

Office of the President

## **Comments to the House Ways and Means Committee Tax Reform Working Group on Education and Family Benefits**

**April 15, 2013**

### **Introduction**

On behalf of the higher education associations listed below, which represent approximately 4,300 two- and four-year public and private non-profit colleges and universities, we thank you for the opportunity to share our views with the working group on several tax provisions which are important to college students and their families.

Although originally enacted discretely, the current federal tax code contains a number of provisions that taken together create a framework that functions as a kind of “three-legged stool” intended to advance three important goals: 1) to encourage saving for higher education; 2) to help students and families pay for college; and, 3) to assist with the repayment of student loans. We strongly support this “three-legged stool” framework. In addition, we believe tax reform provides an excellent opportunity to make improvements to certain provisions in order to maximize their effectiveness and enhance access to higher education.

### **Provisions to Encourage Saving for Higher Education:**

The tax code currently contains two provisions intended to encourage families to save for higher education: Section 529 Education Savings Plans and Coverdell Education Savings Accounts.

- **Section 529 Education Savings Plans** – Under Section 529, states are authorized to sponsor “Qualified Tuition Programs” that are tax-advantaged savings vehicles for qualified postsecondary education expenses, such as tuition, fees, books, required supplies, equipment and room and board. There are two types of 529 Plans: savings plans, which allow families to save for expenses, and pre-paid tuition programs, which generally allow families to make advance tuition payments to cover future attendance at a designated in-state public college or university system.
- **Coverdell Education Savings Accounts** – Under Section 530, individuals can contribute up to \$2,000 annually tax-free to pay for the qualified education expenses of a designated beneficiary. Individuals remain eligible to contribute with income up to \$110,000 (\$220,000 for joint filing). Qualified education expenses are broadly defined to include tuition, fees, course materials and room and board. The \$2,000 annual maximum contribution cap was recently made permanent as part of the American Taxpayer Relief Act of 2012 (ATRA).

According to a recent Treasury report, Section 529 Education Savings Plans and Coverdell Education Savings Accounts offer “an attractive and convenient means of saving for college that offer substantial tax benefits.”<sup>1</sup> We strongly believe that the tax code should continue to encourage savings for higher education expenses. By doing so, the federal government incentivizes financial responsibility in families with the means to save for college. This long-term planning helps reduce student debt, and allows governments and charities to better target scarce student aid funds to those without the means to save.

### **Provisions to Help Pay for Higher Education:**

The current tax code contains several provisions that help students and families pay for higher education: the American Opportunity Tax Credit (AOTC), the Lifelong Learning Credit, the above-the-line deduction for qualified tuition and related expenses (tuition deduction), Section 127 Employer-provided Educational Assistance, and the Sec. 117 Qualified Scholarship exemption.

- **American Opportunity Tax Credit (AOTC)** – The AOTC significantly enhances and broadens the permanent Hope Scholarship Credit by increasing it from \$1,800 to \$2,500, expanding eligible expenses, making it available for four rather than only two years of college, increasing the income phase-out thresholds, and making the credit partially refundable. Since its enactment, there has been a significant increase in the use of the AOTC across income levels, particularly for middle class students and their families. According to a recent U.S. Government Accountability Office (GAO) study, in 2009, more than 9 million tax filers claimed the AOTC, receiving \$16 billion in tax benefits. Almost 65 percent of these benefits went to middle-income families with incomes above \$40,000.<sup>2</sup> The AOTC was recently extended for five years under ATRA.
- **Lifetime Learning Credit (LLC)** – Under this permanent nonrefundable tax credit, a taxpayer can claim up to 20 percent of the taxpayer’s first \$10,000 – for a maximum of \$2,000, which is not indexed for inflation – of qualified tuition and related expenses paid during each calendar year. The LLC is available for all years of postsecondary education, and there is no limit on the number of years that it can be claimed for each student in a family. The credit phases out for a taxpayer with an income of \$60,000 or more (\$120,000 for married taxpayers filing jointly). The LLC serves as incentive for taxpayers to pursue higher education or to acquire new or enhanced job skills, thereby strengthening our nation’s workforce. According to the GAO, in 2009, 3.4 million taxpayers claimed the credit for a total of \$2.4 billion. Approximately 80 percent of the taxpayers claiming the LLC had incomes of \$80,000 or less.<sup>3</sup>
- **Tuition Deduction** – The above-the-line deduction for qualified tuition and related expenses permits students or their parents to deduct up to \$4,000 per year in qualified higher education

---

<sup>1</sup> See U.S. Department of Treasury report, *Analysis of Section 529 College Savings and Prepaid Tuition Plans* (Sept. 2009), p.3.

<sup>2</sup> See GAO Report to the Committee on Finance, U.S. Senate, *Higher Education – Improved Tax Information Could Help Families Pay for College* (May 2012), pp. 24, 63.

<sup>3</sup> Id.

expenses from their taxable income. The deduction phases out for taxpayers with incomes of up to \$80,000 (\$160,000 for joint filers). Like the AOTC and LLC, the tuition deduction enhances access to higher education by helping to reduce the cost of attending college. The tuition deduction is particularly beneficial to graduate students who are ineligible for the AOTC. The deduction was extended for one year in ATRA.

- **Enhancing Effectiveness of Tax Credits and the Tuition Deduction Through Consolidation and Simplification**

It is broadly acknowledged that the current set of higher education tax credits and the tuition deduction are overly complicated and difficult for taxpayers to correctly use.<sup>4</sup> We have long supported legislative efforts to consolidate and simplify these tax incentives in order to maximize their impact and enhance access to higher education. We strongly support reform of the current tax credits and tuition deduction to create a simpler, consolidated higher education tax credit that provides assistance towards an associate or bachelor's degree, post-baccalaureate education and lifelong learning. A permanent AOTC-style credit, for example, available beyond the first four years of college, would negate the need for the Hope Scholarship tax credit, a Lifetime Learning Credit and the tuition deduction. We would welcome the opportunity to work with the committee on such an effort during tax reform.

For this reason, we strongly supported the “American Opportunity Tax Credit Permanence and Consolidation Act of 2012” (S. 3267) introduced in the last Congress by Senator Charles E. Schumer. The bill would have made a number of important reforms to the AOTC and Lifetime Learning Credit and benefited families across income categories. The bill significantly improved the current AOTC and Lifetime Learning Credit by consolidating them into one simplified, permanent AOTC that would provide up to \$3,000 per year in tax relief. In addition, the bill incorporated the expanded eligible expenses of the current AOTC, increased income phase-out thresholds and replaced current limits on the number of years a student can utilize the AOTC with a \$15,000 lifetime cap. Moreover, in steps that would have particularly benefited low- and moderate-income students, the bill maintained the 40 percent partial refundability of the current AOTC and better coordinated the interaction of the credit with the Pell Grant, thereby making postsecondary education more affordable. This legislation shared a number of ideas incorporated into bipartisan legislation (H.R. 2458) in the 110<sup>th</sup> Congress introduced by Chairman Dave Camp and then Rep. Rahm Emanuel.

- **Section 127 Employer-provided Educational Assistance** – Section 127 allows employers to offer up to \$5,250 in tuition assistance to employees annually. These funds offer tax benefits to both employers and student employees. According to the most recent available Department of Education

---

<sup>4</sup> See GAO Report to the Committee on Finance, U.S. Senate, *Higher Education – Improved Tax Information Could Help Families Pay for College* (May 2012); GAO Testimony before Subcommittee on Select Revenue Measures, Committee on Ways and Means, U.S. House of Representatives, *Multiple Higher Education Tax Incentives Create Opportunities for Taxpayers to Make Costly Mistakes* (May 1, 2008).

data, the nearly 1 million American workers who used this tuition assistance in the 2007-08 academic year had average annual employment earnings of \$42,711. This provision has been an important means of building and adding to the competencies of the workforce, and is a critical tool to help our nation accelerate its economic engine. The top majors among recipients of tax-free tuition include those in the science, technology, engineering and mathematics fields. More than 35 percent of degrees pursued by employees using education assistance are master's degrees. Section 127 was made permanent in ATRA. This provision should be enhanced to allow employers to offer higher levels of tax-favored tuition assistance to their employees. The \$5,250 annual limit, which has not changed since the 1970s, should be increased with an automatic adjustment for inflation.

- **Qualified Scholarships** – Currently, scholarship, fellowship, and grant funds are excluded from taxable income if the recipient is a student at a primary, secondary, or postsecondary educational institution and the funds are used for the payment of tuition and required fees, books, supplies, and equipment. However, such scholarship/grant aid is subject to taxation if used for living expenses, such as room and board. Prior to the 1986 tax reform bill, such grant aid was not taxed if used to pay non-tuition higher education expenses like room and board. In addition, scholarship, fellowship, and grant funds received in exchange for teaching or research services are subject to taxation. Low-income students, who receive scholarships or grants to cover all, or most, of their college costs, including room and board, are particularly at risk under current policy. Current law could be improved to broaden the tax-free treatment for these grants to be used to cover non-tuition expenses such as room and board.

#### **Provisions to Assist in Repayment of Student Loans:**

The current tax code contains provisions that affect the ability of students to repay student loan debt incurred while enrolled in a college or university.

- **Student Loan Interest Deduction (SLID)** – This above-the-line deduction permits taxpayers with less than \$75,000 of income (\$155,000 for joint filers) to deduct up to \$2,500 in federal student loan interest payments each year. To qualify, a student loan must have been taken out to pay for qualified education expenses, such as tuition and fees, course materials, room and board. Over the course of an undergraduate education, many students take out at least one federal student loan. According to the College Board, 35 percent of undergraduates used a federal Stafford loan to finance their education in academic year 2011-12. Managing student loan debt after graduation can be a significant hardship. Recent federal actions have increased borrowing costs by eliminating the six-month interest grace period college graduates previously received, and by implementing interest charges for graduate student borrowers while they are in school. With these increased loan costs, SLID has become even more important. The current \$2,500 interest limit has been in place since 1997. SLID should be expanded to allow a greater amount of interest to be deductible.
- **Federal Loan Forgiveness Programs** – The Income-Based Repayment (IBR) and Income Contingent Repayment (ICR) programs permit students with high student loan debt to more easily manage their debt and avoid default by lowering their monthly loan payments, which are capped at

a percentage of their disposable incomes. Under IBR or ICR, some individuals may end up with loan repayment plans that extend beyond 25 years; however, provisions in the Higher Education Act allow for any loan debt amount remaining after 25 years to be forgiven (in 2014, forgiveness will begin after 20 years). Unfortunately, the tax code will penalize such responsible borrowers by treating debt forgiven under IBR and ICR as taxable income. The tax code is also inconsistent in the way it handles such forgiven debt by excluding it from taxable income under other federal loan repayment programs, notably Public Service Loan Forgiveness and the Teacher Loan Forgiveness Program. We strongly support efforts like the legislation introduced in the 111<sup>th</sup> Congress by Rep. Sander Levin which would remedy this problem by expanding the current income tax exclusion to cover amounts forgiven under the IBR and ICR programs.

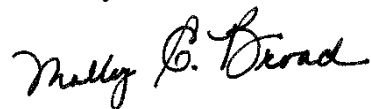
As students have come to increasingly rely on loans to finance their college education, we strongly believe that the tax code should continue to assist borrowers as they repay their loans. In addition, as Congress sought to address the challenge of increased student loan debt when it created the Income-Based Repayment and Income Contingent Repayment programs, we believe that the tax code should not penalize responsible borrowers and undermine this effort taxing debt forgiven under these programs.

**Conclusion:**

We strongly support the “three-legged stool” framework in the current tax code that: encourages saving for higher education; helps students and families pay for college; and assists borrowers as they repay student loans. Our nation’s long-term economic growth depends upon a larger well-educated and trained workforce. Together these tax provisions help to improve access to and completion of higher education, and advance the important goal of producing enough well-trained workers essential to our economy. We believe that tax reform provides an excellent opportunity to improve some of the individual provisions that will make the framework more effective for students, their families and taxpayers repaying student loans.

We thank the Education and Family Benefits Tax Reform Working Group for the opportunity to submit these comments and for considering our views.

Sincerely,

A handwritten signature in black ink that reads "Molly C. Broad". The signature is written in a cursive, flowing style.

Molly Corbett Broad  
President

Education and Family Benefits Tax Reform Working Group

Page 6

April 15, 2013

On behalf of:

American Association of Community Colleges

American Association of State Colleges and Universities

American Council on Education

Association of American Universities

Association of Community College Trustees

Association of Jesuit Colleges and Universities

Association of Public and Land-grant Universities

National Association of College and University Business Officers

National Association of Independent Colleges and Universities

National Association of Student Financial Aid Administrators