November 27, 2017

The Honorable Mitch McConnell
Senate Majority Leader
United States Senate
Room S-230, The Capitol
Washington, DC 20510

The Honorable Charles E. Schumer
Senate Minority Leader
United States Senate
Room S-221, The Capitol
Washington, DC 20510

Re: Endowment Excise Tax Provision in the Senate Version of H.R. 1, the Tax Cuts and Jobs Act

Dear Majority Leader McConnell and Minority Leader Schumer:

As the Senate prepares to vote on the tax bill that was marked up in the Senate Committee on Finance, I wanted to make sure you and all members of the Senate saw two articles that show the fundamental flaws in the provision that would impose an excise tax on private college and university endowments.

The first is a piece in Bloomberg by Michael R. Strain, a scholar at the American Enterprise Institute, which emphasizes:

“University endowments are a form of wealth. Republicans typically oppose wealth taxes for a variety of reasons. If you tax something, you get less of it, and wealth is not something we want less of. Wealth doesn’t sit under the mattress. It is invested in the economy, which increases the productivity and wages of workers and the economy’s rate of growth. In a world where wealth is mobile, taxing wealth would cause assets to be relocated to other countries.”

America’s colleges and universities are the best in the world and an extraordinary national asset. We don’t want less of them.

The second piece, by George Will, stresses that the proposed tax on endowments would take direct aim at academic excellence.

“To raise less than $3 billion in a decade—less than 0.005 percent of projected federal spending of $53 trillion—Republicans would blur important distinctions and abandon their defining mission,” Will writes.

Both of these insightful articles are attached. I very much hope you will consider them and agree that removing this problematic provision from the Senate tax bill is the appropriate course of action.

Sincerely,

Ted Mitchell, President
Five Reasons Not to Tax University Endowments

It's unprincipled. It's counterproductive. Republicans, come to your senses!

By Michael R. Strain

November 14, 2017

The late Daniel Patrick Moynihan’s prescription for building a world class city? “Build a great university, and wait 200 years.” Moynihan understood that fruit grows when a few square blocks are seeded with producers and consumers of knowledge, intensely focused on those activities.

Republicans seem not to share Moynihan’s understanding. Their tax proposal seeks to subject private universities with endowments of more than $250,000 per full-time student to a 1.4 percent excise tax on their net investment income. There are about 70 such universities.

It's a bad idea.

University endowments are a form of wealth. Republicans typically oppose wealth taxes for a variety of reasons. If you tax something, you get less of it, and wealth is not something we want less of. Wealth doesn’t sit under the mattress. It is invested in the economy, which increases the productivity and wages of workers and the economy’s rate of growth. In a world where wealth is mobile, taxing wealth would cause assets to be relocated to other countries. The saved income that accumulates as wealth has already been taxed, so wealth taxes are a form of double-taxation. The motivation behind wealth taxes is often envy.

Charitable contributions enrich university endowments, and are the source of the investment income Republicans wish to tax. Republicans typically oppose taxing contributions to (traditional) nonprofits, including universities. Any university contributions you make benefit the university, and not you (apart from recognition, like your name on a classroom door). Therefore, discouraging contributions to universities hurts universities, not donors. A taxpayer who donates to a university has less money with which to pay taxes. Allowing a deduction for charitable giving creates a level playing field between those who do and don’t donate to universities. And the tax treatment of university donations recognizes the American commitment to the (partially) private provision of social goods, like higher education.

You might argue that my criticisms are a bit overstated, and you would be right. The GOP proposal isn’t a wealth tax because it taxes income from endowments, and not endowments themselves. And the GOP tax plan doesn’t (directly) change the tax deductibility of university contributions. But the clear target of the plan is university endowments, and taxing their income might reduce charitable contributions. Wealth taxes and the reasons for the charitable deduction are the right things to be thinking about when evaluating this proposal.
Arguing that the GOP plan is a tax on human capital is not an overstatement. Elite universities use endowments in part to relieve students and their families of the burden of paying tuition. Many universities have been increasingly targeting this relief at households who need it most. For example, parents with income below $65,000 do not pay tuition for their children’s Harvard College education. One in five Harvard undergraduates fall into this category. Taxing endowment earnings would make these efforts more difficult, and would probably raise tuition for students from families that would struggle to pay it.

A tax on human capital in a bill intended to raise wages represents policy incoherence that should be more surprising than it is.

Endowment earnings also support the world-class research that make U.S. universities the envy of the world, attracting talent from across the globe. That research advances innovation and, ultimately, social welfare. Moreover, the social returns to university activity exceed the private returns — one reason to subsidize them. Simply living near college graduates raises the wages of less-educated workers. Companies located near research universities generate more patents and spend more on research and development. Cities with more human capital are better able to adapt to economic shocks. Why tax the income that helps make this possible?

That question has answers, and the idea of targeting endowments isn’t new. You often hear that government should redistribute some endowment funds from elite universities to the rank-and-file, to fund federal subsidies for student aid, to reduce tuition and increase scholarships, or to help reduce the burden of student debt. These are bad ideas. But the GOP’s use of the tax revenue — simply to raise $2.5 billion of the $53 trillion the federal government will spend over the next ten years — is even worse.

It makes you wonder if something else is afoot. Universities are increasingly irritating places to conservatives. Jonathan Haidt, who does not identify as a conservative but whose heroic work in challenging the current state of universities is admired by them, asks: “What is the telos” — the purpose, the goal — “of university?” Is it truth, as it should be? Or social justice? Increasingly, it is the latter, and conservatives — these are my words, not Haidt’s — view universities’ pursuit of their understanding of social justice as a part of the broader progressive political project. Conservatives are correct that universities need to reverse course and reaffirm their commitment to their core mission.

But it is beyond unseemly to tax a few dozen institutions in part because you don’t like their politics. It is also shortsighted. When Democrats are in power, will they target the endowments of conservative institutions? Where does this end?

My answer: It should end with the removal of this provision from the GOP’s tax proposal.
The Republicans take aim at academic excellence

By George F. Will

November 8, 2017

Such is the federal government’s sprawl, and its power to establish new governing precedents, mere Washington twitches can jeopardize venerable principles and institutions. This is illustrated by a seemingly small but actually momentous provision of the Republicans’ tax bill — a **1.4 percent excise tax** on the endowment earnings of approximately 70 colleges and universities with the largest per-student endowments. To raise less than **$3 billion in a decade** — less than 0.005 percent of projected federal spending of $53 trillion — Republicans would blur important distinctions and abandon their defining mission.

Private foundations, which are generally run by small coteries, pay a “supervisory tax” on investment income to defray the cost of Internal Revenue Service oversight to guarantee that their resources are used for charitable purposes. In 1984, however, Congress created a new entity, an “operating foundation.” Such organizations — often museums or libraries — are exempt from the tax on investment earnings because they apply their assets directly to their charitable activities rather than making grants to other organizations, as do foundations that therefore must pay the supervisory tax.

Most university endowments are compounds of thousands of individual funds that often are restricted to particular uses, all of which further the institutions’ educational purposes. Hence these endowments are akin to the untaxed “operating foundations.” Yet the Republicans, without public deliberations, and without offering reasons, would arbitrarily make university endowments uniquely subject to a tax not applied to similar entities.

Are Republicans aware, for example, that Princeton University’s endowment earnings fund more than half its annual budget and will support expansion of the student body? They also enable “need-blind” admissions: More than 60 percent of undergraduates receive financial assistance; those from **families with incomes below $65,000** pay no tuition, room or board; those from families with incomes below $160,000 pay no tuition. No loans are required. PhD candidates receive tuition and a stipend for living costs. Furthermore, the endowment has funded a significant increase in students from low-income families: Princeton has recently tripled to **22 percent** the portion of freshmen from families with the most substantial financial needs. The idea that Princeton is largely populated by children of alumni is a canard slain by this fact: Such “legacies” are **only 13 percent** of this year’s freshman class.

For eight centuries, surviving thickets of ecclesiastical and political interferences, the world’s great research universities have enabled the liberal arts to flourish, the sciences to advance and
innovation to propel economic betterment. Increasingly, they foster upward mobility that fulfils
democratic aspirations and combats the stagnation of elites. It is astonishingly shortsighted to
jeopardize all of this, and it is unseemly to do so in a scramble for resources to make a tax bill
conform to the transitory arithmetic of a budget process that is a labyrinth of trickery.

Great universities are great because philanthropic generations have borne the cost of sustaining
private institutions that seed the nation with excellence. Donors have done this in the expectation
that earnings accruing from their investments will be devoted solely to educational purposes, in
perpetuity. This expectation will disappear, and the generosity that it has sustained will diminish,
if Republicans siphon away a portion of endowments’ earnings in order to fund the federal
government’s general operations.

Its appetite whetted by 1.4 percent, the political class will not stop there. Once the understanding
that until now has protected endowments is shredded, there will be no limiting principle to
constrain governments — those of the states, too — in their unsleeping search for revenue to
expand their power. Public appetites are limitless, as is the political class’s desire to satisfy them.
Hence there is a perennial danger that democracy will degenerate into looting — scrounging for
resources, such as universities’ endowments, that are part of society’s seed corn for prosperous
tomorrows.

Government having long ago slipped the leash of restraint, the public sector’s sprawl threatens to
enfeeble the private institutions of civil society that mediate between the individual and the state
and that leaven society with energy and creativity that government cannot supply. Time was,
conservatism’s central argument for limiting government was to defend these institutions from
being starved of resources and functions by government. Abandonment of this argument is
apparent in the vandalism that Republicans are mounting against universities’ endowments.

This raid against little platoons of independent excellence would be unsurprising were it
proposed by progressives, who are ever eager to extend government’s reach and to break private
institutions to the state’s saddle. Coming from Republicans, it is acutely discouraging.

Disclosure: George F. Will is a former Princeton University trustee.