DEPARTMENT OF AUDITS AND ACCOUNTS

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December 22, 2020

Honorable Jesse Petrea
State Representative
408-A Coverdell Legislative Office Building
Atlanta, Georgia 30334

SUBJECT: Fiscal Note
House Bill (LC 43 1732)

Dear Representative Petrea:

The bill would to exempt from income taxation all retired pay and survivor benefits received by Georgia taxpayers from the United States' uniformed services. This exemption would be effective beginning January 1, 2022 and would expire December 31, 2032.

The uniformed services covered by the bill include the Department of Defense (Army, Navy, Marines, and Air Force), Department of Homeland Security (Coast Guard), Department of Health and Human Services (Public Health Service Commissioned Corps), and Department of Commerce (NOAA Commissioned Officer Corps), including their reserve components where relevant. Survivor benefits derived from these services' retirement benefits would also be exempt. The eighth uniformed service, the Space Force of the Department of Defense, is not covered by the bill. The analysis assumes that while payments under the Department of Defense Survivor Benefit Plan or other DoD benefit payments to military survivors (collectively, SBP) would qualify for this exemption, survivor and dependent benefits paid by the Department of Veterans Affairs are not included in this analysis as these payments are not currently subject to income tax.

Impact on State Revenue
Georgia State University's Fiscal Research Center (FRC) estimated that the bill would decrease state revenue between $59.6 million and $105.4 million in fiscal year 2023, the first year of the bill's full effect (Table 1). The revenue decrease would grow in subsequent years. The attached appendix provides details of the analysis.

Table 1: Estimated Revenue Effects of LC 43 1732

($ *millions*)	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026
High	($43.2)	($105.4)	($109.9)	($114.8)	($120.0)
Low	($24.8)	($59.6)	($60.2)	($60.9)	($61.7)

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, Director
Office of Planning and Budget

GSG/KF/mt

Analysis by the Fiscal Research Center

As the subject bill affects four departments' uniformed services' retirees and survivors, this appendix is divided by governing department for ease of reading. To estimate the revenue impact of exempting uniformed services retired pay and survivor benefits from income taxation, it is first necessary to account for the fact that taxpayers age 62 to 64 are already exempt from Georgia income taxes on up to $35,000 of retirement income and those over age 65 are exempt on up to $65,000 of retirement income. This age breakdown will be addressed in each department's section, and its tax implications in the final section.

Department of Defense

According to the Department of Defense (DoD) Statistical Report on the Military Retirement System for FY 2019 (the latest available), 100,389 persons retired from the U.S. military resided in Georgia as of September 2019, of whom 91,600 were receiving military retired pay. Note that the Space Force did not exist as a separate service under Department of Defense as of the cut-off date of this Statistical Report, and accordingly there are no reported retirees or survivors thereof; as personnel are transferred to the Space Force from other DoD services, retirement income and survivor benefits therefrom would not be exempted by this law and so the total tax revenue loss could be reduced compared to the estimates presented here.

The 2019 Statistical Report did not provide state-level breakdowns by age, but the prior year's report (2018) revealed that, of those receiving retired pay, approximately 44.7 percent were age 65 or over. Further age breakdowns were available on military retirees nationally in the 2019 report; on the basis of the national data, approximately 18.8 percent of those under age 65 are assumed to be 62 to 64 years of age. Thus, it is estimated that approximately 44.9 percent of military retirees in Georgia receiving retired pay are under age 62. Georgia SBP beneficiaries, who numbered 13,421 as of September 2018, are much more likely to be over 65, 11,117 or 82.8 percent of recipients at that time. Based on the finer age groupings in national figures, it is assumed that 24 percent of the under-65 benefit recipients are 62-64, bringing the total share of recipients eligible for some amount of retirement income exclusion to about 87 percent.

Growth rates of Georgia recipients of military retired pay have differed by age group in recent years, with the over-65 group growing by about 3.5 percent annually, on average, since 2011 and the under-65 group declining by 1 percent annually over the same period. In 2018, the number under age 65 actually fell from 2016 by 0.9 percent annually while the number over 65 grew by 2.6 percent. For purposes of projecting military retired pay recipients, it is assumed that the number above age 65 will grow by between 2 percent and 4 percent annually while those below age 65 will grow by -1 percent to 1.5 percent annually.

Overall growth in SBP beneficiaries, which had been running 0.4 percent annually from 2011-2016, reversed, declining by 0.2 percent annually the last two years. Growth in the 65+ age group also reversed, averaging a 0.6 percent decrease annually since 2016 (compared to a 1.0 percent annual increase for 2011-16) while the under-65 age group also reversed, gaining 1.9 percent annually since 2016 (compared to -2.2 percent annually for 2011-16). To project survivor benefit recipients, growth rates of -1 to 1.5 percent are assumed for the 65+ age group and -2 to 2 percent are assumed for the under-65 group.

Projected numbers of retired pay and survivor benefit recipients in Georgia for tax years 2022 through 2026 are provided in Table 2.

Table 2: Projected Total Military Retired Pay and Survivor Benefits Recipients, by Age Group

		TY 2022	TY 2023	TY 2024	TY 2025	TY 2026
Under 62	High	45,146	45,833	46,530	47,238	47,956
	Low	41,816	41,382	40,953	40,526	40,105
Age 62-64	High	10,233	10,389	10,548	10,709	10,873
	Low	9,472	9,372	9,273	9,177	9,080
65 & Over	High	57,693	59,711	61,805	63,978	66,234
	Low	54,249	55,011	55,791	56,590	57,409
Total	High	113,072	115,933	118,883	121,925	125,063
	Low	105,537	105,765	106,017	106,293	106,594

Average military retired pay differs by age as well, with the average for Georgia recipients over age 65 at $27,668 annualized as of September 2018 and for those under age 65 at $26,282. Average SBP payments as of September 2018 were $12,178 annualized for recipients over age 65 and $9,828 for those under age 65. Payments are adjusted annually based on the prior year's consumer price index (CPI) inflation rate.

The official COLA rates for 2019, 2020 and 2021 were set at 2.8 percent, 1.6 percent, and 1.3 percent respectively, based on CPI inflation for the preceding years. COLA rates for 2022 and beyond are assumed to be equal to the prior-year projected CPI-U rates as projected by the Congressional Budget Office in its July 2022 10-Year Economic Projections. The resulting projected average pay figures, together with the projected retiree and survivor figures from Table 2, result in high and low total retiree pay and survivor benefit projections, by age group, as shown in Table 3.

Table 3: Projected Total Military Retired Pay and Survivor Benefits, by Age Group

($ *millions*)		TY 2022	TY 2023	TY 2024	TY 2025	TY 2026
Under 62	High	$1,237.6	$1,279.5	$1,326.8	$1,377.1	$1,429.5
	Low	$1,147.6	$1,157.0	$1,169.9	$1,184.1	$1,198.6
Age 62-64	High	$277.9	$287.3	$298.0	$309.3	$321.1
	Low	$257.6	$259.7	$262.6	$265.8	$269.1
65 & Over	High	$1,516.8	$1,602.8	$1,698.9	$1,802.4	$1,912.7
	Low	$1,428.6	$1,479.9	$1,537.7	$1,599.3	$1,663.8
Totals	High	$3,032.3	$3,169.7	$3,323.6	$3,488.8	$3,663.2
	Low	$2,833.9	$2,896.6	$2,970.2	$3,049.2	$3,131.5

Department of Homeland Security
The Department of Homeland Security houses one uniformed service, the Coast Guard and its Reserves. Its substantially smaller size relative the uniformed services of the DoD, data is

proportionally scarcer. This analysis relies on two primary data sources, as follows. Information on Coast Guard retirees and survivors was provided in past issues of the Statistical Report on the Military Retirement System (up through FY 2016's report) in parallel to that of DoD services, allowing similar calculations to be made regarding the share of retirees and survivors in Georgia and over the age of 65. However, direct benefit information was not available in this document. Instead, total benefit amounts were located in the Appendix to each Presidential budget. While more recent years report all Coast Guard Retiree benefits as a lump sum, older budgets (federal FY 2010 through FY 2014, reporting information on actual expenditures in 2008 through 2012) do provide information on the breakdown of retirement versus survivor benefits, allowing estimation of the per-person benefit amount at this earlier point in time and a rough basis for estimating likely future shares. This information also revealed that the per-person survivor benefit varied considerably in the sample available, but the per-person retiree benefit remained relatively stable, making it more suitable for projection and guiding subsequent techniques.

The most reliable information was judged to be that of the total budgeted amount per year, available through federal FY 2021. This figure was projected forward using the average growth of most recent seven years of data to find likely total budgets for the FY 2022-26 period. The next key datum was the likely number of recipients (retirees and survivors) in that period, whose growth rate could likewise be determined by averaging that of the most recent seven years of data available and projecting accordingly. Finally, Cost of Living Adjustment (COLA) information was integrated into the model. Unlike the Department of Defense services, the Coast Guard does not use a CPI-based COLA but instead employs a set of COLAs depending on the particulars of service and retirement. Information about several years' COLA patterns was integrated to form high and low COLA estimates, where the high rate assumes all retirees are eligible for the highest COLA rate and low rate assumes half of retirees receive that COLA amount and half are eligible for a lower amount applicable to the already-retired who selected the career-bonus option at retirement.

Based on the above, high and low average per-retiree benefits were projected forward according to COLA estimates, then multiplied by the estimated retiree population. This figure was subtracted from the projected total benefit, leaving a total survivor benefit figure, which was divided by the projected survivor population to establish high and low per-survivor benefit estimates.

Next, the nation-level retiree and survivor totals were shared down to those in Georgia, and the Georgia populations divided into 65-and-over and under-65 segments based on the seven-year average of shares for those categories found in the Statistical Report. Finally, the under-65 populations were split into their 62-64 and under-62 components based on the national age breakdowns for all DoD retirees and survivors, as the Coast Guard populations were judged to be substantially similar in circumstances to make the approximation appropriate. This final adjustment yielded Table 4 below. Note that scarcity of data precluded division into meaningful high and low population estimates, with high and low groupings deriving from differing COLA assumptions described above. Estimated Georgia benefit-population totals were multiplied by the high and low average per-person benefit values estimated as described above. The results are in Table 5.

Table 4: Projected Coast Guard Retired Pay & Survivor Benefit Recipients, by Age Group

	TY 2022	TY 2023	TY 2024	TY 2025	TY 2026
Under 62	521	528	536	545	552
Age 62-64	117	119	120	122	124
65 & Over	599	609	620	629	641
Total	1,237	1,256	1,276	1,296	1,317

Table 5: Projected Total Coast Guard Retired Pay & Survivor Benefits, by Age Group

($ *millions*)		TY 2022	TY 2023	TY 2024	TY 2025	TY 2026
Under 62	High	$17.7	$18.2	$18.7	$19.3	$19.8
	Low	$16.8	$17.2	$17.7	$18.1	$18.5
Age 62-64	High	$4.0	$4.1	$4.2	$4.3	$4.5
	Low	$3.8	$3.9	$3.9	$4.0	$4.2
65 & Over	High	$24.3	$25.1	$26.1	$26.9	$27.9
	Low	$17.6	$18.1	$18.7	$19.2	$19.8
Total	High	$45.9	$47.4	$49.0	$50.5	$52.2
	Low	$38.2	$39.2	$40.3	$41.4	$42.5

Department of Health and Human Services

The uniformed service of the Department of Health and Human Services is the Public Health Service Commissioned Corps, or PHS Corps. The PHS Corps is another magnitude smaller than the Coast Guard, and data likewise quite scarce. The primary sources used were the appendix section to each Presidential budget, which provided nation-level totals for active, retired, and survivor populations of the corps, as well as the latter two groups' respective total benefits. These figures were elaborated upon in the congressional justification documentation provided as part of the budget process, which included five-year projections of the budget for these categories (through 2026). Using these data, average per-person benefit information for both retirees and survivors was calculated by dividing the provided total in each category by the relevant projected population figure, based on a seven-year average of the category's growth.

With the per-person benefit estimated for the period, the next task was to determine the Georgia and by-age breakdowns of the population totals, but such data were lacking. The totals were thus shared down assuming a similar Georgia share as in DoD retirees and survivors.[1] Likewise, the DoD national survivor age breakdown was used to estimate the number of Georgia PHS Corps survivors in each age category. Finally, a slightly different source was used to estimate likely Georgia PHS Corps retiree ages. The PHS Corps is composed exclusively of officers, O-grade (though W-grade warrant officers are permitted in the corps by law, there are none serving at this time), whose career trajectories may meaningfully differ from the numerically larger enlisted population of the DoD all-personnel retiree age estimates. Instead, the national age breakdown for retired O-grade DoD officers was used as a proxy for the likely age breakdown of retired PHS Corps officers. The resulting estimates are presented in Table 6. As with the Coast Guard above,

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[1] Georgia has a higher share of DoD retirees (5%) than its overall share of the U.S. population (3%). Applying the higher percentage to the uniformed services of DHHS is deemed reasonable given that the Centers for Disease Control and Prevention is in Georgia.

due to data limitations there is only one set of PHS Corps age breakdowns. As the benefit amounts derive from the stronger set of still-limited data, Table 7's total benefits also lack a high and low component.

Table 6: Projected PHS Corps Retired Pay & Survivor Benefit Recipients, by Age Group

	TY 2022	TY 2023	TY 2024	TY 2025	TY 2026
Under 62	86	86	87	87	88
Age 62-64	25	25	25	24	25
65 & Over	229	233	236	239	243
Total	340	344	348	351	356

Table 7: Projected Total PHS Corps Retired Pay and Survivor Benefits, by Age Group

($ *millions*)	TY 2022	TY 2023	TY 2024	TY 2025	TY 2026
Under 62	$7.0	$7.1	$7.4	$7.6	$7.9
Age 62-64	$2.1	$2.1	$2.2	$2.1	$2.2
65 & Over	$17.0	$17.7	$18.4	$19.1	$19.9
Total	$26.0	$27.0	$27.9	$28.9	$30.0

Department of Commerce

Finally, the smallest uniformed service is the Department of Commerce's National Oceanic and Atmospheric Administration Commissioned Officer Corps, often referred to as the NOAA Corps, consisting of a total of 324 officers nationwide. Its data was minimal, but also primarily found in the NOAA Blue Book publication (some years of which provide a total active personnel count), the appendix section to each Presidential budget, and the congressional justification for those budget requests.

Unlike the other uniformed services in this note, all recent budget appendices present NOAA Corps retirement benefits as a single sum, without indication of the amount applied to retiree versus survivor benefits, nor the size of either population. Accordingly, NOAA Corps estimates relied heavily on the analysis of the PHS Corps, as another small, officer-only, unarmed uniform service composed of scientific subject matter experts. Additionally, by consulting the retirement announcement rolls in the "Long Blue Line" retiree newsletter (serving retired Coast Guard, PHS Corps, and NOAA Corps members), the relative rate of retirements per year versus active personnel could be established for both the PHS and NOAA Corps, and were found to be substantially similar, further supporting the use of PHS as a comparison population.

Based on the figure of 324 active-duty personnel per year, the national retired and survivor populations were found by multiplying the fractions of the PHS population in those categories by the NOAA active figure. These national figures were then shared down to Georgia and divided into age category in the same way as the PHS populations were, by reference to the national DoD survivor and officer (O-grade) age breakdowns. The results are presented in Table 8 below.

Table 8: Projected NOAA Corps Retired Pay & Survivor Benefit Recipients, by Age Group

	TY 2022	TY 2023	TY 2024	TY 2025	TY 2026
Under 62	4	4	4	4	4
Age 62-64	1	1	1	1	1
65 & Over	11	11	11	11	11
Total	16	16	16	16	16

The next task was to estimate per-person benefit amounts. Without having any direct NOAA information, the PHS rates were employed again. The per-person benefit for survivors was divided by the benefit for retirees to find approximate the share survivor versus retiree benefits represented in the reported total and their 2022-2026 projections (which again used the seven-year average growth). These estimated survivor and retiree benefit totals were divided by the estimated national populations for each, yielding per-person amounts that could be multiplied by the age-separated Georgia populations estimated in Table 8, the results of which are presented in Table 9. Again, due to data limitations, only a midpoint estimate is offered.

Table 9: Projected Total NOAA Corps Retired Pay & Survivor Benefits, by Age Group

($ *millions*)	TY 2022	TY 2023	TY 2024	TY 2025	TY 2026
Under 62	$0.4	$0.4	$0.4	$0.4	$0.4
Age 62-64	$0.1	$0.1	$0.1	$0.1	$0.1
65 & Over	$0.9	$0.9	$0.9	$0.9	$0.9
Total	$1.4	$1.4	$1.4	$1.4	$1.4

Tax Implications

With the retiree and survivor populations for all seven of the active uniformed services calculated and their benefits estimated, as shown in Tables 3, 5, 7, and 9, the total estimated income amount subject to this bill is summarized in Table 10.

Table 10: Total Uniformed Services Retired Pay & Survivor Benefits, by Age Group

($ *millions*)		TY 2022	TY 2023	TY 2024	TY 2025	TY 2026
Under 62	High	$1,263	$1,305	$1,353	$1,404	$1,458
	Low	$1,172	$1,182	$1,195	$1,210	$1,225
Age 62-64	High	$284	$294	$304	$316	$328
	Low	$264	$266	$269	$272	$276
65 & Over	High	$1,559	$1,647	$1,744	$1,849	$1,961
	Low	$1,464	$1,517	$1,576	$1,639	$1,704
Total	High	$3,106	$3,245	$3,402	$3,569	$3,747
	Low	$2,899	$2,964	$3,040	$3,121	$3,205

The retirement income exclusion available to the 62 and over age groups requires different assumptions across the groups as to effective tax rates. For all Georgia full-year resident taxpayers (excluding those with negative Federal AGI), the weighted average effective tax rate (net tax divided by taxable income) was 5.07 percent in tax year 2018 after accounting for reduction in the top tax rate since that time. Thus, for military retirees under age 62, an effective tax rate of 5.07

percent is assumed going forward. For those eligible for the retirement exclusion, much of their military retired pay (if not all) is already excluded, so this measure of effective tax rates would be misleading. Instead, net tax is divided by federal adjusted gross income, which would include military retired pay. On this basis, the effective tax rate for all Georgia retirees in 2018 was 2.15 percent. Those retirees with AGI below the exclusion limits will still have tax liabilities to the extent they have earned income in excess of $4,000, but no liability associated with their retirement income. Those with higher retirement or other income may be taxable on some or all of their military retired pay or survivor benefits. It is conceivable, then, that no military retired pay or survivor benefits received by age 62 or older taxpayers is currently taxable, so high and low effective tax rates of 2.15 percent and zero are assumed for both the 62-64 age group and those age 65 or older. From these assumptions and the retired pay and survivor benefit figures in Table 10, projected tax liabilities under current law are as shown in Table 11.

Table 11: Projected Taxes on Uniformed Service Retired & Survivor Pay, by Age Group

($ *millions*)		TY 2022	TY 2023	TY 2024	TY 2025	TY 2026
Under 62	High	$64.0	$66.2	$68.6	$71.2	$73.9
	Low	$59.4	$59.9	$60.6	$61.4	$62.1
Age 62-64	High	$6.1	$6.3	$6.5	$6.8	$7.0
	Low	$0.0	$0.0	$0.0	$0.0	$0.0
65 & Over	High	$33.5	$35.4	$37.5	$39.8	$42.2
	Low	$0.0	$0.0	$0.0	$0.0	$0.0
Total	High	$103.6	$107.9	$112.7	$117.8	$123.1
	Low	$59.4	$59.9	$60.6	$61.4	$62.1

These figures are adjusted to fiscal year basis assuming that tax collections are substantially all through withholding and thus are spread evenly over the year, with the first five calendar months' withholding payments collected in the fiscal year ending in June of that calendar year and the balance collected in the following fiscal year. For example, 7/12 of the TY 2021 and 5/12 of the TY 2022 tax liabilities would be collected in FY 2022, with future years' liabilities similarly divided. The results are shown in Table 1 of the fiscal note.