1993 S.C. Op. Atty. Gen. 47 (S.C.A.G.), 1993 S.C. Op. Atty. Gen. No. 93-18, 1993 WL 720081

Office of the Attorney General

State of South Carolina
Opinion No. 93-18
March 19, 1993

***1 SUBJECT: Taxation and Revenue—Compensation Of National Guard Members And Reservists**

The exclusion from income of the compensation of National Guard members and members of Reserve Units of the United States Armed Forces is not unconstitutional when reviewed in light of Davis v. Michigan, 489 U.S. 803, 109 S.Ct. 1500 (1989). Such exclusion is proper since both state employees (Guard) and federal employees (Reservists) equally receive the benefit. The benefit is not conferred based upon the source of the payment, and any potential different treatment of regular military personnel is justified by the significant difference between part-time military and full-time military.

QUESTION: Is the exclusion of income provided for by S.C.Code Ann. Section 12–7–570 (1976), constitutional in light of Davis v. Michigan, supra?

APPLICABLE LAW: S.C.Code Ann. Section 12–7–570 (1976); 4 U.S.C. Section 111 (1989).

DISCUSSION:

The pertinent part of 4 U.S.C. Section 111 is as follows:
The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States ... by a duly constituted taxing authority having jurisdiction, if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation.

This statute, which is coextensive with intergovernmental tax immunity, was interpreted in Davis v. Michigan, supra, in the following manner:
[4 U.S.C. Section 111] ... waives whatever immunity past and present federal employees would otherwise enjoy from state taxation of salaries, retirement benefits, and other forms of compensation paid on account of their employment with the Federal Government, except to the extent that such taxation discriminates on account of the source of the compensation.

Davis, supra, 109 S.Ct. 1500, 1505.

The Court further stated the presence of discrimination is not unlawful as long as "the inconsistent tax treatment is directly related to and justified by 'significant differences between the classes' ". Davis, 109 S.Ct. at 1508. Thus, under Davis, supra, before a violation of 4 U.S.C. Section 111 and correspondingly intergovernmental immunity is established, there must be a showing of three elements. First, the state tax statute must create a class that discriminates against federal employees. Second, the discrimination must be based upon the source of the income. Third, the discrimination must not be justified by significant differences between the classes. These elements are not violated by Section 12–7–570.

S.C.Code Ann Section 12–7–435(f) (Supp.1992) allows a deduction from South Carolina income for amounts received within the exclusion section of Section 12–7–570. Section 12–7–570 states the following:
No part of the compensation received by the members of the South Carolina National Guard from the State or from the Federal Government or by members of the reserve components of the armed forces of the United States who are

residents of this State from the Federal Government for services in performing their duties shall be considered as any part of the income, gross or net, of the respective members in computing income taxes payable to the State of South Carolina. But the provisions of this section shall not be applicable to income derived from tours of active military duty extending beyond the customary training periods established for national guard and reserve units.

A. Discrimination

*2 Discrimination in treatment between federal and state classes is a prerequisite to a violation of intergovernmental tax immunity. In Davis, supra, the Court expressed this prerequisite by stating "the retention of immunity in section 111 is coextensive with the prohibition against discriminatory taxes embodied in the modern constitutional doctrine of intergovernmental tax immunity". Davis, 489 U.S. at 813. In applying the discrimination test, the Court found Michigan retirees were exempt from tax while their counterpart federal retirees were taxed. The Court concluded "[i]t is undisputed that Michigan's tax system discriminates in favor of retired state employees and against retired federal employees". Davis, 489 U.S. at 814. Under Section 12–7–570, however, there is no discrimination.

A benefit given to some state employees does not require the granting of the benefit to all federal employees. What is required is that the "State treat those who deal with the [federal] Government as well as [the State] treats those with whom it deals itself." Phillips Chemical Co. v. Dumas Independent School District, 361 U.S. 376, 385, 80 S.Ct. 474 (1960). A tax does not discriminate "so long as the tax is imposed equally on the other similarly situated constituents of the State". United States v. County of Fresno, 429 U.S. 452, 462 (1977). Under South Carolina's taxation scheme, the State treats federal employees the same as it treats its own employees.

South Carolina has defined a class of employees that consists of members of the Guard (who are viewed in most respects as state employees) [1] and Reservists who are federal employees. All state employees are taxed except those who are state employees by virtue of being members of the Guard. Guard members are taxable on their income from duty beyond the customary training period. In fact, nontaxability of the income of a Guard member is limited solely to the income from customary training. When the Governor orders the National Guard into the active service of the State (see S.C.Code Ann. Section 25–1–1840 (1976)), the pay for such active duty is from the State (see S.C.Code Ann. Section 25–1–2200 (1976)). Such pay, because it is active duty pay not within the customary training period, is taxable. Further, when the Guard is called into federal duty by the Congress or President (see 10 U.S.C. Section 672), that pay is also subject to tax. See S.C.Tech.Adv.Memo 89–16. Corresponding to the treatment of state employees, all federal employees are taxed except those who are federal employees by virtue of being a Reservist (the counterpart to the Guard). Again, Reservists, just like Guardsmen, are taxable on their income from duty beyond the customary training period. Such consistent treatment of state and federal employees demonstrates no discrimination is exercised by the State.

B. The Source Of The Payment

Even if discrimination toward federal employees were found, Section 111 of Title 4 is not violated unless "such taxation discriminates on account of the source of the compensation". Here, any different treatment is not because of the source of the payment. The Guard and the Reserve for their customary training periods have the same source for payment as federal employees, i.e. the federal government. [2] Under 10 U.S.C. Section 261, the Army National Guard and the Air National Guard are part of the Reserve components of the United States Armed Forces. The funds for compensation of the Guard and the Reserve are part of the defense budget of the United States. Specifically, 32 U.S.C. Section 106 authorizes federal funds for appropriation to the Army National Guard and the Air National Guard. A member of the Guard engaged in annual training receives pay and allowances from the federal government. 32 U.S.C. Section 503. Thus, any difference in treatment of federal employees is not based upon the source of the payment since the source is the federal government for both Guard members and federal employees.

C. Significant Differences Between Classes

*3 Inconsistent tax treatment is not unlawful as long as the "inconsistent tax treatment is directly related to and justified by 'significant differences between the classes' ". Davis, 109 S.Ct. at 1508. We do not believe there is inconsistent treatment between state and federal employees in a constitutional sense; however, the potential for finding inconsistent treatment exists as to the taxable treatment of members of the regular Armed Forces. There is, however, a significant difference between the two which justifies the difference in treatment.

Guard members and Reservists serve in the military as part-time employees while regular Armed Forces are full-time military employees. National Guard members and Reservists serve annually for a customary training period. The Guard's training period is normally 48 weekend drills and an annual training period of 15 days each year. See 32 U.S.C. Section 502(a). Reserve members participate in at least 48 weekend drills and not less than 14 days of annual training. See 10 U.S.C. Section 270(a). Thus, in the absence of being placed on active duty, Guardsmen and Reservists pursue part-time military employment. Members of the regular military, however, do not pursue a part-time military position. Rather, members of the regular military are full-time Armed Forces personnel.

There is a direct relation between the tax benefit and the difference between the Guard/Reserve and the regular military. The exemption is available only for the income earned from the part-time duties of the job. In other words, the benefit is tailored to include only part-time duties and once those duties become full time, the benefit is no longer available. For example, income from full-time active duty is taxable whether the active duty is performed at the direction of the Governor (see Section 25-1-1840) or by direction of the Congress or President (see 10 U.S.C. Section 672). Thus, the benefit is directly related to the difference between the classes (part-time military employment versus full-time military employment) since only the part-time military income is exempt.

Further, the benefit is justified by the difference between members of the Guard/Reserve and the regular military. A Guard member or Reservist traditionally has a full-time civilian job in addition to the member's part-time military employment. The limited exemption of the Guard's or Reservist's military pay is justified as an inducement to assume a military career as a second job beyond civilian employment. Drilling on weekends and training approximately two weeks out of the year may present an impediment to the pursuit of the individual's civilian career. Further, the member of the Guard or Reserve may be placed on active duty by the State or Federal Governments for extended time periods. Such possibilities further present difficulties for the pursuit of a military career.

The pursuit of a military career does not present such difficulties for members of the regular military since there is traditionally no simultaneous pursuit of both a civilian and a military career. Accordingly, as an inducement to pursuing a military career by becoming a member of the Guard or the Reserve, the State has chosen to exempt a limited portion of the income of a member of the Guard or Reserve. This inducement is justified by the difficulties created by pursuing a part-time military career. Such difficulties are not presented to full-time military personnel. Accordingly, the different treatment is justified by the significant difference between the classes.

CONCLUSION:

*4 The exclusion from income of the compensation of National Guard members and members of Reserve Units of the United States Armed Forces is not unconstitutional when reviewed in light of Davis v. Michigan, 489 U.S. 803, 109 S.Ct. 1500 (1989). Such exclusion is proper since both state employees (Guard) and federal employees (Reservists) equally receive the benefit. The benefit is not conferred based upon the source of the payment, and any potential different treatment of regular military personnel is justified by the significant difference between part-time military and full-time military.

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Footnotes

1 See Attorney General's Opinion dated December 12, 1980, to Purvis W. Collins, from Kenneth P. Woodington; Perpich v. Department of Defense, 496 U.S. 334, 110 S.Ct. 2418 (1990); Maryland v. United States, 381 U.S. 41, 85 S.Ct. 1293, vacated 382 U.S. 159, 86 S.Ct. 305 (1965); Turner v. State, 494 So.2d 1292 (1986); Aube v. United States, 25 Cl.Ct. 351 (1992). Cf. Wells v. State, 524 So.2d 778 (1988); Commonwealth Dept. of Military Affairs v. Greenwood, 508 A.2d 292 (1986); and Yount v. State, 774 S.W.2d 919 (1989), for various purposes, found Guardsmen were not state employees.

2 We note that S.C.Code Ann. Section 25–1–3230 (1976) provides for a maximum of $1200 per year as a retirement benefit to the Guard. Such amount is exempt from taxation by Sections 12–7–570 and 25–1–3230. Further, state funds are paid for members of the Guard called into active duty by the Governor. See Sections 25–1–1840 and 25–1–2200.

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