

**Paying for Government in South Carolina**  
**A Citizen's Guide**

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# Getting Started

## ***the purpose***

► This booklet has been written to help citizens of South Carolina understand how their state and local revenue system works and why we use the revenue sources we do. Understanding how the system works may not change how you feel about taxes. But it should help you to take part more effectively in the ongoing conversation about taxes, fees and charges and the public services they support.

## ***a revenue “system”***

► Governments rely primarily on taxes to fund public spending, but fees and charges are also an important part of the revenue system. Most (but not all) taxes are “general revenue,” meaning that they can be used for any public purpose, while fees and charges usually are designed to pay for a specific purpose, such as tuition at a public college, entrance fees to public parks, or licenses and permits that often pay for inspection and enforcement costs.

► The parts of a revenue system are connected. You can’t single out a particular tax or fee to change without affecting other parts of the revenue system. A change, large or small, can shift the tax burden from one group to another, change the amount of revenue raised, and affect people’s decisions about location, spending, and investing.

► For example, in 2000 the General Assembly invited citizens to vote on a referendum to reduce the assessment rate on cars from 10.5 percent to 6 percent over six years. Most of us were happy to vote in favor of cutting taxes. But property taxes on cars were about 16 percent of the local property tax base in 2000, more in some smaller counties and cities. Where were local governments going to find revenue to make up for this loss? How would it affect the ability of smaller, rural school districts to meet state mandates for class size and teacher pay? If we, and our legislators, had thought about how taxes on cars fit into the overall revenue system, we still might have cut property taxes on cars, but in a different way.

***state and local  
interconnections***

- ▶ State taxes and fees and local taxes and fees are part of a single interconnected system. All local governments depend on state aid to fund their budgets, especially school districts. Both the state and many cities and counties use the sales taxes to raise revenue, so any change the state makes in the base of the sales tax (like a lower rate on food) affects the revenue of both levels of government. Sales taxes also play an important role in funding education.
- ▶ The General Assembly tells local governments what taxes they may levy and under what conditions. The state has control over the rules governing the property tax, an important source of local government revenue, and provides most of the funding for various statewide property tax relief programs.
- ▶ When we try to compare South Carolina's revenue system and tax burden to other states, it is usually better to compare combined state and local figures rather than just state or just local revenue or taxes. Taxes collected at the state level in one state may be used by local governments in others. Some state governments collect more revenue than in South Carolina, but also send more aid back to cities, counties, and school districts. Services that are provided by the state in South Carolina may be supplied by local governments in other states. For example, the state covers almost all of the cost of K-12 education in Hawaii, while it falls almost entirely to local governments in New Hampshire.

# The Ideal Revenue System

## **the challenge**

- ▶ When we get up in the morning, and water doesn't come out of the faucet, what do we do? Call public works at City Hall. When our cars are out of alignment because of potholes on the way to work, we complain to our county council members. When we are unhappy with our local school, we let our school board members know. And when we discover the hours at our favorite state park have been cut, we call our state legislators. Government equals services in the minds of most citizens.
- ▶ Putting together a plan to pay for the services people want from government isn't easy for elected officials. Taxes are never popular, and raising taxes is even less popular. But state legislators face the challenge of ensuring enough revenue in every legislative session. Local elected officials have to address the same question at budget time every year. There's no getting around it.
- ▶ Suppose we had the opportunity to start from scratch, to design a revenue system of taxes and fees from the ground up. How would we do it? We could start by looking at what are the qualities of a "good" tax or a "good" fee. Thinking about these qualities can help us choose the right or best mix of revenue sources.

## **revenue sources**

- ▶ Governments must decide whether to tax spending, income, or wealth or some combination of the three. They also must set the rates for the various taxes.
- ▶ Governments also charge fees for particular government services.
- ▶ Some levels of government provide or receive grants, which are often intended to promote national or state priorities. For example, grants are often used to offset differences in resources between richer and poorer areas.

## **rating a tax**

- ▶ Each tax (or fee) has its own strengths and weaknesses. If there were a perfect tax, it would have these qualities:  
**Adequacy:** A perfect tax would bring in a steady, dependable stream of revenue, adequate for public needs.

**Equity:** A perfect tax would be distributed fairly among different kinds of taxpayers based on their ability to pay and to some degree on their demand for public services. Equity is the hardest quality to measure and to agree on. If taxpayers with higher incomes pay a larger percentage of their income than lower income taxpayers, then that tax or that tax system is called *progressive*. If a tax or a tax system takes a higher percentage of income from lower-income residents than higher income residents, that tax or that tax system is *regressive*. If a tax or a tax system takes the same percentage of income from lower-income residents and higher income residents, that tax or that tax system is *proportional*. Most state and local revenue systems are mildly regressive to proportional.

Some states (not including South Carolina) attempt to reduce the regressivity of their revenue systems with circuit breakers. *Circuit breakers* can increase tax equity for lower-income citizens by providing tax credits that are phased out as income rises.

**Efficiency:** A perfect tax would not discourage desirable activities like building a house or moving a business firm to the state or to a particular county or city, but it might be used to discourage an undesirable activity like smoking or gambling.

**Cost of collection and compliance:** A perfect tax would be easy to administer and inexpensive to collect, so the state doesn't spend a lot in the process of collecting revenue. The burden on the taxpayer (or retailer in the case of a sales tax) is called compliance cost, and it too would be very low for the ideal tax.

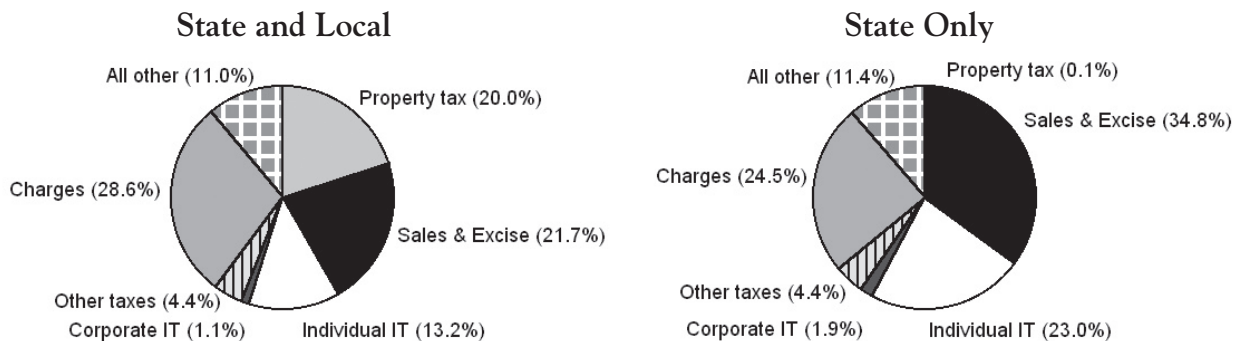
### ***a perfect tax?***

► No tax fits all criteria of a *perfect* tax, so there is no perfect tax. The positives of one tax or fee, then, will need to balance the negatives of another to create a *good* revenue system. The answer in South Carolina and most other states is to create a revenue system that uses a mix of taxes and fees.

**where South Carolina gets its revenue**

- ▶ State and local governments depend on taxes on wealth like real estate and personal property, taxes on what people buy and use, taxes on income, and fees for public services.
- ▶ States that do not use a mix of sales, income and property taxes have to use higher rates on other taxes to generate enough revenue. Tennessee, with no broad-based income tax and a very high sales tax, ranks 51st in per capita own-source revenue. Oregon, which has no sales tax, derives 75 percent of its revenue from the income tax, with rates ranging up to 9 percent.
- ▶ South Carolina uses the three major taxes (individual income, retail sales and property) as well as a number of minor taxes (corporate income and a variety of excise and other taxes). State and local governments also depend heavily on fees of various kinds for revenue. Minor taxes do not provide a lot of revenue but they serve other goals. For example, taxes and fees aimed at tourists, such as hospitality and accommodations taxes, can ensure that visitors pay for some of the local services that they use. Taxes on gasoline are intended to make the people who use highways the most pay a larger share of the cost of building and maintaining them. Taxes on luxuries can shift some of the burden of paying for public services to higher income families.
- ▶ In 2004, South Carolina’s state-only general revenue from own sources came from general sales and excise taxes (35%), fees and charges (25%), individual income taxes (23%), and other sources (18%). Combined state and local own-source revenue relied more heavily on fees and charges (29%), then sales and excise taxes (22%), property (20%) and individual income (13%) taxes.

**S.C. State and Local Revenue Shares, 2004**



# Revenue By the Numbers

## **the challenge**

- ▶ When taxpayers think about taxes and tax revenue, they usually want to know whether the tax burden is growing in their state and how their taxes compare to taxes paid by residents of other states.
- ▶ It may seem that these questions should be easy to answer, but they're not. Different ways of phrasing the question or formulating an answer can give very different pictures of how one citizen or one state compares to another.

## **what it is**

- ▶ **Total revenue** is all the funds available for a state or local government to spend from any source, including intergovernmental aid..
- ▶ **Intergovernmental** revenue comes from outside. For states, it is mostly from the federal government. For local governments, it comes from the federal, state, and other local governments.
- ▶ **Own source revenue** is the revenue that state and local governments raise by themselves. It is the best measure for comparing the tax burdens in different states because it excludes intergovernmental aid.
- ▶ **General revenue**, unlike total revenue, does not include the revenue from public enterprises like water and sewer, or other enterprise funds that can only be used for a particular purpose. General revenue is a better measure than total revenue of the funds available to a state or local government.

## **per capita revenue**

- ▶ **The question.** How much does South Carolina collect per person in state and local revenue from taxes, fees and other sources?
- ▶ **The math.** Divide total own source revenue by the number of people living in the state, including children. The answer is called *per capita revenue*.
- ▶ **The answer.** In 2004, South Carolina collected \$4,408 per capita in state and local revenue from own sources. That's \$578 less than the national average, \$92 more than in North Carolina, and \$201 more than in Georgia.
- ▶ **The rank.** South Carolina ranked 36th among the states (including the District of Columbia) in per capita own-source revenue. Mississippi, Arkansas, and Tennessee were at the bottom, each with less than \$4,000 per capita. Alaska topped the list at \$9,284 per capita.

► **Cautions.** Per capita own-source revenue doesn't mean that every South Carolinian paid \$4,408 in taxes and fees in 2004. Some paid more, some paid less. Also, some taxes and fees were paid by people from other states who vacation, shop, work, or own property here. These nonresidents are not included in per capita revenue calculations. For example, Alaska and Wyoming both ranked near the top in per capita revenue, but these states have revenue related to oil and minerals. Delaware, the home of many out-of-state corporations because of favorable incorporation laws, receives a lot of corporate income tax revenue.

► Per capita revenue is most useful in comparing how much the state and local governments have in the way of resources to provide public services, since service demands are closely tied to population. A state may be low in per capita taxes simply because its citizens have a low income, not because it has low tax rates.

***growth in per capita revenue***

► **The question.** Is state and local revenue per capita in South Carolina growing faster than the average person's income?

► **The math.** Apply the same math as in the previous question to data for the year 1994. Subtract the answer for 1994 from the answer for 2004.

► **The answer.** In 1994, per capita own-source revenue was \$2,846. Own-source revenue per capita in 2004 was \$4,408, but much of the \$1,562 increase over the decade was from inflation. After adjusting for inflation, per capita revenue rose 17.1 percent from 1994 to 2004.

► **The rank.** South Carolina rose from 40th to 36th over that ten-year period in per capita state and local revenue from own sources.

► **Cautions.** Growth in South Carolina's per capita state and local revenue since 1994 averaged 1.6 percent per year, faster than the national rate of 1.2 percent. However, per capita revenue in South Carolina in 2004 remains well below the national average of \$4,986.

**revenue in  
relation to income**

- ▶ **The question.** What share of state personal income goes to state and local government in the form of taxes, fees, and other revenue?
- ▶ **The math.** Divide total state and local own-source revenue collected by the total personal income of state residents. The answer is called *revenue as a percent of personal income*.
- ▶ **The answer.** In 2004, South Carolina state and local revenue as a percent of personal income was 16.2 percent. That's higher than the national average of 15.1 percent, and higher than in North Carolina (14.7%) and in Georgia (14.1%). In 1994, South Carolina's state and local revenue was 15.5 percent of personal income. The increase in this number means that revenue grew a little faster than personal income over the decade of the nineties.
- ▶ **The rank.** In 2004, South Carolina ranked 11th in state and local revenue as a percent of personal income. South Dakota, Tennessee, and New Hampshire shared the bottom at 12-13 percent. Alaska topped the list again at 27.3 percent.
- ▶ **Cautions.** South Carolina ranks higher among the states when comparing revenue as a percent of income instead of per capita income. This difference in rankings reflects the state's low per capita income, not high tax rates. South Carolina's per capita personal income is about 82 percent of the national average.

# State Sales and Use Taxes

## ***what it is***

- ▶ Taxation of retail sales of tangible goods at a rate of 6 percent (as of June 1, 2007) paid by the buyer. Non-prepared food is taxed at a lower rate of 3 percent.
- ▶ Out-of-state purchases are subject to a use tax at the same rate as retail sales, but with a credit for taxes paid to other states.
- ▶ Goods and services subject to the tax are found in Title 12, Section 36 of the S.C. Code of Laws. South Carolina taxes most tangible goods but very few services, like most states.

## ***revenue***

- ▶ South Carolina collected \$2.7 billion in sales and use taxes, about 26 percent of state own-source revenue in 2004.

## ***features***

- ▶ Retail business firms collect the tax for the Department of Revenue.
- ▶ Use taxes on out-of-state purchases must be reported by the taxpayer on the state income tax form. Enforcement is difficult but the state is working on increasing revenue from the use tax.

## ***exemptions***

- ▶ Most services are not subject to the sales tax, although some are subject to excise taxation.
- ▶ By federal regulation, purchases made with food stamps are exempt.
- ▶ Prescription drugs, Bibles, textbooks, livestock sales, and toll charges for transmission of messages are not taxed.
- ▶ Purchases by business and agricultural operations for resale, for use in production, or for further processing are exempt.
- ▶ The sales tax on motor vehicles, boats, and airplanes is capped at \$300. The purchaser of a \$6,000 used car pays the same tax as the purchaser of a \$60,000 luxury car. The revenue loss from this exemption is about \$100 million a year.

## ***cautions***

- ▶ Tax holidays and adding new exemptions cause revenue loss for the state.
- ▶ Increased spending on non-taxed services, catalog purchases and internet sales mean that sales tax revenue does not keep pace with inflation and population growth.

- ▶ Catalog purchases and internet sales, which are mostly untaxed, not only result in loss of revenue for the state but also create a handicap for local “Main Street” merchants.
- ▶ High state sales tax rates combined with local sales taxes can encourage cross-border, catalog, and internet shopping, with cross-border shopping especially likely in South Carolina’s 20 counties that border North Carolina and Georgia.
- ▶ Too many exemptions can make the sales tax more expensive to collect, erode the tax base and require a higher tax rate to bring in the same revenue.
- ▶ Failure to tax services favors middle- and high-income households and makes the sales tax more regressive.

### ***other states***

- ▶ Forty-five states tax general retail sales. About two-thirds (26 of 45) of these states exempt food completely. No other state places a ceiling on sales taxes for cars, boats, and airplanes. Hawaii, New Mexico, and South Dakota and a few other states levy retail sales taxes on many services in addition to tangible goods. South Carolina’s state sales tax rate of 6 percent is the most common rate, but only 9 states have higher statewide rates, while 25 have lower rates.

### ***evaluation***

- ▶ ***Adequacy:*** The tax receives good marks for adequacy because sales tax revenues grow almost but not quite as fast as personal income.
- ▶ ***Equity:*** The tax is regressive because taxable purchases are a higher percentage of income for lower-income households. The taxation of food and the cap on taxes on vehicles, boats, and airplanes makes the tax more regressive.
- ▶ ***Efficiency:*** If tax rates get too far out of line with those in other states, cross-border shopping and catalog and internet shopping may increase, resulting in revenue loss as well as reduced income to in-state merchants.
- ▶ ***Cost of collection and compliance:*** The sales tax is not expensive to administer, although much of the cost falls on merchants. Sales taxes are paid in small amounts over time, making them more acceptable than other taxes to taxpayers. The consumer can also decide whether or not to purchase taxed items. Collection of the use tax depends on self-reporting by the taxpayer. The state forgoes revenue from the use tax because it has not developed a more efficient collection system.

# Local Sales Taxes

## **what it is**

- ▶ The local option sales tax is an additional tax on retail sales of tangible goods at a rate of one percent. It has been adopted by 29 counties.
- ▶ Other local sales taxes are additional taxes on retail sales of tangible goods at a rate of one or two percent to specifically fund capital projects, transportation, and schools. Fifteen counties are using these taxes.

## **revenue**

- ▶ \$161 million from general local option sales taxes in 2004. The largest share of this revenue is used for property tax relief each year.
- ▶ An additional \$28 million allocated to specific local capital projects in 2004.

## **features**

- ▶ Counties and their municipalities share revenue from the local option sales tax in 29 counties. Citizens must approve its use in a county referendum.
- ▶ Only counties can levy sales taxes for specific purposes, although they may direct some of the revenue to school purposes.
- ▶ By law, at least 71 percent of revenue from the local option sales tax goes to reduce county and municipal real estate taxes. Some counties and municipalities allocate 100 percent of the revenue to reducing taxes. In others, the remainder goes to fund county and municipal budgets.
- ▶ The revenue from the local option sales tax used for property tax reduction is distributed based on the market value of properties, rather than tax assessments, so homeowners get a proportionately higher share of the relief.
- ▶ Sales taxes that are levied for specific purposes must terminate when the bonds associated with the projects have been repaid.

## **exemptions**

- ▶ Vehicles, boats, and airplanes are exempt from local sales taxes. Other items and services exempt from state sales taxes also are exempt locally.

### ***cautions***

- ▶ Changes in state sales tax exemptions can adversely affect local revenue.
- ▶ The same cautions related to the state retail sales tax also apply to local retail sales taxes.

### ***other states***

- ▶ The state's combined state and local retail sales tax rate of 7 percent in counties with the local option sales tax is the same as Georgia's maximum combined rate and just below North Carolina's (7.5%). Tennessee's maximum combined rate is high at 9.75 percent, because the state has no broad-based income tax.

### ***evaluation***

- ▶ ***Adequacy:*** Local sales taxes receive good marks for adequacy because tax revenues grow with personal income, but a little more slowly.
- ▶ ***Equity:*** Local sales taxes are regressive because taxable purchases are a higher percentage of income for lower-income households. The taxation of food adds to that inequity.
- ▶ ***Efficiency:*** Retailers may choose to locate in counties without the local sales taxes, but if they do, they may find that their property taxes are higher.
- ▶ ***Cost of collection and compliance:*** Local sales taxes are not expensive to administer because merchants already report sales to the state. Most of the cost falls on merchants.

# State and Local Excise Taxes

## **what it is**

▶ Taxation of a good or service, like gasoline, usually based on the quantity sold rather than the dollar value of the sale.

## **revenue**

▶ \$963 million in state excise tax revenue in 2004, about 9 percent of state own-source revenue.

▶ \$206 million in local excise taxes in 2004.

## **features**

▶ The state collects most excise taxes and sends some of them back to counties and municipalities.

▶ The state levies excise taxes on gasoline, distilled spirits, beer, wine, tobacco products, admission to entertainment and sporting events, public utilities, coin-operated devices, and bingo games, among others.

▶ Local governments are allowed to levy taxes on public utilities, accommodations, and restaurant meals. Excise taxes on accommodations and restaurant meals are based on the dollar value of the purchase, rather than on the quantity sold.

▶ A 2 percent accommodations tax is levied statewide and distributed to the counties and cities of origin. Counties and cities may also levy an additional local accommodations tax as long as the total local tax does not exceed 3 percent. The accommodations tax is used to pay local government costs created by visitors, such as law enforcement and litter control. It also funds the promotion of tourism and tourism facilities.

▶ Revenue from the excise tax on gasoline is earmarked for building and maintaining highways and public transportation. South Carolina's rate of 16 cents per gallon is among the lowest in the nation.

▶ Addictive activities like smoking and drinking alcohol are attractive targets for excise taxes. States tax addictive substances both to raise revenue and to discourage consumption. Revenue from excise taxes goes into the state's general fund. South Carolina has higher than average tax rates on beer and wine and lower rates on distilled spirits. The 7 cents per pack tax on cigarettes is the lowest in the nation.

**cautions**

▶ If excise taxes are not routinely adjusted for inflation, the reduction in the purchasing power of the excise tax amounts to an annual tax cut. As the price of a gallon of gas or a pack of cigarettes rises, the excise tax per gallon or per pack remains the same, but the revenue buys less in state services.

**other states**

▶ State and local governments in South Carolina received 10.5 percent of their tax revenue from excise taxes in 2004. North Carolina brought in 12.3 percent from excise taxes in 2004 compared to Georgia's 9.1 percent.

▶ Every state has accommodations taxes at some level.

**evaluation**

▶ **Adequacy:** Excise taxes represent a small and declining share of state revenue in South Carolina. Between 1994 and 2004, state excise tax revenue declined from 6.6 percent to 6.2 percent of general revenue from own sources.

▶ **Equity:** Many but not all excise taxes are regressive.

▶ **Efficiency:** Excise taxes may induce residents to purchase and use fewer undesirable goods such as alcohol or tobacco. The gasoline tax ensures that highway users pay a portion of the cost of their highway use.

▶ **Cost of collection and compliance:** Most of the cost falls on producers or retailers but the state incurs some collection cost as well.

# Local Property Taxes

## ***what it is***

► Taxation of real and personal property based on a percentage of market value at rates from 4 percent to 10.5 percent, depending on the classification of property.

## ***revenue***

► Local governments collected almost \$4 billion in local property tax collections in 2004. \$434 million of this total came from state funds to pay local governments for property tax relief, and \$93 million came from local sales taxes for property tax relief.

► \$2.6 billion went to school districts, \$1.1 billion to counties and municipalities and \$222 million to special purpose districts.

## ***property classification***

► Property taxes are levied on a percentage of the market value of property. The percentage applied to each class of property (assessment rate) is specified in the state's constitution.

► The assessment rates are:

4 percent for owner-occupied housing and noncommercial farm land.

6 percent for rental and commercial property, commercial agriculture, and personal vehicles.

9.5 percent for companies offering transport for hire, such as freight haulers and bus companies.

10.5 percent for manufacturing, utilities, and personal property other than personal vehicles.

► New and expanding industries can negotiate with counties to pay a fee in lieu of taxation instead of paying taxes based on the assessment rate of 10.5 percent. In some cases, fees effectively reduce industrial tax assessment rates to 4 percent, the residential property rate. Under fee-in-lieu agreements, an industry can be exempt from tax increases for an agreed upon period of time.

► Property classified as farm and forest, now including golf courses, is assessed at use value rather than market value, which results in very low tax bills.

### ***exemptions and property tax relief***

- ▶ The first \$50,000 of market value of an owner-occupied house is exempt from local property taxes for persons over 65 years of age— a homestead exemption. The state reimburses local governments for the lost revenue.
- ▶ From 1995 through 2006-07, the first \$100,000 of the market value of all owner-occupied houses was exempt from property taxes for education operations (not debt service) at the tax (mill) rate in effect in 1995. This exemption is in addition to the homestead exemption. The state does not fully fund the exemption, so some of the cost falls on school districts.
- ▶ Beginning with tax bills sent at the end of 2007, the entire market value of all owner-occupied houses will be exempt from property taxes for education operations (not debt service). The state will reimburse school districts using the funds generated by raising the state sales tax from 5 percent to 6 percent. In future years, increased payments to districts will be based on inflation and growth of school population.

### ***features***

- ▶ The property tax rate, or mill rate, is the amount per \$1,000 of assessed value. 100 mills would be \$100 per \$1,000 of assessed value, or 10 percent.
- ▶ The state authorizes local governments (cities, counties, school districts, and special districts) to levy the property tax and sets up the rules for the operation of the tax.
- ▶ Counties normally administer property taxes for school districts, municipalities, and special districts.
- ▶ The property tax is a tax on assets, but not all assets are taxed. Land and buildings including mobile homes are taxed as real property. Cars, boats, airplanes, motorcycles, manufacturing equipment, business vehicles, farm equipment, and furnishings for commercial and rental properties are taxed as personal property. Investments, bank accounts, and personal possessions and furnishings, which are also assets, are not taxed.
- ▶ County and municipal taxes pay for services which protect or enhance the value of property, such as police protection, fire departments, street lights, street maintenance, zoning administration, and parks. Good public services may permit owners of rental property to charge higher rents to offset the higher taxes they pay for those services. Special purpose districts (created before 1974) and special tax districts (created by county councils since 1974) collect taxes to pay for specific services such as fire protection, street lights, or recreation.

▶ The state usually reimburses local governments for lost property tax revenues when it passes legislation that reduces their property tax income. The reimbursements include money to pay for revenues lost when the legislature ended the tax on merchants' inventories, adopted homestead exemptions for the elderly, and passed property tax relief from school taxes for the first \$100,000 value of owner-occupied houses. The state does not reimburse local governments for the loss of personal property tax revenues brought about by the reduction in the assessment rate on personal vehicles from 10.5 percent to 6 percent.

### ***cautions***

▶ Tax exemptions such as the homestead exemption do not necessarily make the state and local tax systems less regressive or more equitable. The recent increase in the property tax relief for homeowners was funded by a regressive tax with the benefits going to people owning homes worth more than \$100,000. Renters, whose rent reflects the cost of paying property taxes, got no relief.

▶ The strategy of attracting retirees with low property (and income) taxes may ultimately prove costly because retirees can also add to the costs of services, especially as they grow older and place increased demands on the state health care system.

▶ Reimbursing local governments for cuts in property taxes has been and could continue to be a considerable drain on the state budget. In 2004, the state appropriated \$485 million to repay local governments for property tax relief.

▶ School districts with less taxable wealth must levy higher mill rates to provide the same level of education as districts with larger property tax bases. The state offsets some of the difference by giving more money per pupil to poorer districts.

### ***other states***

▶ Every state levies property taxes. In most states the tax is local and a large share finances education. South Carolina state government exercises much more control over local property taxes than most other states.

▶ South Carolina is one of only seventeen states that assess property at different rates depending on classification rather than at a single flat rate.

## ***evaluation***

- ▶ ***Adequacy:*** The tax receives fair marks for adequacy because it is a stable tax that grows somewhat slowly. Tax revenue from new property lags one or two years behind its completion.
- ▶ ***Equity:*** The tax on real property is regressive in South Carolina because many low-income families live in rental housing, which is assessed at a higher rate than owner-occupied homes. Spending on housing also takes a higher percentage of income for low-income households. Only homeowners get the tax exemption for property tax for the schools. Tax breaks for the elderly are generous, but not all elderly people have low incomes.
- ▶ ***Efficiency:*** High property taxes in poorer school districts make it hard to attract industry. Firms like locations with both low tax rates and good schools.
- ▶ ***Cost of compliance:*** The property tax system is expensive to administer, although it is easy to comply with as an annual bill.

# State Income Tax

## **what it is**

- ▶ Taxation of income of individuals at rates ranging from 2.5 percent to 7 percent.
- ▶ Taxation of income of corporations and unincorporated businesses (proprietorships and partnerships) at 5 percent of profits or net income.

## **revenue**

- ▶ \$2.4 billion from individuals in 2004, or 23 percent of state general revenue from own sources and 35.8 percent of state tax collections.
- ▶ \$197 million from corporations in 2004, or only 1.9 percent of own-source general revenue and 2.9 percent of tax revenue.

## **features**

- ▶ South Carolina bases its definition of gross income on the federal definition, using the same adjustments, deductions, and exemptions. When the federal rules change, so does the state tax code.
- ▶ The state adjusts the tax brackets for inflation every year. Federal tax deductions, exemptions, and brackets are also adjusted for inflation yearly. Federal adjustments in exemptions and deductions are automatically carried over into the South Carolina income tax.
- ▶ The tax on individuals is mildly progressive; that is, the amount of tax due increases more than in proportion to increases in taxable income.
- ▶ The revenue from the corporate income tax is quite low in South Carolina because of the low rate (5% compared to 6% in Georgia, 6.5% in Tennessee and 6.9% in North Carolina) and the extensive use of business location incentives in order to attract industry.

## **tax breaks**

- ▶ New and expanding firms receive credits against the corporate income tax for creating jobs and making capital investments.
- ▶ The biggest individual income tax breaks go to retirees. All social security income is exempt. Pension income up to \$3,000 is not taxed for persons up to age 65. Persons 65 or older can exempt \$10,000 in pension income.

▶ Children under the age of six receive double exemptions. The state also offers a child care credit for children under 15 years of age.

### **cautions**

▶ The income tax can be easily adapted through adjustments, exemptions, deductions and credits to make allowances for differences in ability to pay or to address special needs, such as families with children, the elderly, or concerns about the environment. However, this very flexibility is an invitation to lobbyists for special interests to seek changes that reduce revenue and lessen the fairness of the system.

▶ Changes in the federal income tax, carried over into the state system, sometimes reduce revenue from both the individual and corporate income tax.

### **other states**

▶ Thirty-five states and the District of Columbia have progressive individual income taxes, while another 6 states in 2006 have flat-rate individual income taxes. Vermont has the highest top bracket rate for personal income at 9.5 percent. South Carolina's range of rates is about average, but the income level of \$12,850 where the highest rate begins is lower than in many other states. Some states also have local income taxes, but South Carolina does not.

### **evaluation**

▶ **Adequacy:** This tax receives highest marks for adequacy because it produces a lot of revenue, but it is very vulnerable to economic downturns with falling revenues. As personal income grows, tax revenues grow slightly faster.

▶ **Equity:** As the only progressive tax in the state tax system, the individual income tax helps to offset regressive taxes such as the sales tax. Tax breaks for the elderly shift some of the individual income tax burden to younger taxpayers.

▶ **Efficiency:** With two nearby states (Florida and Tennessee) having no broad-based income tax, this tax may discourage higher-income persons from either relocating to South Carolina or remaining here. However, other states may have higher sales and/or property taxes or lower quality public services.

▶ **Cost of compliance:** The individual income tax is not very expensive to administer and fairly easy for taxpayers to file because of its link to the federal tax system.

# Fees and Charges

## **what is a fee?**

► Fees are primarily payments in exchange for a government service available to all taxpayers, such as garbage collection, or a service that only a part of the community uses or values, such as public tennis courts or parking garage spaces. Unlike taxes, there is a close link between the payment and the service it supports. Most fees are more nearly optional than taxes, and are not based on such criteria as spending, income or wealth.

## **revenue**

- \$5.3 billion or about 29 percent of state and local own-source revenue in 2004.
- \$2.6 billion to state government and \$2.7 billion to local governments in 2004.

## **features**

- Fees provide an alternative revenue source when taxpayers object to additional taxes or the General Assembly limits the use of certain taxes.
- Fees are collected for many purposes: car registration, drivers' licenses, use of recreational facilities, garbage collection, fire inspection, traffic fines, parking, and building permits.
- Some services are financed partly by taxes and partly by fees in order to encourage use of the service. Low public transportation fares and low garbage collection fees encourage use of services that benefit the community by reducing traffic congestion and keeping the community clean and healthy.
- Many local governments provide water and sewer services for fees based on how much is used. These services are run like private enterprises, with the fee or charge intended to cover the cost of providing services. The fees are kept separate from a government's other revenue funds in *enterprise funds*. Tax revenues normally are not spent on these services.
- Municipalities rely most heavily on fees and charges, followed by counties. Municipalities sometimes charge nonresidents fees that are higher than fees to residents for using municipal facilities and services.

### ***cautions***

- ▶ Many government services should be available to everyone, regardless of ability to pay. The use of fees instead of taxes can limit access to these services for low-income residents, who often rely more on public services. In some cases, services can be made more accessible by using a sliding scale fee based on income.
- ▶ Fees can be costly to collect relative to the revenue they generate, particularly for low-usage services like toll roads with limited traffic or parks in the cooler months of the year.

### ***other states***

- ▶ South Carolina's governments rank well above the national and southeastern average in the use of fees. State and local governments in South Carolina collect over \$1,200 per resident in fees and charges.

### ***evaluation***

- ▶ ***Adequacy:*** If fees and charges are set to cover the full cost of a service, they will be adequate but may exclude low-income residents and thus reduce equity in access to public services.
- ▶ ***Equity:*** Overall, fees and charges are more burdensome to lower-income citizens when fees are the same for everyone. Fees are also regressive because low-income households tend to rely more on public services.
- ▶ ***Efficiency:*** When services are tax-financed, they appear to be free, so citizens demand more than they would if they had to pay at least part of the cost. Fees ensure that people pay at least part of the cost and that those who do not want or benefit from the service are not required to pay for it for others.
- ▶ ***Cost of collection and compliance:*** Some fees are inexpensive to collect while others can be costly if volume is low, particularly if a "gatekeeper" is needed (tolls, parking fees, entrance fees to parks).

# What Can a Citizen Do?

## ***the challenge***

- ▶ A democratic system of government depends on the participation of informed citizens. Citizens who are aware and informed on public issues are an important counterweight to special interests demanding services for their own benefit or trying to lower their own tax burdens. Citizens must represent the general interests when decisions are being made not only about the appropriate level of taxes, but also about the quality of public services like education, transportation, and public safety.
- ▶ Citizens also need to make sure that the interests of families and children, the poor and the elderly, and communities and people with special needs get an equal place at the tax policy and budgeting table. Without concerned citizens expressing their views, legislators and local officials may only hear from self-serving special interests.
- ▶ Tax policy matters very much to every citizen and every household. Tax policy determines how much you pay in taxes, who bears the costs, and what resources our state, cities, counties, and school districts have with which to provide quality public services.
- ▶ If you've been interested enough to read this booklet, you might be one of those citizens who wants to make a difference.

## ***state budgeting***

- ▶ The state builds its budget in the spring. The legislative session runs from January to June, and the new fiscal year starts July 1. However, legislators are also considering new ideas and proposals in the off-season. So watch for emerging developments during the late fall, particularly in election years as new ideas are being developed to catch the voters' attention.
- ▶ The formal budget process starts when the governor puts together his budget proposal. His budget is the basis for the state-of-the-state address delivered in January and is forwarded to the House, where budgets must begin by law. The House sends its budget to the Senate. After the Senate adopts its version, the budget goes to a joint committee of the House and Senate that prepares the final version for the House to vote upon. It is then sent to the governor for his signature or vetoes. The governor can veto individual items (line-item veto).

### ***local budgeting***

- ▶ Most local governments build their budgets in the spring, from March through June, because most of them operate on a fiscal year from July 1 to June 30. Others budget on the calendar year or from October 1. Watch for budget hearings. Get acquainted with local public officials and with the basic outline of where the money comes from and how it is spent.
- ▶ Local governments are required by law to have an annual audit, to publish and hold public hearings on their budgets before adoption, and to adopt a balanced budget.

### ***get information***

- ▶ On the state level, you can get information directly from the General Assembly at [www.scstatehouse.net](http://www.scstatehouse.net). Clicking on the legislative manual will take you to a legislator's telephone number, e-mail address, and postal address. If you are looking for budget bills and other tax policy legislation, you'll find them here. Choosing the government section at [www.sc.gov](http://www.sc.gov), the state web site, will also take you to the General Assembly.
- ▶ Many local governments have web sites that will let you know when budget and tax decisions are being made. Local newspapers carry schedules for meetings, work sessions and public budget hearings where many decisions are made. The Municipal Association of South Carolina and the South Carolina Association of Counties also provide information on local tax policy proposals and issues of interest to citizens. An easy way to find web sites for local governments and these two associations is through the government link at [www.myscgov.com](http://www.myscgov.com). Don't overlook the link to your Regional Council of Government, which is another useful resource.
- ▶ If you don't have a computer or don't know how to use one, drop by your local library for help in getting on the Internet.
- ▶ South Carolina tax policy research by Clemson University's Strom Thurmond Institute of Government and Public Affairs is found at [www.strom.clemson.edu](http://www.strom.clemson.edu). USC's Institute for Public Service and Policy Research has produced reports on tax policy that can be found at [www.iopa.sc.edu](http://www.iopa.sc.edu).

**information  
sources**

Federation of Tax Administrators: <http://www.taxadmin.org>

Governing Magazine (management): <http://governing.org>

Institute of Taxation and Economic Policy: <http://www.itepnet.org>

Who Pays: <http://www.ctj.org/itep/index.htm>

National Association of State Budget Officers:  
<http://www.nasbo.org/publications.php>

Tax Foundation: <http://www.taxfoundation.org>

Tax Policy Center: <http://www.taxpolicycenter.org>

The Urban Institute-Brookings Institution Tax Policy Center.  
State & Local Government Finance Data Query System:  
<http://www.taxpolicycenter.org/slf-dqs/pages.cfm>

U.S. Census Bureau, State and Local Government Finances:  
<http://www.census.gov/govs/www/estimate.html>

National Center for Education Statistics: <http://nces.ed.gov>

S.C. Comptroller General: <http://www.cg.state.sc.us>

S.C. Home Page (choose government section): <http://www.mysc.gov.com>

S.C. Department of Commerce (publications on business incentives and  
S.C. property tax rates): <http://www.teamsc.com/library.html>

S.C. Department of Revenue: [http://www.sctax.org/annual\\_report/tables.htm](http://www.sctax.org/annual_report/tables.htm)

S.C. Office of State Budget: <http://www.budget.sc.gov/osb.historical>

