DOAA
Georgia Department
of Audits & Accounts

Greg S. Griffin
State Auditor

February 27, 2023

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

SUBJECT: Fiscal Note
Senate Bill 118 (LC 43 2594)

Dear Chairman Hufstetler:

The bill has three sections that would impact state revenue collections. The provisions would:

- amend the existing tax credit for qualified child and dependent care expenses to increase the match of the federal credit from 30 percent to 100 percent and make the credit refundable;
- create a refundable state child tax credit equal to 25 percent of the federal child tax credit; and
- create a refundable state income tax credit equal to 20 percent of the federal earned income credit (EITC).

The bill would be effective for tax years beginning on or after January 1, 2023.

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. The refundable state child tax credit results in a revenue reduction of nearly $1 billion in FY 2024 to 2026. The revenue reduction is smaller in later years because of a scheduled reduction in the federal child tax credit on which the state credit is based. FRC provided a range of $516.5 to $556.3 million for the state EITC in FY 2024, while the child and department care credit changes were significantly less at just over $113 million. The appendix provides details of the analysis.

Table 1. Estimated State Revenue Effects of LC 43 2594

($ *millions*)	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028
High Case	($1,638.6)	($1,669.4)	($1,691.6)	($1,231.7)	($1,252.1)
Low Case	($1,598.7)	($1,589.6)	($1,580.6)	($1,094.2)	($1,088.5)

Impact on State Expenditures

The Department of Revenue (DOR) would occur additional one-time and annual costs associated with the bill (see Table 2). Additional staffing costs are associated with three audit staff and examiners in the taxpayer services division. The two divisions also estimate significant costs associated with printing and mailing associated with audit notices and refunds.

Table 2. Estimated Short-Term Expenditure Effects of LC 43 2079

	One-Time Costs	Annual Costs*
Audit Division		
Staff (Two audits and one examiner)	$7,650	$228,250
Mailings		$472,500
Taxpayer Services Division		
Staff (15 tax examiners)	$38,250	$983,700
Mailings		$520,000
Total	**$45,800**	**$2,204,450**

Existing DOR resources would be used to make necessary information system changes. The changes would take six employees approximately 30 weeks, equating to approximately $381,000 in staff time.

Respectfully,

Greg S. Griffin
State Auditor

Kelly Farr, Director
Office of Planning and Budget

GSG/KF/mt

Analysis by the Fiscal Research Center

Section 2 – Qualified child and dependent care expenses credit

Section 2 of the bill proposes to amend O.C.G.A. §48-7-29.1, the existing qualified child and dependent care expense credit, by increasing the match of the federal credit under IRC Section 21 from 30 percent to 100 percent and by making the credit refundable for all the taxable years beginning on or after January 1, 2023. To estimate the revenue effects of this provision, the projected tax expenditure baselines from the Georgia Tax Expenditure Report for FY 2024 are extended through FY 2028 based on pre-pandemic trend growth. This baseline is then adjusted upward based on historical differences between credits generated and those utilized in a given year to reflect the proposed refundability of the credit and finally grossed up to reflect the higher match of the federal credit. Baseline tax expenditures and proforma projections with the proposed modifications are provided in Table 3.

Table 3. Baseline and Proforma Tax Expenditures and Net Revenue Impact of Section 2

($ *millions*)	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028
Baseline	($46.8)	($48.0)	($49.2)	($50.4)	($51.6)
Proforma	($159.9)	($164.0)	($168.1)	($172.2)	($176.3)
Net Revenue Effect	**($113.1)**	**($116.0)**	**($118.9)**	**($121.7)**	**($124.6)**

Section 3 – State child tax credit

Section 3 of the bill proposes to create a new, refundable state tax credit equal to 25 percent of the federal child tax credit under IRC Section 24, subject to the taxpayer's income for purposes of determining eligibility for the federal child credit remaining below the relevant eligibility limits after adding back net operating loss (NOL) carryforwards deducted on their federal return in arriving at federal adjusted gross income (AGI). Eligibility for the credit depends on, among other things, AGI being below certain limits based on filing status and the number of eligible dependents.

We use Statistics of Income (SOI) data for Georgia from the Internal Revenue Service, aggregated data from returns filed for TY 2020 with a Georgia address at the time of filing. These SOI data would not include nonresident Georgia taxpayers and would also differ in counting of part-year residents, excluding those who move out of state before filing their returns for the year. SOI data show that TY 2020 federal returns from Georgia claimed approximately $3.9 billion of federal child tax credits, including amounts reported on both line 19 and line 28 (the refundable portion of the federal credit) of Form 1040. Administrative tax return data from the Department of Revenue (DOR) for which federal form data are available include only e-filed returns, so likely materially understate the total amount of federal credits claimed by Georgia taxpayers. The amount claimed on federal returns by Georgia e-filers for TY 2020 totaled approximately $3.6 billion, generally supporting the use of the SOI aggregate figures for the base year of our analysis.

From the TY 2020 base year, we project the Georgia credit amount – 25 percent of the federal credit – based on the Governor's Office of Planning and Budget (OPB) 2021 projections of the state's child population (aged 0-14). OPB's projections show an average decline in this population of approximately 0.4 percent per year from 2020 to 2027. Notably, the congressional Joint Committee on Taxation (JCT) projects a similar, though slightly faster, decline in its tax expenditure estimates for the federal child tax credit from 2023 to 2025, the period after expiration of the pandemic expansion of the credit in 2021 and before expiration in TY 2026 of modifications made in the Tax Cut and Jobs Act (TCJA).

Under current federal law, the per-child amount of the federal credit is scheduled to fall from $2,000 to $1,000, the level before passage of TCJA, in TY 2026. TCJA's increased income limits for the federal credit will also expire in TY 2026, if not extended. JCT's federal tax expenditure estimates project the federal cost of this credit dropping approximately in half beginning TY 2026, thus we make a similar adjustment, impacting the estimates for FY's 2027 and 2028. Results are reported in Table 4.

Table 4. Projected Tax Expenditure Cost of Section 3

($ *millions*)	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028
Net Revenue Effect	($969.2)	($965.1)	($961.1)	($479.5)	($478.5)

Section 4 – State earned income tax credit

Section 4 of the bill proposes to create a state earned income tax credit (EITC) equal to 20 percent of the federal EITC. The credit is subject to the taxpayer's income for purposes of determining eligibility for the EITC remaining below the relevant eligibility limits after adding back net operating loss (NOL) carryforwards deducted on their federal return in arriving at federal adjusted gross income (AGI). Eligibility for the credit depends on, among other things, AGI being below certain limits based on filing status and the number of eligible dependents.

Based on administrative tax return data from the Department of Revenue (DOR) for which federal EITC data are available, approximately 977 thousand Georgia taxpayers claimed the federal credit in TY 2020, including about 910 thousand full-year residents, 26 thousand part-year residents, and 32 thousand nonresidents. The total amount of federal EITC claimed was approximately $2.46 billion, $2.30 billion of that by full-year residents. For purposes of this fiscal note, it is assumed that the Georgia EITC would be adjusted for part-year and nonresident filers, as are most deductions and exemptions, to reflect the filer's Georgia share of total AGI shown on the Georgia return's Schedule 3, line 9.

Approximately 3.5 thousand filers claiming the EITC also reported federal NOL carryforwards on their Georgia returns, where they are an addition to federal AGI in arriving at Georgia AGI and taxable income. Reported NOL carryforwards are added to reported federal AGI for comparison to the relevant EITC eligibility limits.

Using a microsimulation model of the proposed credit, together with the DOR return data for TY 2020, it is estimated that about 958 thousand Georgia filers would have received the Georgia EITC in an aggregate amount of about $236.1 million for TY 2020 had the proposed law been in effect at the time.

As an alternative source, because the return data from DOR only includes e-filers and thus may understate the number and amount of federal EITC claims by Georgia taxpayers, we use Statistics of Income (SOI) data for Georgia from the Internal Revenue Service. These aggregated data include returns filed for TY 2020 with a Georgia address at the time of filing, so would not include nonresident Georgia taxpayers and would also differ in counting of part-year residents, excluding those who move out of state before filing their returns for the year. SOI data show approximately 1.07 million TY 2020 federal returns from Georgia claiming approximately $2.71 billion of federal EITCs. Given refundability of the proposed state EITC, this implies proforma TY 2020 Georgia EITCs of approximately $271 million.

We project the DOR-based and SOI-based estimates for TY 2020 forward under the following assumptions:

- *High-growth case*: The DOR-based estimate of $236 million is projected forward assuming growth at the rate of population growth, as projected by OPB, plus inflation at actual rates through TY 2022 and using Congressional Budget Office February 2023 forecasts of inflation for subsequent years. Inflation is measured with a 1-year lag as the prior year's inflation is the basis for annual inflation adjustments to EITC parameters made by the IRS.

- *Low-growth case*: The IRS-based estimate of $271 million is projected forward assuming a 1.5 percent annual decline in EITC amounts claimed, the average annual percent change from 2013 to 2020.

Projected revenue effects under the high- and low-growth cases are provided in Table 4. Note that these projections differ in two ways from those in the fiscal note for the similar state EITC of prefiled bill LC 43 2497. The earlier proposal was for a refundable EITC at 10 percent of the federal credit instead of 20 percent, so the amounts in Table 5 are roughly twice those of the earlier note. Much smaller differences arise in the high-growth case from the updated inflation forecast from CBO.

Table 5. Projected Tax Expenditure Cost of Section 4

($ *millions*)	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028
High-Growth Case (DOR)	($556.3)	($588.4)	($611.7)	($630.5)	($649.0)
Low-Growth Case (SOI)	($516.5)	($508.5)	($500.7)	($493.0)	($485.4)

Note: the changes in all three sections are assumed to impact state revenues at the time of filing of returns. Given that TY 2023 is the first tax year affected, the first state fiscal year impacted is assumed to be FY 2024.