DOAA
Georgia Department
of Audits & Accounts

Greg S. Griffin
State Auditor

January 9, 2023

Honorable Shaw Blackmon
Chairman, House Ways and Means
133 State Capitol
Atlanta, GA 30334

SUBJECT: Fiscal Note
House Bill (LC 43 2501ER)

Dear Chairman Blackmon:

The bill would repeal O.C.G.A. Chapter 7 of Title 48, relating to personal and corporate income taxes, and replace the current state sales and use tax with a broader 6.70% sales and use tax on final consumption. The bill also provides for a monthly rebate in the amount equal to the product of the tax rate and the "monthly poverty level" for a qualified family's size. The bill would be effective on January 1, 2024.

The bill provides exemptions or credits on property or services purchased as an "intermediate article" (e.g., education, training), for a business purpose in a trade or business, for investment purposes, or for sales or use outside the state. Government purchases and purchases by public or private schools, colleges, and universities would be exempt, as would purchases by qualified non-profit organizations. Georgia purchasers of goods or services from outside the state must remit tax due, if not collected by the seller. Finally, "taxable employers", as defined, must remit tax on wages paid for services rendered.

Impact on State Revenue

Georgia State University's Fiscal Research Center (FRC) estimated that the bill would decrease state revenue (Table 1). In the first full year of the bill's impact (2025), the bill is estimated to result in state revenue loss of approximately $3.2 billion. The loss would grow slightly in succeeding years. The appendix provides details of the analysis.

Table 1. Estimated State Revenue Effects of the Georgia FairTax Act

($ *millions*)	**FY 2024**	**FY 2025**	**FY 2026**	**FY 2027**	**FY 2028**
Total State Taxes Repealed	($12,421)	($26,582)	($27,638)	($28,818)	($29,950)
State FairTax:					
Revenues	$15,220	$31,764	$33,100	$34,475	$35,918
Less: Rebates Paid	(4,106)	(8,358)	(8,641)	(8,919)	(9,205)
Net FairTax Proceeds	$11,114	$23,407	$24,459	$25,556	$26,713
Net Change in State General Funds	**($1,306)**	**($3,175)**	**($3,179)**	**($3,262)**	**($3,237)**

* Includes state corporate net worth tax.

Impact on State Expenditures

The Department of Revenue (DOR) would incur additional annual costs of approximately $27.4 million. A significant amount of the estimated annual cost—$17.2 million—is for smart card technology to issue tax rebate credits. Estimated costs for smart cards is based on costs incurred by the Georgia Department of Human Services for their EBT card. DOR would also have one-time costs of approximately $450,000, without considering the redirection of staff to make IT system modifications. Details of the estimate are included in Table 2 and the rationale for the changes are discussed below.

Table 2. Estimated Expenditure Effects of LC 43 2501ER

	One-Time Costs	Annual Costs*
Tax Policy		
Staff Training (Manager, attorney or CPA, support staff)	-	$387,267
Computer and Equipment	$14,250	-
Compliance		
Travel	$100,000	-
Postage	-	$3,200,000
Taxpayer Services		
Technology; Contact Center Support	$334,800	-
Staff (tax examiner, support staff, customer service, helpdesk analysts), postage, and Contact Center Support	-	$6,406,435
Smart Card Technology	-	$17,172,000
IT Systems Governance		
Staff (analysts, testers, developers, project manager)	See Note	-
Training and Development Outreach		
Equipment (Computer, phone, accessories)	$4,050	-
Staff (training and development specialists)	-	$198,261
Total	**$453,100**	**$27,363,963**

Note: DOR IT staff would be redirected from other activities to make system changes to implement the bill's provisions. The work would take approximately 32 weeks of staff time, equivalent to $1,063,680.

- *Tax Policy* – A significant amount of work would be necessary to determine the entire universe of services covered by the bill. In addition, implementation of a new tax type would require drafting new regulations, forms, and other guidance, training of DOR staff, and outreach to the external entities impacted by the law.

- *Compliance* – The Compliance Division would be able to shift collections staff to Fair Tax collections, but those staff will initially need to conduct field visits to ensure compliance with registration requirements, particularly educating taxpayers on what services will be taxable. In addition, the "final notice" provisions of the bill will increase DOR's postage expenses.

- *Taxpayer Services* – Staff will be needed to support the larger workload resulting from an increase in the number of sales tax vendors and the registration of more than 5 million families annually.

- *Training and Development Outreach* – Limited staff would be needed for continuous outreach activities (e.g., webinars, training material development, in-person training) to explain taxpayers' reporting and tax compliance responsibilities.

It should be noted that not all income tax personnel would be able to immediately transition due to subsequent audits of filed returns, filing of amended returns, IRS adjustments in later years that affect filed returns, audit protests, etc.

Respectfully,

Kelly Farr

Greg S. Griffin
State Auditor

Kelly Farr, Director
Office of Planning and Budget

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Analysis by the Fiscal Research Center

The Georgia FairTax Act, if enacted, would replace Georgia's corporate and personal income taxes, corporate net worth tax, and state sales and use tax with a new sales and use tax the base of which would include essentially only *final* consumption of goods and services in Georgia by households, and would exclude from taxation all intermediate goods and services purchases of for-profit businesses, purchases for investment purposes, eligible education and training purchases, government purchases, and purchases for consumption or use outside the state. As written, the act is to be effective January 1, 2023. However, it is assumed for purposes of this note that the effective date would be amended before enactment to January 1, 2024.

Repeals of Existing State Income and Sales Taxes
Section 3 of the subject bill would repeal O.C.G.A. §48-7 in its entirety, thus eliminating all state income taxes, corporate and personal. Sections 4 and 5 of the bill would amend, respectively, O.C.G.A. §48-7-30 and §48-7-32 by reducing the state sales and use tax rate from 4 percent to 0 (zero) percent, while leaving all other provisions of Chapter 7 of Title 48 intact. Section 6 of the bill clarifies that, beginning on January 1, 2023, the state sales and use tax shall not be imposed or collected, but that all other (i.e., local) sales and use taxes imposed by Chapter 7 shall continue to be imposed and collected. Section 7 of the bill would repeal Article 4 of O.C.G.A. §48-13, thus eliminating the state corporate net worth tax (CNWT).

Table 3 shows projections of the affected taxes through FY 2028, based on the most recent projections available from the Office of Planning and Budget (OPB), as of October 2022. Note that the corporate income tax (CIT) projections from OPB include amounts attributable to the CNWT and the financial institutions business occupations tax (FIBOT), which are generally included in corporate income tax revenues for state reporting and forecasting purposes. The CNWT would be fully repealed under HB 1459, but the FIBOT is not affected and will remain in place. Thus, FIBOT revenues are netted out of OPB forecasted CIT revenues based on linear forecast from FY 2016-22 actual FIBOT collections out to FY 2028. Finally, we assume that the OPB projections reflect all tax changes enacted in the 2022 legislative session to income or sales taxes.

Table 3. Forecasted State Revenues from Income and Sales Taxes

($ *millions*)	FY 2024**	FY 2025	FY 2026	FY 2027	FY 2028
State Taxes to be Repealed:					
Personal Income Tax	$15,207	$15,551	$16,206	$16,870	$17,569
Corporate Income Tax	$1,888	$2,026	$2,067	$2,208	$2,252
State Sales and Use Tax	$8,658	$9,005	$9,365	$9,740	$10,129
State Taxes to be Repealed	$25,753	$26,582	$27,638	$28,818	$29,950

* Includes state corporate net worth tax. ** FY 2024 not adjusted for part-year effect of repeal.

Given the presumed effective date of the bill, revenues would first be affected in FY 2024. In estimating the revenue loss from these repeals, it is assumed that 50 percent of the forecasted revenues for corporate income and sales taxes for FY 2024 would be eliminated, along with 47 percent of personal income tax revenues, which are collected less evenly over the year.

Regarding income taxes for taxpayers with tax years not corresponding to the calendar year, income taxes for the tax year in which the effective date of the bill falls will be due only on income attributable to the period prior to the effective date. Finally, all tax loss and tax credit carryforwards from periods before the effective date will be terminated as of the effective date.

FairTax Base and Rate

A stated purpose of the proposed Georgia FairTax is "to tax all consumption of goods and services in Georgia once, without exception, but only once" (lines 65-66 of the bill), subject to only limited exceptions. Specifically, the proposed bill would apply as follows:

- New goods and services, including but not limited to financial intermediation services, that are produced and consumed in the state **are** taxed.
- New goods and services "imported" from out of state **are** taxed.
- Sales of new homes (net of land value) **are** taxed.
- Services in the form of labor purchased by households employing domestic servants **are** taxed, with the tax payable by such taxable employer on the total compensation paid.
- New goods and services that are produced in the state but are "exported" and sold outside of the state **are not** taxed.
- Used goods and intangible property **are not** taxed.
- Education and training expenses (tuition for primary, secondary, or postsecondary level education, and job-related training courses) **are not** taxed.
- Goods and services purchased for resale, or as inputs to, or in the production of, new goods and services **are not** taxed.
- Goods and services purchased by the federal government, by state and local governments including school districts, or by qualified non-profit organizations **are not** taxed.
- Goods and services purchased for educational purposes by the University System of Georgia or any of its educational units as well as by eligible private colleges, universities, and elementary and secondary schools **are not** taxed.

The tax rate applicable to all taxable purchases under the Act would be 6.70 percent.

Forecasted FairTax Revenues

Revenue estimates are based on applying the tax rate under the bill to estimates of the tax base derived from Bureau of Economic Analysis (BEA) data on Georgia (and national) economic activity. Essentially, the broad base includes all personal consumption expenditures (PCE) except for education, used vehicles, and imputed rent on owner-occupied housing, plus new fixed investment in owner-occupied homes. Unlike in previous versions of this legislation, the base does not include any government expenditures.

BEA estimates of total PCE also include amounts for the net consumption of nonprofit institutions serving households – that is, the gross output in services to households by nonprofits less any receipts of nonprofits in payment for those services. Purchases by households of services from nonprofits would be taxable, but the net difference, representing services provided without compensation, would not be taxable, so this net amount is deducted from total PCE in estimating the taxable portion.

PCE data at the state level is currently available only through calendar 2021 and does not provide sufficient detail to break out the PCE subcategories that would not be taxed, so national data is used to estimate the non-taxable subcategories. Taxable PCE is estimated to be approximately 84.0 percent of total Georgia PCE, which is projected from 2021 levels to 2028 based on May 2022 Congressional Budget Office (CBO) projections of personal income growth nationally, averaging about 4.14 percent annually over the 2022-28 period

New owner-occupied home investment (including improvements to existing homes) grew nationally at an average annual rate of 10.5 percent from 2014 through 2021, but growth rates varied widely, from only 1.2 percent in 2019 to 25.1 percent in 2021. Georgia investment in new homes and home improvements is estimated based on BEA data on national investment in residential structures through 2021 shared down to Georgia using Census estimates of U.S. and Georgia owner-occupied shares of homes by structure type (i.e., single- and multi-family, and manufactured homes). For example, approximately 81 percent of single-family homes in Georgia are owner-occupied while Georgia's share of all single-family homes nationally is about 3.2%, so those figures are multiplied by the total investment in new single-family structures nationally to arrive at the Georgia estimate for owner-occupied, single-family home investment. A similar calculation is done for multi-family structures and manufactured homes. Improvements and ownership transfer costs are shared down to Georgia based on Georgia's share of all owner-occupied homes. Projections beyond 2021 assume growth based on CBO projections for nominal GDP growth nationally (averaging 4.75 percent annually).

Finally, the estimated base must be adjusted for tax avoidance or evasion. For example, businesses may underreport their taxable sales and online sales by out-of-state businesses will likely remain difficult to tax, as they are now under the sales and use tax. No estimates of underreporting by dealers with nexus in the state are available for Georgia, but Washington State periodically reports estimates of taxpayer noncompliance for sales and other taxes based on audits of random samples of returns, finding from the most recent study an estimated rate of underreporting for the sales tax of approximately 1.8 percent. This figure does not include untaxed sales by sellers who are not registered as dealers in the state, i.e. those operating in the so-called underground or informal economy, but it is assumed either that this activity is not included in reported PCE figures used to estimate the tax base, as is the case for illegal goods and services according to BEA, or that any amounts included are not material. As for untaxed online sales, estimates made for fiscal notes on various versions of the "economic nexus" bill from the 2017 legislative session suggest another roughly 1.06 percent of taxable sales under the FairTax would remain untaxed, bringing the total noncompliance rate to 2.86 percent.

Resulting tax base and revenue projections by fiscal year are shown in Table 3. Revenues are net of administrative credits (vendor compensation), estimated for simplicity at ¼ percent of the gross amount of tax. Given the assumed January 1, 2024, effective date of the bill, FY 2024 includes only consumption and revenue for the second half of the fiscal year.

NOTE: The tax base under the proposed state FairTax includes sales of new motor vehicles purchased for consumer use, which would also continue to be taxed under the state's Title Ad Valorem Tax (TAVT) at a rate of 7 percent, bringing the total tax rate on new vehicles to 13.7 percent. Because this seems likely to have been an oversight in drafting, FairTax revenue is also estimated under the assumption that, while the TAVT would remain in place, new vehicles would be carved out of the tax base for the FairTax to avoid double-taxation. The estimated effect on projected revenue from removing all new vehicles from the base is also presented in Table 4. If the bill is so amended, these amounts would add directly to the revenue loss estimates presented in Table 1.

Table 4. Projected Tax Base and Revenues

($ *billions*)	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028
Taxable PCE	$217.1	$453.2	$472.5	$492.4	$513.2
Residential Fixed Investment	17.4	36.1	37.4	38.7	40.2
Total Taxable Consumption	$234.5	$489.4	$509.9	$531.1	$553.4
Taxed Consumption (net of 2.86% noncompliance adjustment)	$227.7	$475.3	$495.3	$515.8	$537.4
Tax Revenue at 6.7%*	$15.2	$31.8	$33.1	$34.5	$35.9
Addendum: Effect of Exempting Consumer-use New Vehicles ($ *millions*)	($354.7)	($740.6)	($772.1)	($804.5)	($838.4)

* net of administrative credits estimated @ 1/4% of gross tax amount

FairTax Monthly Rebates

A Family Consumption Allowance or rebate (sometimes referred to as a "prebate") is to be paid to each and every eligible household in the state to offset the tax liability for some base level of spending. Rebate amounts are based on federal poverty level income (PLI) guidelines, published annually by the Department of Health and Human Services (HHS), which income levels vary according to the number of persons in the household. The base for calculation of rebates is generally the PLI for the given household size, but includes an adjustment referred to as the "marriage penalty elimination amount" for married couple households, calculated by adding an amount equal to the difference between the PLI for a one-person household and the amount added for each additional person. This base amount is then multiplied by the tax rate, 6.7 percent, to determine the annualized amount of the rebate. The rebates are assumed to be payable to all legal resident households in the state on a monthly basis, for each month of residency.

For purposes of this note, a base year estimate of the total prebate payments is made for calendar year 2022 based on growing Census estimates of 2021 Georgia households, approximately 4.0 million, by OPB's projection of Georgia population growth for the year, approximately 1.0 percent. The number of married households and the average household size are also from 2021 Census estimates, with married households grown to 2022 at the same rate as total households. PLI figures are from HHS for 2022. CY 2022 rebate estimate calculations are shown in Table 5.

Table 5. Rebate Base Year Estimate

	CY 2022
2022 Poverty Level Income:	
1st Person	$13,590
Each Additional Person	$4,720
Marriage Adjustment	$8,870
2021 GA average Household size	2.84
2022 Est'd GA Households	4,040,506
2022 Est'd Married GA Households	1,900,099
Avg PLI Base before Marriage Adj.	$22,275
Avg PLI Base with Marriage Adj.	$26,446
Gross Rebate Base ($mil)	**$106,855**
Rebate Payments ($ mil)	**$7,159**
Avg. Annual Rebate per HH	**$1,772**

Total rebate payments are projected to grow from CY 2022 based on projected inflation, which affects PLI going forward, and population growth. Inflation estimates are based on OECD projections for 2023 to 2024 and CBO projections from January 2024 to 2028 of CPI inflation while population growth is again based on OPB projections. Average household size and the married share of households are assumed constant. The projected total rebate payments on a fiscal year basis through FY 2028 are presented in Table 1, with payments beginning mid-FY 2024.