

SC REVENUE RULING 06-1

- SUBJECT:** Nonresident Military Servicemembers
(Income Tax)
- EFFECTIVE DATE:** For individual tax returns filed for tax years 2003 and thereafter.
- SUPERSEDES:** All previous advisory opinions and any oral directives in conflict herewith.
- REFERENCES:** Title 12, Chapter 6 of S.C. Code of Laws
- AUTHORITY:** S.C. Code Ann. Section 12-4-320 (2000)
S.C. Code Ann. Section 1-23-10(4) (2005)
S.C. Revenue Procedure #05-2
- SCOPE:** The purpose of a Revenue Ruling is to provide guidance to the public and to Department personnel. It is an advisory opinion issued to apply principles of tax law to a set of facts or general category of taxpayers. It is the Department's position until superseded or modified by a change in statute, regulation, court decision, or another Departmental advisory opinion.

Introduction

Due to changes in federal law, nonresident military servicemembers¹ may qualify for a refund of some South Carolina income taxes paid for years 2003 or 2004 in either of the following circumstances:

1. The nonresident servicemember and spouse filed a joint South Carolina income tax return for tax years 2003 or 2004 as nonresidents and the spouse earned non-military income in South Carolina for that period; or
2. The nonresident servicemember filed a South Carolina income tax return for tax year 2003 or 2004 as a nonresident and earned nonmilitary income in South Carolina (such as from a second, nonmilitary job) for that period.

These potential refunds are a result of a change in federal law that affects how personal exemptions and deductions against state income tax are computed for certain nonresident servicemembers. Servicemembers who are residents of South Carolina are not affected.

¹ Nonresident military servicemembers are those servicemembers whose state of legal residence is a state other than South Carolina. Servicemembers whose state of legal residence is South Carolina are taxed on military income earned in South Carolina to the extent that income is taxable under Federal law.

Law and Discussion

The federal Servicemembers Civil Relief Act (SCRA)², which became law December 19, 2003, updates and revises the Soldiers' and Sailors' Civil Relief Act of 1940.³ The SCRA states that "a tax jurisdiction may not use the military compensation of a nonresident servicemember to increase the tax liability imposed on other income earned by the nonresident servicemember or spouse that is subject to tax by the jurisdiction." In other words, "a nonresident servicemember's military compensation cannot be used to increase the tax liability for other income of the servicemember or spouse. . . ."⁴

The SCRA was designed to negate a specific method of computation, "the so-called 'Kansas Rule' [or 'California Rule'] that permitted a state to tax the non-military income at a higher rate."⁵

In certain states with graduated income tax rates, the income tax rate which is applied to the off-base pay may be based on the servicemembers' total income, including military pay, and not the off-base pay only. Including military pay in the calculation can push the off-base pay into a higher tax bracket. That method of calculating state income tax is, sometimes called the "California Method" (although as many as 18 or more other states also use it).⁶

Although the relevant SCRA provision was drafted to address the specific Kansas method above, the SCRA's language is broad enough to prohibit other means of computing tax liability, including South Carolina's method of prorating personal exemptions and deductions against total income when applied to nonresident servicemembers with in-state non-military income or nonresident servicemembers with spouses having in-state income and filing jointly.⁷

Prior to the enactment of the Servicemembers Civil Relief Act, nonresident servicemembers included military income in their entire adjusted gross income (AGI) ("Income As Shown On Federal Return") in Column A of Schedule NR, but did not include military income in their South Carolina AGI ("South Carolina Income") in Column B of Schedule NR. This exempted such military income from South Carolina income taxes; however, it also reduced the servicemembers' prorated personal deductions and exemptions (and those of the servicemember's spouse if married and filing jointly). Since, under this formula, the AGI included the military compensation of the nonresident servicemember, the ratio used to prorate the exemptions and deductions could be lower than if the military income was not included in the

² Section 511(d) of the Servicemembers Civil Relief Act (SCRA), Pub. L. No. 108-189, 117 Stat. 2835, codified as amended at 50 App. U.S.C. § 571(d).

³ See Terry M. Jarrett, The Servicemembers Civil Relief Act: Important New Protections For Those in Uniform, J. Mo. B. 174, 178 (July/Aug. 2004).

⁴ H.R. REP. 108-81, 42-43, 2004 U.S.C.C.A.N. 2367, 2386.

⁵ Terry M. Jarrett, The Servicemembers Civil Relief Act: Important New Protections for Those in Uniform, J. Mo. B. 174, 178 (July/Aug. 2004), citing *United States v. State of Kansas*, 580 F. Supp. 512 (D. Kan. 1984), *aff'd*, 810 F.2d 935 (10th Cir. 1987).

⁶ H.R. REP. 108-81, 55-56, 2004 U.S.C.C.A.N. 2367, 2397.

⁷ The proration formula is required by S.C. Code § 12-6-1720 (2000 and Supp. 2005).

AGI. As such, applying the lower ratio against the exemptions and deductions could have caused an increase in South Carolina tax liability for nonmilitary income of the nonresident servicemember or spouse.

Conclusion

In accordance with the Servicemembers Civil Relief Act, a nonresident servicemember is no longer required to include any military income not taxable in South Carolina on Line 1, Columns A and B, on Schedule NR ("Nonresident Schedule") to SC Form 1040.

Note: Nonresident servicemembers due a refund for 2003 and 2004 should file an amended individual income tax return, Form SC 1040X and Schedule NR, for each year a refund is due and write "Nonresident Servicemember" across the top of the face of each return and Schedule NR.

SOUTH CAROLINA DEPARTMENT OF REVENUE

s/Ray N. Stevens
Ray N. Stevens, Director

March 28, 2006
Columbia, South Carolina