

### **Proposed Plan:**

The proposed plan would end many, but not all, sales tax exemptions. Some of the most egregious “economic development” exemptions – including, for instance, the exemption of “any device, equipment, or machinery operated by hydrogen or fuel cells” – remain in full effect. As one lawmaker put it, the bill would preserve exemptions “that benefit families” – including medicine, food, and electricity. The extra revenue collected as a result of ending the exemptions must go to reducing the overall sales tax rate.

Under the proposed plan, however, many special interest exemptions remain, including an exemption for “vacation time sharing plans.” The question becomes: why eliminate some exemptions, but not others? If the state eliminated all exemptions and lowered the overall sales tax, South Carolina families would have more of their own money to spend however they saw fit. Why do legislators feel entitled to decide which purchases “benefit families” and which don’t? As long as the government is handing out exemptions, they are attempting to plan the economy.

### **The Best Plan for the State:**

Eliminate all sales tax exemptions and use all the revenue to lower the rate. Sales exemptions are one of the more obvious and insidious forms of politicians trying to centrally plan the economy. Eliminate all exemptions, and let individuals decide what to purchase.

In addition to providing relief to taxpayers, a decrease in our sales tax would provide much needed relief to our state’s businesses who are located near the border of two states – Georgia and North Carolina – with lower sales tax rates than South Carolina. If the state fails to lower the rate, South Carolina business owners will continue to be disadvantaged.

## Industrial Property Tax: H. 4993

### The Problem:

Among its many dubious distinctions, South Carolina has one the nation's highest manufacturing property taxes. Instead of addressing the actual problem preventing manufacturers from doing businesses, lawmakers have time and time again opted to pass theatrical and ineffective "economic development" packages. However, lawmakers who seek to address the *actual cause* of the loss of manufacturing jobs in the state should look no further than the state's crippling manufacturing property tax.

### The Proposed Bill:

Since the property tax rates are set in the constitution, it is very difficult to reduce the rates. The governor's proposed plan has recommended changing the law so that these tax rates are set by statute instead of constitutionally. This proposed bill takes a different track: instead of reducing the rate, the bill phases in exemptions over the course of 4 years that would exempt roughly 43 percent of industrial property tax. The legal rate would remain 10.5 percent, but by exempting roughly 43 percent of the 10.5 percent tax, the exemptions would functionally reduce the overall rate to around 6 percent. If this sounds complicated to you, you aren't alone. And the fact that it is complicated is a problem. The tax code should be simple.

### The Best Plan for the State:

While any reduction of the state's excessively high manufacturing property tax is a great idea, the proposal raises questions. First, why spread the cut over four years? Unemployed South Carolinians don't have four years to wait; they need immediate relief, and that relief should come in the form of lowering job-destroying tax rates. Real tax relief needs to happen immediately.

Second, the way lawmakers are bringing about this "tax reduction" is misguided. We understand that it is politically easier to use exemptions to reduce the rate than to amend the constitution. However, having property taxes set by the state constitution makes it extremely difficult for lawmakers to reduce rates when it becomes obvious – as it currently is – that those rates are far too high. That is why it is a better idea to make it so rates are set by law, while simultaneously reducing the rates.

And third, the question remains as to whether a 6 percent rate is low enough. The state should make the tax rate *as low as possible* by cutting waste from the budget and using the savings to reduce taxes for individuals and businesses. And as long as the state is still funding waste, still handing out exemptions, and still overspending, the rates are too high. Reducing the rate from 10.5 percent to 6 percent is a start, but as long as the state is wasting money, it's just a start.

## Corporate Income Tax

### The Problem:

Every cent that the government takes from a business is a cent that won't go towards hiring new employees. South Carolina businesses are hurting, and simply cannot afford to be paying 5 percent to the state government. As long as the state has a corporate income tax, potential jobs are being destroyed.

**The Purposed Plan:**

Like [the governor's tax reform plan](#), the House plan would gradually phase out the corporate income tax over four years, ultimately leaving the rate at 0 percent. That means that state corporations would still have to a corporate tax into the immediate future. As we said when the governor proposed the phase-out: "Eliminating the corporate income tax . . . is one tangible step the state could take to increase our business competitiveness and decrease unemployment. Lowering taxes for all companies – as opposed to the current practice of only giving tax credits to those with good lobbyists and good connections – would signal to out-of-state firms that South Carolina is a fair place to do business."

**The Best Plan for the State:**

A better idea than phasing out the corporate income tax would be to eliminate it immediately. The state could do so relatively easily. The most recent estimate from the BEA projects that the corporate income tax will provide the state with \$185 million in revenue, or 1.3 percent of state spending. Considering how vital job creation is for the 9.3 percent of South Carolina's labor force who are unemployed, and considering the immediate positive effect eliminating the corporate income tax would have on hiring and employment, surely state lawmakers could find a way to eliminate the tax immediately. They could start with the \$29.3 million state hand out to PRT, or the nearly \$20 million in state money given to the Department of Commerce.