



DOAA

Georgia Department
of Audits & Accounts

Greg S. Griffin
State Auditor

March 21, 2023

Honorable Chuck Hufstetler
Chairman, Senate Finance Committee
133 State Capitol
Atlanta, GA 30334

SUBJECT: Fiscal Note
House Bill 454 (LC 43 2769S)

Dear Chairman Hufstetler:

The bill makes several changes to income taxes. It updates state income tax conformity to the Internal Revenue Code (IRC) for federal changes enacted in 2022 and adds an exception to federal conformity for IRC Section 174 to allow expensing of research expenditures as allowed under that section in 2017. In addition, the bill proposes to make several changes to the state's personal income tax, including:

- Clarifies language regarding potential rate reductions of 0.1% that occur if conditions are met
- Relax the 5-year lookback condition for scheduled rate reductions to a 3-year lookback.
- Eliminate personal exemption amounts that take effect under current law for tax year 2024 and replace them with new standard deductions in like amounts based on filing status.
- Allow taxpayers itemizing deductions on their federal tax returns to choose between itemizing deductions or taking the new standard deduction on their Georgia returns.
- Create a new income tax credit for filers who itemize deductions on their Georgia returns in the amount of \$300. This credit would be nonrefundable and may not be carried forward.

Finally, the bill would amend the definition of "force majeure" for purposes of the new facilities jobs tax credit to include a pandemic for projects certified on or after July 1, 2023.

The IRC conformity section of the bill would be applicable to all tax years beginning on or after January 1, 2022; the new facilities jobs credit change would be effective July 1, 2023; and the remaining provisions would be effective for tax years beginning on or after January 1, 2024.

Impact on State Revenue

Georgia State University's Fiscal Research Center (FRC) estimated that the bill would decrease state revenue as shown in Table 1 on the following page. It should be noted that:

- The revenue effects are in comparison to the Governor's current revenue estimate, which incorporates tax provisions found in HB 1437 (passed in 2022).
- Current law and this bill contain annual personal income tax rate reductions of 0.1% if certain conditions are met. A rate reduction of 0.1% would equal approximately \$320 million in tax year 2027 (the table is presented by fiscal year), and the amount of that revenue loss would grow approximately 4% annually as a result of inflation and population growth (i.e., \$333 million in 2028, \$346 million in 2029).
- Revenue reductions in FYs 2027 and 2028 are primarily due to consecutive tax rate reductions assumed to occur in tax years 2027 and 2028. The rate reductions occur due to the three-year

lookback period in this bill. Under HB 1437, the five-year lookback period results in no rate reduction.

Details of the analysis are provided in the attached appendix.

Table 1. Estimated State Revenue Effects of LC 43 2769S

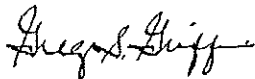
(\$ millions)	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028
Section 1	(\$30.9)	(\$6.3)	(\$0.7)	\$1.3	(\$1.8)
Sections 2-5:					
Rate Reductions ¹				(\$133.7)	(\$476.3)
Other Provisions	(\$63.8)	(\$156.4)	(\$103.9)	(\$22.2)	\$62.9
Sections 2-5 Total	(\$63.8)	(\$156.4)	(\$103.9)	(\$155.9)	(\$413.4)
Section 6	** Not Estimated **				
Total	(\$94.7)	(\$162.7)	(\$104.6)	(\$154.6)	(\$415.2)

¹ Rate reductions in current law are not expected to take effect during FY24-28 due to the law's five-year lookback period trigger not being met. Under this bill, a three-year lookback period is used, resulting in a rate reduction in the final two years.

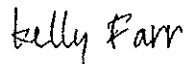
Impact on State Expenditures

The Department of Revenue (DOR) would be able to implement the provisions of the bill with existing resources. DOR estimated approximately 20 weeks to make the required changes to its information system, equating to approximately \$210,000 in staffing costs.

Respectfully,



Greg S. Griffin
State Auditor



Kelly Farr, Director
Office of Planning and Budget

GSG/KF/mt

Analysis by the Fiscal Research Center

Section 1 of LC 43 2769S updates conformity language of the Georgia income tax code to the Internal Revenue Code (IRC) in O.C.G.A. §48-1-2 to reflect changes enacted in 2022 in the Consolidated Appropriations Act (CAA) and the Inflation Reduction Act (IRA), adds an exception to federal conformity for IRC Section 174 to allow expensing of research expenditures as allowed under that section as in effect in 2017. Under the Tax Cut and Jobs Act of 2017, expensing, rather than capitalizing and amortizing, research expenditures was set to expire for all tax years beginning on or after January 1, 2022. Table 2 below details the projected revenue effects of conforming to the CAA and IRA as well as for the conformity exception to IRC Section 174. Note that the retroactivity of the conformity exception to January 1, 2022, is assumed to impact state revenues in FY 2024, after which the estimated cost of that provision returns to the trend of the five years before expensing of research costs expired.

Table 2. State Revenue Effects of IRC Conformity Section

(\$ millions)	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028
CAA items that affect Georgia	(\$6.9)	\$5.6	\$11.4	\$13.6	\$11.1
IRA items that affect Georgia	(\$3.5)	(\$3.0)	(\$2.8)	(\$2.5)	(\$2.7)
Conformity Exception to Sec. 174	(\$20.5)	(\$8.9)	(\$9.4)	(\$9.8)	(\$10.2)
Section 1 Net Revenue Effect	(\$30.9)	(\$6.3)	(\$0.7)	\$1.3	(\$1.8)

Sections 2-5 propose to make several changes to the state's personal income tax as follows:

- Relax the condition in O.C.G.A. §48-7-20(a.1)(2)(B) as in effect on and after January 1, 2024, that would cause deferral of an annual 10-basis-point rate reduction if the prior fiscal year's net revenue collections did not exceed that of each of the prior three fiscal years. Under current law, it must exceed collections of each of the prior five years for the rate reduction to proceed.
- Eliminate personal exemption amounts under O.C.G.A. §48-7-26(b)(1) as in effect on and after January 1, 2024 and replace them with new standard deductions in like amounts based on filing status in new subparagraph (B) of O.C.G.A. §48-7-27(a)(1).
- Revise O.C.G.A. §48-7-27(a) further so as to require taxpayers itemizing deductions on their federal tax returns to choose between itemizing deductions or taking the new standard deduction on their Georgia returns. Note that as is the case in current law, those taking the standard deduction on their federal returns may not itemize deductions on their Georgia returns.
- Create a new income tax credit for filers who choose to itemize deductions on their Georgia returns in accordance with new subparagraph (A) of O.C.G.A. §48-7-27(a)(1) in the amount of \$300. This credit would be nonrefundable and may not be carried forward.

The bill would be effective on and applicable to all tax years beginning on or after January 1, 2024.

Revenue effects of the bill are estimated using a microsimulation model and TY 2020 administrative tax return data from the Georgia Department of Revenue, specifically that of full-year resident filers. The simulation first recalculates net tax liabilities to reflect changes to the tax code from that in effect for TY 2020 to that in effect under current law as applicable to TY 2024 tax returns. Tax liabilities are then recalculated to reflect the changes proposed in this bill. The simulated aggregate percent change in tax liability is then applied to baseline personal income tax forecasts as of January 2023 from the Governor's Office of Planning and Budget (OPB).

As the annual contingent tax rate reductions are scheduled to begin in TY 2025, we use the OPB forecast of total net tax revenue to determine whether the conditions in O.C.G.A. §48-7-20(a.1)(2)(A) and (B) will have been met based on the forecasted revenues. That is, for example, the condition under subparagraph (A) will have been met for the TY 2025 rate reduction if fiscal year (FY) 2024 total net tax revenues exceed the revenues of each of the prior three years. The condition under subparagraph (B)

will have been met for the TY 2025 rate reduction if the governor's then-current forecast for FY 2026 total net tax revenues exceeds that of FY 2025 by at least 3 percent. We assume that the subparagraph (C) condition, relating to balances of the Revenue Shortfall Reserves, will have been met for all relevant periods.

Under current law, the OPB forecast of total net tax revenue, if realized but not materially exceeded, would not meet the conditions for a rate reduction during the time horizon of the forecast. The current-law lookback period under subparagraph (A) is five years and forecasted revenues through FY 2028 do not exceed actual FY 2022 revenues. Thus, the baseline for this analysis assumes not scheduled rate reductions occur during the TY 2025-28 period.

Table 3 presents the OPB baseline forecast for total net tax (TNT) revenues for FY 2024-28 along with proforma TNT revenues after giving effect to rate reductions under the conditions of the proposed bill. For each period, the subparagraph (A) 3-year lookback condition and the forward-looking subparagraph (B) conditions are evaluated, with the proforma forecast adjusted to reflect already-realized rate reductions when making the next year's evaluation.

Table 3 also presents the baseline and proforma personal income tax (PIT) revenues. Proforma PIT revenues in *italics* are for information purposes, enabling comparison of revenues under this bill to the baseline from changes other than the triggered rate reductions in TY 2027 and 2028 that are reflected in the bottom-line proforma estimates. The net revenue effect is presented in Table 1.

Table 3. Baseline and Proforma Rev. Forecasts, and Status of Rate Reduction Conditions

(\$ millions)	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028
OPB Baseline TNT Revenue	\$28,577.5	\$29,381.5	\$30,442.9	\$31,633.3	\$32,780.6
% change	-2.7%	2.8%	3.6%	3.9%	3.6%
Proforma TNT Revenue	\$28,513.7	\$29,225.1	\$30,338.9	\$31,477.5	\$32,367.2
% change	-2.9%	2.5%	3.8%	3.8%	2.8%
Rate for TY beginning in FY ¹	5.49%	5.49%	5.49%	5.39%	5.29%
OPB Baseline PIT Revenue	\$14,706.9	\$15,028.7	\$15,660.0	\$16,299.7	\$16,973.2
<i>Proforma PIT with no rate cut²</i>				<i>\$16,277.5</i>	<i>\$16,950.1</i>
Proforma PIT Revenue	\$14,643.1	\$14,872.3	\$15,556.1	\$16,143.8	\$16,559.8

¹ Rates are assumed to drop in TY27 and TY28 because all triggers would be met, including the bill's three-year lookback.

² PIT revenue if the rate remained at 5.49% in FY 2027 and FY 2028.

Section 6 of the bill amends the definition of 'force majeure' in O.C.G.A. §48-7-40.24, relating to the new facilities jobs credit, to make a 'pandemic', as defined, a force majeure for purposes of this credit's conditions, including the job maintenance and payroll maintenance requirements. This definitional change would be effective only for projects certified pursuant to subparagraph (b)(2) of this code section on or after July 1, 2023. Under this subparagraph, for a planned project to be eligible for the credit, a panel composed of the commissioner of community affairs, the commissioner of economic development, and the director of the Office of Planning and Budget must certify that the project's "new or expanded facility or facilities will have a significant beneficial economic effect on the region for which they are planned" based upon the application required by and described in paragraph (b).

This section also defines a pandemic such that it must "cause a substantial *and unforeseeable* threat to the public health, and materially [impact] the ability to conduct business" (emphasis added) in order to be a force majeure for purposes of this credit. Thus, this definitional change would not be applicable to projects already certified before July 1, 2023, nor presumably would a known, present, or recent pandemic meet the definition of a pandemic for purposes of this credit.

However, it is reasonable to conclude that, in the event of a future pandemic as defined, the state is likely to realize a material revenue loss due to this change and the resulting inability to enforce job maintenance and payroll maintenance requirements for the periods affected by the pandemic. No

information is available regarding the likely credits allowed to any as yet uncertified project, nor is it possible to assess the likelihood of a future pandemic impacting any project or this state. Thus, no estimate of the revenue impact of this provision is possible.