DEPARTMENT OF AUDITS AND ACCOUNTS

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Honorable Chuck Hufstetler
Chairman, Senate Finance
121 State Capitol
Atlanta, Georgia 30334

SUBJECT: Fiscal Note
House Bill 587 (LC 43 2010S)

Dear Chairman Hufstetler:

The bill would create or amend a number of tax credits and extend a sales tax exemption. These provisions include:

- Creating an additional jobs tax credit for manufacturers of medical device and pharmaceutical manufacturers. The $1,250 per new job credit would be in addition to the existing job tax credits. The provision would be effective for tax years beginning on or after January 1, 2021 and for jobs created after July 1, 2021.
- Increasing the maximum amount of port activity tax credits that can be utilized in a year. Currently, the credit can offset no more than 50 percent of state income tax liability. The bill would allow taxpayers to offset up to 100 of income tax liability and, if a balance remains, to offset payroll withholding tax liabilities. This would be effective for credits earned in tax years beginning on or after January 1, 2021.
- Amending the existing new facilities job credit to allow taxpayers, for a limited time, to claim credits for an unlimited number of new full-time jobs for a single project, where the current limit is 4,500 jobs. This change is effective for credits earned in tax years beginning on or after January 1, 2021.
- Extending the sunset date for sales tax exemptions for Competitive Projects of Regional Significance from June 30, 2021 to June 30, 2023.

Impact on State Revenue
Georgia State University's Fiscal Research Center (FRC) provided the estimates of revenue loss shown in Table 1; however, there were challenges with providing reliable estimates for some of the provisions. The attached appendix provides details of the analysis and the challenges are summarized below.

- FRC was unable to estimate the true cost of the proposed Port Activity Credit expansion. The changes create an incentive that could result in a much larger number than the one presented. The uncertainty of company actions means the actual cost could exceed the estimate below by tens of millions annually.
- FRC was unable to provide an estimate for New Facilities Job Credit due to a lack of available information, and the estimate for Competitive Projects of Regional Significance is more speculative than most revenue estimates. Both of these provisions involve a limited number of impacted projects; therefore, a variation of a single project related to either provision would significantly impact an estimate.

Table 1. Summary of State and Local Revenue Effects of HB 587 LC 43 2010S

($ *millions*)	**FY 2022**	**FY 2023**	**FY 2024**	**FY 2025**	**FY 2026**
Medical Device/Pharma Jobs					
High	($1.4)	($2.0)	($2.7)	($3.3)	($3.7)
Low	($0.7)	($1.0)	($1.3)	($1.7)	($1.9)
Port Activity Credit[1]	($2.9)	($1.3)	($0.8)	($0.4)	($0.3)
New Facilities Job Credit			** not estimated **		
CPRS Exemption[2]					
High	($7.8)	($15.5)			
Low	($1.3)	($2.5)			
Total State Effect[3]					
High	($12.1)	($18.8)	($3.5)	($3.7)	($4.0)
Low	($4.9)	($4.8)	($2.1)	($2.1)	($2.2)
Total Local Effect - CPRS Exemption					
High	($6.4)	($12.9)			
Low	($1.1)	($2.1)			

[1] Please see the note on page 5 regarding the incentives that could result in this credit amount being significantly larger.
[2] Please see page 6 for a discussion of the challenges predicting the cost of this exemption.
[3] Numbers may not add due to rounding.

Impact on State Expenditures
The Department of Revenue (DOR) would implement the provisions of the bill with existing resources.

Sincerely,

Greg S. Griffin
State Auditor

Kelly Farr

Kelly Farr, Director
Office of Planning and Budget

GSG/KF/mt

Analysis by the Fiscal Research Center

Sections 2-1 and 2-2
Additional Job Tax Credit for Medical Device and Pharmaceutical Manufacturers
The subject bill supplements and expands O.C.G.A. §48-7-40 and 40.1 relating to the Georgia Job Tax Credit (JTC) by creating an additional credit for medical device and pharmaceutical manufacturers. Companies in these industries, defined as NAICS code classifications of 3391 and 3254, earn an additional credit of $1,250 per employee that otherwise qualifies for a JTC. The proposed credit can be used to offset the employer's tax liability for employee withholding as well as employer income or insurance premium taxes. Any earned but unused credit can be carried forward for up to 10 years. No credit can be earned under this provision for jobs created that also earn a personal protective equipment manufacturer credit under §48-7-40.1A. The credit is effective for taxable years beginning on or after January 1, 2021, for jobs created on or after July 1, 2021, and prior to July 1, 2026.

O.C.G.A. §48-7-40 and 40.1 establish a framework for defining each Georgia county into four tiers based on the local unemployment rate, per capita income, and percentage of populations below poverty level for purposes of earning the state job tax credit (JTC), with differing requirements and credit amounts by tier. In tier 1 (the 71 least developed counties), firms are required to add a minimum of two additional employees year over year to qualify for JTCs. After meeting these requirements companies earn a JTC for each additional job created in that year. These credits continue for five years, assuming this new higher level of employment is maintained. In tier 2 counties, the threshold is 10 additional employees, tier 3 requires 15, and tier 4 requires 25. To be counted, employees' must be full time and be offered health insurance. This bill adds an additional $1,250 credit to the JTCs earned under these requirements for as long as the JTC is allowed for a qualifying job, for companies manufacturing medical devices and pharmaceuticals.

The estimated number of current JTCs being earned by firms in these industries will be the basis for the fiscal impact estimates for the subject legislation. Data obtained from the Georgia Department of Labor (DOL) indicate that 378 companies were operating in Georgia in 2019 in NAICS 3391 and 3254. These data were used to calculate year over year job growth by company for the years of 2015 through 2019 to estimate the number of JTCs each firm could have claimed, accounting for tier 1-4 thresholds by county.

JTC-eligible hiring cohort estimates range from a low of 357 new jobs in CY 2019 to a high of 1,152 in CY 2018, and average 698 per year over the 2016-19 period. The 2020 cohort is assumed to decline because of pandemic effects, but estimates of post-effective-date hiring cohorts assume the following:

- For 2021 the low case cohort size for the full year is assumed to equal that of 2019, 357 credit-eligible hires. For the high case, the number is assumed to rebound faster, equaling the average credit-eligible hires for 2016-19.
- Given the mid-year effective data of the bill, this 2021 cohort is reduced in both cases by 1/3, assuming that some hiring that may have otherwise occurred in the second quarter of 2021 will be deferred in response to passage of this bill to July 1 to take advantage of this additional credit.

- For 2022 and subsequent years, new cohort sizes are estimated based on projections from the Georgia State University Economic Forecasting Center (EFC) of overall job growth for the state (for 2022) and long-range job growth estimates from the BLS. The EFC projects overall jobs to rebound strongly in 2022, growing by 4.4 percent. BLS projects job growth of 2.4 percent annually in subsequent years.
- Low case cohort sizes equal the numbers implied by those growth rates of total employment. The high case allows for potentially faster growth of employment in the eligible industries and assume cohort sizes twice the low case levels.
- The estimates assume for simplicity that cohort sizes remain constant for the full five years they would be eligible for the credits, i.e. no attrition.
- Given that credits may be taken against withholding tax liabilities as well as income and insurance premium taxes, the estimates assume that all credits are utilized within the first calendar year after the creation of a credit-eligible job.

Table 2 summarizes the estimates for CYs 2021-26; fiscal year revenue effects for the high and low cases are included in Table 1.

Table 2. Qualified Jobs for NAICS 3391 and 3254

	CY 2021*	CY 2022	CY 2023	CY 2024	CY 2025	CY 2026
New Job Cohorts						
Low	238	448	255	261	268	274
High	466	896	510	522	536	548
Accumulated Credit Earning Jobs						
Low	238	686	941	1,202	1,470	1,506
High	466	1,362	1,872	2,394	2,930	3,012

* new jobs created beginning July 1

Section 2-3
Increase the Income Tax Offset Allowable for the Port Activity Credit
The subject bill proposes to increase the maximum amount of port activity tax credits under O.C.G.A. §48-7-40.15 that can be utilized in one year. Under current law, business enterprises claiming the credit may not offset more than 50 percent of their state income tax liability in any year, carrying forward unutilized balances. This bill would allow taxpayers to offset up to 100 percent of their state income tax liability in a given year and if any unutilized balance remains, use it to offset payroll withholding tax liabilities. These changes would be effective for credits earned in tax years beginning on or after January 1, 2021 and ending on or before December 31, 2026.

The estimated state revenue impact of this tax credit for FY 2022-26 relies upon data provided by the Georgia Department of Revenue (DOR) on the port activity credits generated and utilized from 2015 through 2019. The data and assumptions estimating the revenue effects are as follows:

- DOR data indicate that port activity credits earned averaged $5.0 million per year between 2015 and 2019 and $2.1 million, on average, were utilized annually. The estimates assume that under current law, half of the credits generated are utilized in the year earned, one quarter in the second year, one tenth each in the third and fourth years, and the reminder in the fifth year.

- The estimates assume that under HB 587, taxpayer's earning port activity credits will fully utilize credits in the year earned. Firms may be limited in their tax liability, but the legislation allows available credits in excess of state income tax liability in a given year to be claimed against payroll withholding taxes without limitation.
- According to data from the Bureau of Economic Analysis (BEA), Georgia's Gross State Product (GSP) grew on an annual basis by an average of 5 percent per year from 2012 through 2019. This growth rate is assumed for port activity credits generated from CY 2020 through CY 2026.

Table 3 details the estimated amount of port activity credits generated and their utilization under current and proposed law for CY's 2022-26 based on these data and assumptions. Estimated revenues effects by state fiscal year, assuming credits impact tax collections evenly over the year, are presented in Table 1.

Table 3. Port Activity Credits Generated and Utilized in CY 2021-2026

($ *millions*)	CY 2021	CY 2022	CY 2023	CY 2024	CY 2025	CY 2026
Credits Earned	$5.5	$5.7	$6.0	$6.3	$6.6	$7.0
Utilized Current Law	$2.7	$4.2	$5.0	$5.8	$6.4	$6.7
Utilized Proposed Law	$5.5	$5.7	$6.0	$6.3	$6.6	$7.0
Revenue Effect	($2.7)	($1.5)	($1.0)	($0.5)	($0.3)	($0.3)

Note: *This analysis notwithstanding, there is reason to suspect that this change to the port activity credit creates or expands an attractive loophole with the potential of costing the state much more in lost revenue than shown above. Under current law, the investment credit portion of the port activity credit allows taxpayers who would otherwise qualify for the manufacturers' investment tax credit (ITC) under O.C.G.A. §48-7-40.2 thru 40.4, at credit rates of 1 percent to 5 percent of qualified investment depending on the tier of the county, to take this credit at a rate of 5 percent instead. Despite this incentive under current law, utilization of the port activity investment credit has been limited in recent years, perhaps because of the limits on utilization to 50 percent of income tax liability.*

The proposed expansion of potential utilization of the credit to allow it to be used against 100 percent of a company's income tax liability and then against withholding taxes has the potential to increase the amount of new credits generated (because facilities in Tier 2-4 counties could earn larger credits at 5 percent instead of 1 or 3 percent) as well as to accelerate utilization tremendously compared to that under the manufacturers' ITC. A firm with facilities located in Tier 2-4 counties could increase shipments through the ports by an economically negligible amount and, as a result, qualify for a credit that is up to five times larger and that can now be applied against withholding, making it usable immediately rather than over a long period of time.

The potential impact of this incentive is difficult to estimate because available data on manufacturers' ITCs generated and utilized is not broken down by county tier. However, it is conceivable, given the overall magnitudes of manufacturers' ITCs generated in recent years that the added cost of this proposed change could reach tens of millions of dollars per year.

Section 2-4
New Facilities Job Credit
The subject bill proposes to amend O.C.G.A. §48-7-40.24, the new facilities job credit, to eliminate, for a period of time, the 4,500 jobs limit on the number of new full-time jobs for which credits may be claimed for any one qualified project.

Current law terms of the New Facilities Job Credit are, in summary, as follows:

- Requirements:
  - 1,800 new jobs created within 6 years, subject to extension to 8 years if $600 million in qualified investment is made within 6 years and to 10 years if $800 million within 8 years;
  - Either $150 million or more of annual payroll or $450 million of qualified investment; and
  - Qualifying new jobs are full-time (35+ hours/week) and pay at or above the average wage of the county with the lowest average wage in the state.
- Credit amount is $5,250 per job for five years, subject to recapture based on failure to meet job and payroll maintenance requirements. Only jobs created by the end of the 7th year qualify for a credit, unless the $600 million within 6 years or $800 million within 8 years investment thresholds are met, in which cases new jobs created within 8 year or 10 years, respectively, can earn a credit. No more than 4,500 such new jobs can earn a credit.

Under the proposed law, effective for credits earned in tax years beginning on or after January 1, 2021, and ending on or before December 31, 2026, the 4,500 jobs limit would not apply.

Given the large scale of projects eligible for this credit, projecting fiscal costs tied to specific state fiscal years is not possible without information on investment and job creation plans and timelines for specific projects currently planned or under consideration. In addition, data on past utilization of this credit are not available from the Department of Revenue as amounts claimed are reported in combination with other job credits to preserve confidentiality of taxpayer information. Thus, it is not possible to estimate the likely fiscal impact of this provision at this time.

Section 2-5
Competitive Projects of Regional Significance
For a project to qualify for this exemption, the commissioner of the Georgia Department of Economic Development (GDEcD) must have determined that a location or expansion of a business enterprise's operations would have a significant regional impact. Once a project has been granted this exemption, any otherwise taxable purchases made during the time of construction are exempt, including those occurring after any applicable sunset date.

The extension of the sunset date from June 30, 2021, to June 30, 2023 will reduce state sales tax collections from construction expenses for qualified projects during FYs 2022-23. Construction expenditures for materials are taxable expenditures (taxed upon purchase by contractors or by the project owner, if purchased directly). The revenue effects of CPRS projects approved during the extended sunset period under the proposed bill are based on the reported facts and assumptions below and resulting otherwise-taxable investment projections are provided in Table 4.

- The estimates rely upon GDEcD-reported aggregate planned investment since the previous renewal of the exemption in 2016, a total of $2.645 billion announced investment over three projects announced during 2016-18, for an average of about $882 million per year over the three years. Since that time, no new projects have been granted the exemption.
- For the high estimate, average annual investment in FY 2022-23 is assumed to be 10 percent higher than the 2016-18 average. For the low, average annual investment is assumed to equal the 2016-20 average of $529 million per year.
- Based on data obtained from corporate financial statements, the Bureau of Economic Analysis, and the U.S. Census, it is estimated that between 12 percent and 40 percent of the project investments will be on otherwise-taxable expenditures. The low share of 12 percent, which is used in the low case estimates, is for manufacturing projects where an estimated 30 percent or less of total plant investment is for buildings and improvements, and 40 percent of that amount is assumed to be for otherwise taxable purchases. For the high case, the 32 percent otherwise-taxable share for non-manufacturing projects is used.
- A study published in the journal *Economic Letters* indicates that large commercial projects take, on average, about one and a half years to complete, accounting for construction time only. Of course, large construction projects also require significant planning and site preparation lead times. The estimate assumes that half of a project's exempt expenditures will occur in the same year that they qualify for the exemption with the other half occurring in the following year.
- Local effects assume a tax rate of 3.32 percent, the Tax Foundation's reported January 2021 weighted average local rate for Georgia.

It is important to note that, because of the large size of some projects and the small numbers of projects approved for this exemption in the past, the general lack of useful data about the projects or the otherwise-taxable spending involved, and the flexibility in the law as to what projects might qualify in the future, these estimates are highly speculative. Though we believe the range estimates bound what is most likely to be experienced, the possibility that state and local revenue costs could fall significantly above or below these estimates cannot be ruled out.

Table 4. Project Expenses and Revenue Effects of Section 2-5

($ *millions*)	**FY 2022**	**FY 2023**
Projects Authorized		
High	$970	$970
Low	$529	$529
Project Expenditures		
High	$485	$970
Low	$265	$529
Otherwise Taxable Amt		
High	$194	$388
Low	$32	$63