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, I am submitting this written testimony for the record of the June 24, 2014, Hearing on Higher Education and the Tax Code. We appreciate the opportunity to submit our views to the committee on several tax provisions that are important to college students and their families as well as on the issue of college costs, which was also discussed during the hearing.

Although originally enacted discretely, the current federal tax code contains a number of provisions that taken together create a framework that functions as a kind of “three-legged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 Department 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.”\(^1\) 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, the Lifelong Learning Credit, the above-the-line deduction for qualified tuition and related expenses (tuition deduction), Section 127 Employer-provided Educational Assistance, and Sec. 117(d) Tuition Reduction.

- **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 low and middle-income 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. Indeed, approximately 66 percent of these benefits went to low and middle-income families with incomes at or below $80,000, with more than 50 percent going to those with incomes at or below $60,000.\(^2\) The AOTC was extended until the end of 2017 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.\(^3\)

- **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 expenses from their taxable income. The deduction phases out for taxpayers with incomes of up to

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


\(^3\) Id.
$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 expired at the end of 2013.

- **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. 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 have long supported reform of the current American Opportunity Tax Credit (AOTC), the Hope Scholarship Credit, the Lifetime Learning Credit, and the tuition deduction, which are overly complex and difficult for students and their families to correctly use. We believe a consolidated credit can simplify the higher education tax benefits while retaining positive aspects of the present credits and deductions to better serve low- and middle-income traditional and nontraditional students now and in the future, helping them attain an associate or bachelor’s degree or pursue post-baccalaureate education or 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.

Because the opportunity to reform these provisions does not come along very often, it is critically important that any reforms address the needs and circumstances of the broad range of students in higher education. To be sure, many students in college still come from the traditional cohort, age 18-22. However, today nearly 50 percent of undergraduates and three-quarters of all students are adult learners, age 23 or older, with a quarter over age 30, a proportion that will likely continue to grow. These students are not just older than their traditional classmates. They tend to work full-time or have dependents—including multiple roles as parents and caregivers—serve in the military, or some combination of these, and take a longer time to complete their degree. Moreover, 50 percent of all students attend part-time, which inevitably increases time to completion. While the median time to degree for all bachelor’s degree recipients is 4.3 years, for adult students (between ages 24-29), the median time to degree is 6.6 years. A reformed, consolidated credit should preserve current benefits for as many students as possible and take into account the demographic profile of all of today’s students. The number of these nontraditional students will increase in the future, and any legislation that creates a permanent, consolidated credit should also address their needs.

For this reason, we strongly supported the “American Opportunity Tax Credit Permanence and Consolidation Act of 2013” (S. 835) introduced by Senator Charles Schumer (D-NY). The bill would make a number of important reforms to the AOTC and Lifetime Learning Credit, benefiting...

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4 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).
families across income categories. The bill significantly improves 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 incorporates the expanded eligible expenses of the current AOTC, increases income phase-out thresholds and replaces current limits on the number of years a student can utilize the AOTC with a $15,000 lifetime cap. Moreover, in steps that will particularly benefit low- and moderate-income students, the bill maintains the 40 percent partial refundability of the current AOTC and better coordinates the interaction of the credit with the Pell Grant, thereby making postsecondary education more affordable. This bill provides a model for reform of these provisions but there are others such as Rep. Lloyd Doggett’s (D-TX) “American Opportunity Tax Credit Act of 2013” (H.R.1738), which currently has 112 House cosponsors. We welcome the opportunity to work with the committee on reforming these important higher education tax incentives.

- **Section 127 Employer-provided Educational Assistance**—Section 127 allows employers to offer employees up to $5,250 annually in tuition assistance, which is excluded from taxable income. It is effectively a matching grant program in which the federal government forgoes a proportionally small amount of revenue to leverage the investment employers make in their employees and the American workforce. According to the most recent available Department of Education data, the more than 1.1 million American workers who used this tuition assistance in the 2011-12 academic year had average annual earnings of $53,880. 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 growth. The top majors among recipients of this benefit include those in the STEM fields. More than 35 percent of degrees pursued by employees using education assistance are master’s degrees.

This provision is a terrific public-private partnership, helping to leverage private dollars for higher education. It supports innovation by employers such as Starbucks, which recently joined with Arizona State University in a partnership which relies on Section 127 to provide access to higher education for Starbucks’ employees. It is widely supported by the employer community and organized labor, and members from both sides of the aisle.

Recently made permanent by ATRA, we believe that this very successful tax provision should be enhanced to allow employers to offer higher levels of tax-favored tuition assistance to their employees. We recommend that the $5,250 annual limit, which has not changed since the 1970s, be increased with an automatic adjustment for inflation. This would be an extremely effective reform that would generate more private sector funds for financial aid to low- and middle-income students.

- **Sec. 117(d) Qualified Tuition Reduction**—Section 117(d) permits educational institutions, including colleges and universities, to provide their employees, spouses or dependents with tuition reductions that are excluded from taxable income. This long-standing provision helps employees and members of their families afford a college education, providing an important benefit to many middle and low-income college employees. A broad cross-section of our employees benefit from Section 117(d). Indeed, under the law, if an institution chooses to offer this benefit, then all employees must be able to receive it. As such, the benefit has been used by a range of employees,
including secretaries and other front-line administrative staff and maintenance and janitorial staff. In addition to the help it provides our employees, Section 117(d) also gives colleges and universities an important tool for recruiting and retaining valued employees, helping maintain the quality of education our schools can offer. It has been particularly important for many small, private, denominational schools to compete for top employees. Eliminating this benefit would particularly harm employees who are poised to send their children to college and have premised their career choices and college savings decisions on the existing tuition benefits for their children, hurting the lowest-paid college employees the most.

In addition, many schools combine the Section 117 Qualified Scholarships exemption with Section 117(d)(5) to help mitigate the tax liability of graduate students engaged in teaching and/or research as part of their academic programs, many of whom earn very little and increasingly finance their graduate educations. According to the U.S. Department of Education, in 2011-12, a quarter of all graduate students earned less than $11,000, and half were below $32,000. During that same year, there were 1.3 million master’s degree students—nearly three-quarters of all graduate students—and approximately 31 percent received no financial aid. Forty-six percent of all master’s students and 25 percent of all doctoral students borrowed for their degree. The median amount of those loans per year was $15,665 for master’s students and $17,629 for doctoral students. The repeal of Section 117(d)(5) would likely result in an immediate unforeseen tax burden for these graduate students who would unlikely have the disposable income to satisfy this tax liability and would be forced to finance their education through additional loans. For all of these reasons, we strongly believe that Section 117(d)(5) should be preserved.

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

The current tax code contains provisions that affect the ability of students to repay their student loan debt. As students increasingly have come to rely on loans to finance their college education, we strongly believe the tax code should continue to assist borrowers as they repay their loans.

- **Student Loan Interest Deduction (SLID)**—SLID currently 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 for qualified educational expenses, such as tuition and fees, course materials, and 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, 34 percent of undergraduates used federal loans to finance their education in the 2012-13 academic year. 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 preserved.

- **Exclusion of Discharge of Student Loan Debt**—Currently, the tax code provides an exclusion for student loan debt forgiven for individuals that worked for a specified time period in certain professions or for a class of employers. This tax exclusion applies to several federal and state loan
forgiveness programs, including the Public Service Loan Forgiveness for borrowers working in government and certain nonprofit jobs, the TEACH program to assist future teachers, and the National Health Services Corps Loan Repayment Program, which assists medical health professionals working in underserved areas of the country. Each of these programs permits former students with high student loan debt to more easily manage their debt and avoid default in exchange for working, likely for lower salaries, in ways that serve our society.

Congress created various student loan forgiveness programs, including some of the programs mentioned above, in an effort to increase college access and affordability by lowering the burden of student loan debt. We have long supported these efforts and the tax exclusion of the discharge of remaining student loan debt as part of these programs because we believe in the policy goal and the attendant benefits it provides to the larger society. Indeed, we have long advocated that this tax exclusion be extended to two other federal loan forgiveness programs, the Income-Based Repayment (IBR) and Income Contingent Repayment (ICR), to which it does not currently apply. Repeal of the current tax exclusion of discharge of student loan debt would undermine the purpose of these important loan forgiveness programs. In addition, for those programs that require regular loan repayment over many years, taxing the discharge of remaining student loan debt would amount to punishment of these responsible borrowers.

Currently, there are 18.4 million students enrolled in college in the United States, with approximately 50 percent taking out student loans to pay for college. Student loan debt is now in excess of $1 trillion, exceeding debt in consumer credit cards. At a time when more students are borrowing more money for college, this exclusion should be preserved and expanded to cover amounts forgiven under the IBR and ICR programs.

**College Costs:**

The condition of our economy has elevated the cost of attendance and avenues of access to higher education to sources of genuine anxiety for many American families. While these concerns are understandable, there are also a number of misperceptions about the true cost of attendance that have fueled this dynamic:

- According to the College Board in 2013-14, nearly two-thirds of full-time students attended four year institutions with a published tuition price of less than $15,000. In addition, 38 percent of all undergraduates attended community colleges, where the average published tuition for a full-time student is $3,264.
- Analysis of data reveals that the net tuition price—the actual cost after incorporating financial aid or tuition discounts, as opposed to the “sticker” price—remains within reach of many students and families, particularly at community colleges. According to the College Board in 2013, students at public four-year schools were paying a net tuition of $3,120 per year on average. Unfortunately, as a direct result of cuts in state appropriations, at public four-year campuses the average net tuition increased by $1,180 after inflation over the past five years.
- Over the five years from 2009–10 to 2013–14, after taking into account grants and education tax benefits, the estimated average net tuition (adjusted for inflation) decreased at community colleges by $300 and at private, nonprofit four-year colleges increased by only $40.
The total amount of institutionally provided student financial aid has more than doubled over the last 10 years, increasing faster than the rate of increase in tuition. Indeed, the investment by colleges and universities in student aid has increased over the last decade from $19.7 billion to $44.4 billion in 2013.

Among multiple reasons for rising college costs, there are four particularly strong drivers:

- **State Appropriations**

  For public institutions, which enroll approximately 72 percent of all students, the single largest factor in driving up college costs is declining state support. In the last 20 years, states have systematically reduced spending on higher education, resulting in increased tuition at public institutions to offset the reduced state revenue. Indeed, there is a direct and inverse relationship between the level of state appropriations and the level of tuition increases, as illustrated in the chart below. For example, at many institutions, a 1 percent decrease in state appropriations may result in a 3-5 percent increase in tuition.

  ![Annual Percent Change in Public 4 Year Tuition and State Support](chart.png)

  In 2010, state and local support for general higher education operations fell to a 25-year low in inflation-adjusted terms, while full time equivalent enrollment increased by 61 percent. Over the decade, 2002-2003 to 2012-2013, state appropriations as a share of institutional revenues per student dropped from 68 percent to 53 percent at public institutions. As a result of declining state support, the share of the total institutional revenue from tuition rose from 32 percent to 47 percent at public institutions over the same period. Between 2007–08 and 2013–14, state appropriations for higher education per student declined by 19 percent in real terms, the largest three-year decline in 30 years.

  Private colleges and universities face a different set of circumstances. Few independent institutions receive significant amounts of state support for their operating budgets. Some states provide financial aid that helps students attend these institutions. When state financial aid is reduced as a result of budget cuts, colleges must use even more of their own funds to fill the gap.
Increasingly, public and private colleges and universities have come to rely on private charitable contributions and endowed funds to help fulfill their teaching, research, and public service missions. Private charitable donations work in concert with federal and state investments in student aid to ensure access to higher education for students irrespective of their socio-economic status. Charitable gifts also support teaching, groundbreaking research and technological innovation, and the public service activities of colleges and universities. In short, the partnership with private donors has delivered enormous economic benefits to our society, but unfortunately, it is a partnership undergoing severe stress.

- **Technology and Knowledge Creation**

  With the rapidly changing nature of information technology (IT), the technological expectations and requirements of students, faculty and staff are rising. Beyond initial costs for IT infrastructure, a significant investment of institutional resources goes to the creating and upgrading of technology-enhanced instruction and research media, student services and faculty and staff training. Today’s college students expect institutions to provide information and technological services that allow them to access instructional resources and campus services anywhere and anytime. This is evidenced by the rising use of wireless classrooms, lecture capture and podcasting, mobile apps and e-portfolios, for example. No one wants colleges and universities to be equipped with scientific and technological resources from 2000 as they try to meet the needs of students in 2014 and beyond.

  Moreover, knowledge in most scientific disciplines doubles every seven to 10 years. Whole new fields of science—such as nanotechnology—have emerged from obscure specialties to essential fields of study that can be found at most institutions. Over the past three decades, the annual volume of paper and electronic subscriptions at academic libraries grew sharply from less than 4,700 to more than 25,000.

- **Government Regulation**

  The persistent growth of federal, state and local regulation creates costs for colleges and universities that institutions cannot control but must consider every year in their budgets as they determine tuition. While some of this regulation may be necessary, a substantial share is burdensome, duplicative and contrary to campus mission. Given the range of their activities, colleges and universities are among the most heavily regulated entities in America. In addition to being regulated by state and local governments, higher education is the only industry regulated by every federal agency. According to Sen. Lamar Alexander (R-TN), in 2005, there were more than 7,000 federal regulations governing colleges and universities.

  Regulations impose a heavy toll on colleges and universities in the form of additional staff, increased professional development and training, additional paperwork, creation of computer systems and software to support record-keeping requirements, and higher legal fees. These regulations, in turn, increase operating costs.
• **Work Force**

Higher education is among the most labor- and skill-intensive sectors of the economy, with college graduates comprising almost 70 percent of its employees. Higher education institutions typically spend 60 percent or more of their budgets on human resource costs. In recent years, institutions had sharp increases in benefit expenses that now comprise nearly 25 percent of total human resource costs. Colleges and universities compete with the private sector to hire outstanding individuals—such as engineers, biologists, chemists, doctors and lawyers—for faculty positions.

Efforts to increase productivity or reduce academic personnel costs by increasing class sizes or hiring fewer full-time faculty can have a direct, detrimental impact on academic quality and are very unpopular with students and faculty. Further, student demands for increased non-instructional academic support services (e.g. counseling, health services and campus security) also drive up human resource costs.

**Federal Financial Aid and Efforts to Control College Costs:**

During the hearing, some of the witnesses raised the so-called Bennett hypothesis, which claims that increases in federal student aid drive increases in tuition. A landmark federal study on college costs conducted by the Department of Education in 1998 found that increases in federal financial aid had absolutely no impact on tuition at any type of institution, public or non-profit private. In testimony before the Senate Finance Committee, Professor Bridget Terry Long, found “[c]oncerns about colleges raising tuition prices in response to federal aid appear to be largely unwarranted.” More recent extensive analysis of the issue by economists Robert Archibald and David Feldman not only found no relationship between Pell Grants and increases in tuition at public universities but a reverse effect at private institutions: Increases in the Pell Grant generally reduced private sector tuitions. The bottom line is there is no empirical data that suggests federal aid significantly drives up college prices.

Colleges and universities have taken a wide range of steps to contain and cut costs as well as help students pay for education. On the cost-containment side, these steps have included: layoffs, pay or hiring freezes; improving administrative efficiency; reducing course offerings, enrollments, or full-time faculty; eliminating academic departments; and imposing budget cutbacks and reallocating resources to pay for other institutional needs. On the affordability side, these steps have included: increasing institutional financial aid, imposing tuition freezes, adopting fixed-tuition guarantees, increasing enrollment through reducing class sizes, and reducing administration costs.

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6 *College Tuition Pricing and Federal Financial Aid: Is there a Connection?*, Before the U.S. Senate Committee on Finance 1, 2-3 (2006) (statement of Dr. Bridget Terry Long, Associate Professor of Education and Economics, Harvard University Graduate School of Education).

initiating accelerated degree completion, instituting curriculum innovation, and reducing textbook costs.

**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 committee for the opportunity to submit this statement for the hearing record and for considering our views.

Sincerely,

Terry W. Hartle
Senior Vice President

TWH/ldw

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 Governing Boards
Association of Jesuit Colleges and Universities
Association of Public and Land-grant Universities
Council for Christian Colleges and Universities
National Association of Independent Colleges and Universities