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Leadership and Advocacy

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The Honorable Dave Camp
Chairman
Ways and Means Committee
United States House of Representatives
1106 Longworth House Office Building
Washington, DC 20515

**Re: Higher Education Provisions in the Tax Reform Act of 2014 Discussion Draft**

Dear Chairman Camp:

On behalf of the American Council on Education and the undersigned higher education associations, we write regarding your recently released discussion draft of the Tax Reform Act of 2014. We commend you for your leadership on an issue as important as tax reform. Reforming the tax code is a critical element to addressing our nation's long-term fiscal health. There are a number of provisions in your discussion draft that would affect students and families, as well as the colleges and universities that serve them. We write now to comment on the education incentives addressed in your discussion draft. In the near future, we will offer additional comments on other provisions affecting higher education.

While the federal tax code is no substitute for the Pell Grant, Federal Work-Study, other federal student aid programs, and the financial aid colleges and universities provide, over the past two decades it has played an increasingly important role in helping low- and middle-income students and families finance higher education. The tax code contains a number of provisions, enacted discretely over time, that 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. This framework helps serve the needs of low- and middle-income students and families as they invest in themselves and their resources in higher education. Moreover, the broadening of access to higher education has larger benefits by helping to sustain a stable and productive society. We believe this framework should be strengthened and made more effective to aid more students and families.

We are very pleased to see that the discussion draft seeks to create a simpler, consolidated higher education tax credit. However, we believe that ultimately, the draft would make substantial changes to a number of higher education tax incentives that will undermine the "three-legged stool" framework and increase the burden on students and families in paying for college. While we support simplification, it can and should be done in a way that will not effectively increase the cost of a higher education for middle-income and nontraditional low-income students and families.

**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 (LLC), the above-the-line deduction for qualified tuition and related expenses (tuition deduction), Section 127 Employer-provided Educational Assistance, and Sec. 117(d) Qualified Tuition Reductions.

- **The American Opportunity Tax Credit, the Lifetime Learning Credit, and the Tuition Deduction:**

We strongly support reform of current tax credits and the tuition deduction to provide students a single credit that provides assistance towards an associate or bachelor's degree, post-baccalaureate education and lifelong learning. Like you, we believe such a tax credit would serve students better than the current overly complex credits and tuition deduction. Indeed, we endorsed the Universal Higher Education and Lifetime Learning Act of 2007 (H.R. 2458), bipartisan legislation which you introduced in the 110th Congress with then-Rep. Rahm Emanuel, which would have created a simpler, consolidated tax credit. Overall, the discussion draft takes several important steps forward to create a simpler, single tax credit. Unfortunately, some of the changes made by the draft would in fact be steps backward for many students and their families who benefit under current law.

Among the most positive steps forward, the bill maintains the expanded eligible expenses of the AOTC, which includes required course materials, as well as permanently extending and indexing a reconfigured AOTC. In a provision particularly important to the neediest students, the bill increases AOTC refundability to 60 percent from the current 40 percent, and permits eligible students to get the maximum value of $1,500 in refundability more easily.

Equally important, the draft better coordinates the interaction of the AOTC with the Pell Grant, and, for the first time, completely excludes the Pell Grant from taxable income. Under current law, the AOTC contains a grant/scholarship offset that has the unintended effect of sharply limiting the size of the tax credit for needy students. As a result, some of the lowest-income students receiving the maximum Pell Grant award ($5,645 for the current academic year) receive ***no*** benefit from the AOTC, regardless of the level of refundability. We applaud you for addressing this problem, which is crucial to helping these needy students.

Unfortunately, the draft would make other changes that would eliminate benefits for many students and thereby adversely impact their financial ability to pursue an associate or bachelor's degree, graduate education, or lifelong learning. In short, we believe that the single, consolidated tax credit created by the draft will harm traditional middle-income undergraduates, adult learners (particularly those with lower incomes), and low- and middle-income graduate students. Because of the draft's reconfigured AOTC, which significantly lowers current income eligibility phase-outs, eliminates the Lifetime Learning Credit, and the tuition deduction, these students would not receive tax benefits they currently rely upon to help finance their higher education.

First, the draft appears to rely on outdated assumptions about the typical student in higher education. 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. Consequently, the bill's four-year limit on benefits, in combination with the elimination of the LLC and tuition deduction for which part-time students are eligible, will cost many undergraduates financial assistance.

A reformed, consolidated credit should preserve current benefits for as many students as possible and take into account the demographic profile of today's students described above. The number of these nontraditional students will increase in the future, and any legislation that creates a permanent, consolidated credit should address their needs. A lifetime dollar usage cap on the benefit rather than a four-year limitation is a potential solution.

Second, with its adoption of the Hope Tax Credit income phase-out limits, the draft reduces the income phase-outs to amounts originally enacted in 1997 for the Hope Tax Credit, which are well below those in the current AOTC. This change would make many middle-income students and their families ineligible for benefits. Many of these families are increasingly caught between stagnant wage growth and their ineligibility for most other forms of federal financial aid. Moreover, these reduced income phase-out limits do not take into account the realities of the cost of living in different regions of the country. For example, no one would consider as wealthy a two-wage earning couple, such as a retail manager and a teacher, living in a high-cost area with one or more children and a combined family income of $135,000. This is equally true of the single parent earning $72,000 with a college-bound child or two. Yet, both families would be ineligible under the reconfigured AOTC in this bill.

Third, the reconfigured AOTC proposed in this draft would provide no benefit to lifelong learners and graduate students, many of whom are low-income and need assistance in pursuing additional skill development or the advanced degrees that employers and our economy require. We need to preserve tax benefits that enhance access for such students.

According to the Tax Policy Center, recent data demonstrate that the LLC is serving students with low and moderate incomes. In 2013, approximately 1.95 million students with an income at or below $75,000 utilized the LLC, including 1 million with an income of $40,000 or less.

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 percentage of African American and Hispanic master's and doctoral students with loans was higher than the national average, and their median loan balances were higher as well. A significant number of master's students pursue degrees in fields that are not highly compensated, like teaching, social work, counseling, or public health. The loss of benefits for graduate students under this draft comes on top of recent decisions by policy makers to end graduate-student eligibility for federal subsidized loans and force them to pay higher interest rates on student loans than undergraduates, a troubling pattern of increasing the cost of education for students pursuing advanced degrees.

In short, we are concerned that the bill takes away benefits from one set of students—both low- and middle-income, as well graduate students—to pay for aid to a narrower set of low-income students. While the goal to enhance assistance to the neediest students is laudable and certainly a goal we share, we do not believe it should be at the expense of other students and families who may be struggling to invest in a higher education.

Given your long-standing interest in improving these overly complex education incentives as well as the bipartisan support for action on this issue, we believe the time may be right to make important reforms to these provisions. Unfortunately, we cannot support the approach taken in the discussion draft. Instead, we urge you to consider other legislative models for reform, such as your previous legislation and the American Opportunity Tax Credit Act of 2013 (H.R. 1738), which would also consolidate the AOTC and Lifetime Learning Credit into one simplified, permanent AOTC but in ways that address the concerns outlined above.

- **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.

Setion 127 was made permanent in the American Taxpayer Relief Act of 2012. Instead of repealing Section 127, we firmly believe this overwhelmingly successful element of the tax code 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.

- **Section 117(d) Qualified Tuition Reductions**

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, as well as faculty. 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. For these reasons, Section 117(d) 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.

- **Repeal of Student Loan Interest Deduction (SLID):**

The draft would repeal the above-the-line deduction for student loan interest. 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 not be eliminated.

- **Exclusion of Discharge of Student Loan Debt:**

The discussion draft would repeal the tax 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 (PSLF) for borrowers working in government and certain nonprofit jobs, TEACH 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 help 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 approximately 20 million students enrolled in college in the United States, with approximately 12 million (60 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, it would be a terrible and shortsighted policy decision to repeal the current tax exclusion for discharge of student loan debt. Instead, this exclusion should be preserved and expanded to cover amounts forgiven under the IBR and ICR programs.

**Conclusion:**

As we know you agree, our nation's long-term economic growth depends upon a larger, well-educated and trained workforce. Despite their well-documented flaws, the current AOTC, LLC, and the tuition deduction work in tandem with other forms of federal student financial support, including Sections 127 and 117(d) and other tax provisions, to enhance access to education, advance attainment and workforce development goals, and help sustain a vibrant society. We are confident that a consolidated credit can simplify the higher education tax benefits while still retaining aspects of the present credits and deductions that serve an increasingly diverse student population. In addition, we strongly believe that comprehensive tax reform provides a critical opportunity to enhance the "three-legged stool" framework of federal education tax incentives.

We stand ready to work with you to improve your discussion draft in ways that will advance the broader goal of reforming the education tax incentives to better serve traditional and non-traditional low- and middle-income students now and in the future.

Sincerely,

Molly Corbett Broad
President

MCB/ldw

On behalf of:

American Association of State Colleges and Universities
American Council on Education
Association of American Universities
Association of Governing Boards of Universities and Colleges
Association of Jesuit Colleges and Universities
Association of Public and Land-grant Universities
College and University Professional Association for Human Resources
Council for Christian Colleges and Universities
Council of Graduate Schools
Hispanic Association of Colleges and Universities
National Association of Independent Colleges and Universities

cc: Ranking Member Sander Levin
Members of the House Ways and Means Committee