U.S. TREASURY DEPARTMENT OFFICE OF PUBLIC AFFAIRS

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TESTIMONY OF DEPUTY ASSISTANT SECRETARY FOR TAX POLICY KAREN GILBREATH SOWELL BEFORE THE HOUSE WAYS AND MEANS SUBCOMMITTEE ON SELECT REVENUE MEASURES ON TAX INCENTIVES FOR HIGHER EDUCATION

Washington, DC--Mr. Chairman, Ranking Member English, and distinguished Members of the Subcommittee:

Introduction

Thank you for the opportunity to appear before the Subcommittee today to discuss tax incentives for higher education, which currently include more than a dozen credit, deduction, exclusion, and deferral provisions. While my testimony today focuses on tax incentives, I note that there are numerous non-tax governmental and other programs to help make higher education affordable and that figure into an individual's or family's decisions regarding higher education. The principal Federal student financial assistance programs are authorized under Title IV of the Higher Education Act of 1965, as amended, and this year will provide more than $90 billion in grant, loan and work-study assistance to students and their families. The Title IV programs include Federal Pell Grants, which serve low-income undergraduate students, and Federal student loans, both the bank-based Federal Family Education Loan program and the Department of Education's Direct Loan program, which serve undergraduate students and their parents, as well as graduate professional school students. In addition, colleges, universities, non-profit organizations, and the private sector furnish scholarships, tuition programs, and other assistance to students pursuing higher education, which according to the College Board exceeds $35 billion annually.

Education is important to the Administration, and we recognize that there is room for improvement in the tax benefits currently provided through the Internal Revenue Code to encourage higher education. We believe that the goal of providing incentives to make higher education affordable is best achieved by identifying the most efficient ways to address student needs and effectively utilizing those mechanisms. My testimony will focus first on a brief review of current tax incentives for college and other post-secondary education, and then discuss areas for potential improvement.

Over the last several decades, various provisions have been added to the Internal Revenue Code to facilitate savings for, and to incentivize the pursuit of, post-secondary education. Building on these existing provisions, the Administration and Congress have made significant progress during the past seven years to provide tax benefits related to higher education, particularly in helping families save for post-secondary education. Notably, the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) expanded Qualified Tuition Programs, also known as section 529 plans, to permit tax-free distributions from plan accounts to be used for post-secondary education expenses, and to allow private educational institutions (in addition to states) to create section 529 plans. The Pension Protection Act of 2006 made these changes to section 529 of the Internal Revenue Code permanent, which helped eliminate uncertainty with respect to this education savings vehicle. Further, the Administration's Budget for FY 2009 includes a proposal to extend the Saver's Credit to contributions to section 529 plans in order to encourage and assist lower-income families in saving for higher education.

EGTRRA also expanded Coverdell education savings accounts (formerly known as Education IRAs) by raising the annual contribution limit to Coverdell accounts from $500 to $2,000, and increasing the income phase-outs for joint filers. In addition, EGTRRA eliminated the disallowance of qualified distributions from Coverdell accounts or section 529 plans for those taxpayers who claim an education credit.

Notwithstanding these savings programs for those who have the ability and who have sufficient time to save for higher education, students and families who are facing immediate education-related costs must confront a patchwork of education-related tax incentives. Current law tax incentives may take the form of a credit against tax liability, a deduction from gross income, an exclusion from gross income, or a deferral of (or exemption from) tax. A detailed table of all the major tax incentives related to post-secondary education is attached as Table 1.

Set forth below is a brief overview of certain of the significant provisions under current law. Focusing on but a few of the available incentives reveals the complexity of these tax incentives, all of which are aimed at post-secondary education, but which apply to different people, in different circumstances, and for different educational ends. It is important to keep in mind that consideration of tax incentives is only one piece of the financial puzzle. Students pursuing higher education – be they recent high school graduates, high school graduates returning to higher education after entering the job market or raising a family, or professionals interested in pursuing an advanced degree or a different career – also have available to them the panoply of government grant and loan programs, as well as the many forms of non-governmental assistance available from educational institutions, non-profit organizations and the private sector.

Overview of Major Current Law Tax Incentives for Post-Secondary Education

As noted above, current law tax incentives may take the form of a credit, deduction, exclusion, or deferral. Many of these incentives have unique eligibility requirements, different phase-out limits, and various filing requirements. Generally, if an expense would qualify under more than one provision, current law allows only one tax benefit for the particular educational expense.

Credits

In 1997, Congress enacted a pair of tax credits to help families pay for higher education – the Hope Scholarship Credit (Hope Credit) and the Lifetime Learning Credit. In 2008, a taxpayer may claim a Hope Credit for 100 percent of the first $1,200 and 50 percent of the next $1,200 in qualified tuition and related expenses (for a maximum credit of $1,800 per student) for the first two years of college for a student enrolled at least half-time. A taxpayer may claim a Lifetime Learning Credit for 20 percent of up to $10,000 in qualified tuition and related expenses (for a maximum credit of $2,000) per taxpayer for any post-secondary education. Both credits are subject to an adjusted gross income (AGI) phase-out. In 2008, the credits phase out between $48,000 and $58,000 of AGI ($96,000 and $116,000 if married filing jointly). Only one credit may be claimed by each eligible student.

Dependent Related Deductions and Credits

For parents supporting college students, there is an extension of the benefit provided by the personal exemption for full-time students aged 19 through 23. Dependent children over the age of 18 do not qualify as children for the personal exemption unless they remain full-time students (through age 23). In 2008 the personal exemption amount is $3,500.

This favorable treatment of a full-time student aged 19 through 23 as a qualifying child also applies for purposes of the Earned Income Tax Credit (EITC). The EITC is a refundable tax credit for working families with low incomes. The EITC for families with one eligible child phases in over the first $8,580 of earned income for a maximum credit of $2,917. The credit phases out between $15,740 and $33,995 of earned income ($18,740 and $36,995 for joint filers). For families with modest incomes, allowing dependent students to qualify as children for EITC purposes provides the families supporting the students with a large tax benefit.

Deductions

A deduction may be allowed above-the-line (i.e., without itemization) for up to $2,500 of interest per year on any qualified education loan, subject to an AGI phase-out beginning at $55,000 ($115,000 if married filing jointly). In addition, through 2007, a taxpayer could claim an above-the-line deduction for qualified tuition and related expenses. The maximum amount of the deduction was $4,000 for taxpayers with AGI below $65,000 ($136,000 if married filing jointly), or $2,000 for taxpayers with AGI between $65,000 and $80,000 ($136,000 and $160,000 if married filing jointly) in 2007.

Moreover, deductions may be allowed to taxpayers for work-related education expenses. An employee who itemizes deductions may deduct work-related education expenses as one of a class of miscellaneous itemized deductions subject to a floor of 2 percent of AGI. Similarly, if an employer pays an employee's education expenses and the reimbursement does not take place through an accountable plan, the amount reimbursed is included in the employee's gross income, but the employee may deduct the expenses as a miscellaneous itemized deduction subject to the 2-percent floor.

Exclusions from Income

In addition to any available credits or deductions, any student who receives a qualified scholarship to a degree-granting program (including certain Federal medical training programs) may exclude from gross income amounts used to pay qualified tuition and related expenses, including fees, books, supplies, and required equipment. Under another provision, originally enacted in 1976, a student may exclude from gross income the amount of a loan that is forgiven if the student works for a required period of time in certain professions or locations. For example, after graduating from college, a student might have a loan forgiven if he or she were to become a teacher in an underserved community. Additionally, there is an unlimited exclusion from the gift and generation-skipping transfer tax for tuition paid directly to a school on behalf of a student, resulting in an incentive to make gifts of college tuition

There are also incentives for individuals to continue their education while employed. An employee may exclude employer-provided education expenses (up to $5,250 since 1986) that are part of an Educational Assistance Program (EAP). Under an EAP, there is no requirement that the education be work-related. In addition, like other work-related expense reimbursements, an employee may exclude from gross income employer reimbursements for work-related education made under an accountable plan.

Certain colleges and universities offer tuition-reduction programs to their employees (which can include the employee's spouse or dependent child). Tuition benefits under such programs may be excluded from gross income. Also, certain graduate students employed in teaching or research may exclude tuition reductions from gross income.

Savings Related Deferrals and Exclusions

Traditionally, tax deferral has been afforded to income saved for retirement in an Individual Retirement Arrangement (IRA). Since 1998, an IRA distribution for qualified higher education expenses has been permitted, with penalties waived, although tax attributable to the amounts distributed is still due. The exclusion covers both Traditional and Roth IRAs (effectively without income limits on contributors), encompasses grandchildren as beneficiaries, and extends qualified expenses beyond tuition and required fees to room and board (for students attending college at least half time), books, and supplies.

As noted above, tax deferral on income saved for college expenses has been available since 1996 through Qualified Tuition Programs, also called section 529 plans. Individuals at all income levels may contribute to a section 529 account or prepaid tuition plan. Contributors may use up to five years of annual gift tax exclusion amounts in advance for a gift-tax-free contribution to a student in a single year (for a total of $60,000 in 2008). There is no limit on the number of permissible student donees per year. Some states permit contributors to deduct a limited amount of contributions for state income tax purposes. Not only does income accumulate tax-free in a section 529 account, but distributions from the account, which include a return of contributions and earnings on those contributions, are also excluded from gross income as long as they are used for qualified higher education expenses.

In 1997, an additional deferral vehicle was created in the form of an Education IRA. Subject to an AGI phase-out, contributors were allowed to contribute in the aggregate up to $500 per year to an Education IRA. As noted above, EGTRRA increased contribution limits to Education IRAs, now named Coverdell Education Savings Accounts, to $2,000. Not only does income accumulate tax-free in a Coverdell account, but distributions from the account, which include a return of contributions and earnings on those contributions, are also excluded from gross income as long as they are used for qualified education expenses, including college expenses.

Since 1988, there also has been a college saving incentive in the form of an exclusion of interest on qualified United States Savings Bonds, provided that the proceeds are used to pay for qualified higher education expenses, subject to an AGI phase-out.

Complexity of Tax Incentives

As reflected in the overview above, the education tax incentives under current law are numerous, often overlapping, and complex. The incentives vary in terms of who may receive benefits, which expenses may be covered, and how large an exclusion, deduction, or credit may be allowed. For example, part-time students may be eligible for the education credits (at least half-time in the case of the Hope Credit) and savings bond interest exclusion. Only full-time students may qualify for the dependent deduction or EITC. Some provisions, like the Hope Credit, are calculated per student, but others, like the Lifetime Learning Credit and the student loan interest deduction, are calculated per taxpayer. Different expenses qualify under different provisions. For example, books, supplies and equipment are qualified expenses for many savings provisions but not for purposes of the credits. Finally, phase-outs with different thresholds apply for purposes of the credits, dependent deduction, student loan interest deduction, Coverdell account contribution, and savings bond interest exclusion.

Consider the following examples and their disparate results. The examples show the value of education benefits available under 2007 law to typical families facing a wide range of circumstances regarding their education expenses.[1] In each example, we calculate the tax benefits that typical families would receive from five tax provisions that may help families with education expenses as in effect for 2007: (a) the Hope Credit, (b) the Lifetime Learning Credit, (c) the tuition deduction (expired December 31, 2007), (d) the dependent exemption, and (e) the EITC. Savings incentives, such as Coverdell accounts and section 529 accounts are not considered.

Because the provisions interact, and because only the EITC is refundable, some families may not have sufficient tax liability to benefit fully from all provisions for which they are eligible. The examples show that total tax benefits vary with the family's specific circumstances: family income, filing status, age of the student, dependent status of the student, whether the student attends part-time, year of study, and their expenses. The families in the examples presented are otherwise typical of families with similar incomes. Of course, the results may vary as the facts vary from the typical family model.

Taxpayers may often be eligible for more than one benefit and only some benefits may be used together. Thus, in many instances, the family must choose among the various benefits. The first example shows the optimal choice may not be obvious before computing the family's taxes.

Example 1: A Family May Need to Make Many Calculations to Determine the Best Outcome

A family of three (Family A) has an income of $100,000. Their 19-year-old son is a full-time freshman at the local state university. His tuition and fees for the year are $6,000. The family knows that they are eligible for the Hope Credit, the Lifetime Learning Credit, the tuition deduction, and the dependent exemption that the family would not be eligible for if the son were not a full-time student. The family may use no more than one of the following three benefits: the Hope Credit, the Lifetime Learning Credit, or the tuition deduction. The family is in the phase-out range for the education credits.

[1] The families in these examples have average levels of deductible expenses and no capital gains income. For families eligible for the EITC, all income is from wages.

- Family A could receive \$2,005 – from the Hope Credit (\$1,555) and the dependent exemption (\$850).
- Family A could receive \$1,690 – from the Lifetime Learning Credit (\$840) and the dependent exemption (\$850).
- Family A could receive \$1,850 – from the tuition deduction (\$1,000) and the dependent exemption (\$850).

Note that if this family had additional children with education expenses, the calculation exercise would be even more complicated. For example, the Lifetime Learning Credit provides a maximum of \$2,000 per family and thus, may be limited for families whose total tuition expenses exceed \$10,000.

The remaining examples calculate the optimal education benefit for a series of taxpayers with different incomes, filing status, and education needs to demonstrate the potential range of results.

Example 2: Individual in Part-time Training Programs – Income Affects Tax Benefits

A single taxpayer attends a training program that costs \$1,000. He attends less than half-time, is not in a degree program, and is not in his first two years of post-secondary study.

- If Taxpayer B earns \$25,000, B could receive a Lifetime Learning Credit of \$200 (the tuition deduction would be worth \$150).
- If Taxpayer B earns \$50,000, B could receive a tuition deduction worth \$250 (the Lifetime Learning Credit would be worth only \$140 due to the phase out).

Example 3: Moderate Income Students Working Toward an Associate's Degree – Family Structure Affects Tax Benefits

A student begins work on an associate's degree at the local community college. The student's family has income of \$25,000. The student attends at least half-time. Tuition and required fees are \$4,000.

- C, a single student who is not dependent on his or her parents, could receive the maximum Hope Credit of \$1,650.
- D, a married student who is not a dependent, could receive a Hope Credit or a Lifetime Learning Credit for \$750. (D's family does not have sufficient tax liability to benefit from the education credit fully.)
- E, the married parents of a 19-year old living at home and supported by his or her parents, could receive benefits totaling \$2,387 from the Hope Credit (\$410), the dependent exemption (\$340), and the EITC (\$1,637).

Example 4a: Students Attending the Local State University – Income Affects Tax Benefits

A college-age student enrolls full-time at the local state university where tuition and fees are \$6,000. The student is in his or her first year of study.

- F, a family earning \$25,000, would receive \$2,387 – from the Hope Credit (\$410), the dependent exemption (\$340), and the EITC (\$1,637).

- G, a family earning $50,000, would receive $2,160 – from the Hope Credit ($1,650) and the dependent exemption ($510).
- H, a family earning $100,000, would receive $2,005 – from the Hope Credit ($1,155) and the dependent exemption ($850).
- I, a family earning $150,000, would receive $1,350 – from the tuition deduction ($500) and the dependent exemption ($850).
- J, a family earning $200,000, would receive $952 – from the dependent exemption.

Example 4b: This example is the same as Example 4a, except that the student is enrolled in his or her third year of study. As a result, the Hope Credit would no longer be available.

- F, a family earning $25,000, would still receive $2,387 – from the Lifetime Learning Credit ($410), the dependent exemption ($340), and the EITC ($1,637).
- G, a family earning $50,000, would receive $1,710 – from the Lifetime Learning Credit ($1,200) and the dependent exemption ($510).
- H, a family earning $100,000, would receive $1,690 – from the Lifetime Learning Credit ($840) and the dependent exemption ($850).
- I, a family earning $150,000, would still receive $1,350 – from the tuition deduction ($500) and the dependent exemption ($850).
- J, a family earning $200,000, would still receive $952 – from the dependent exemption.

Attached as Table 2 are figures that illustrate graphically the tax value of education benefits under 2007 law, taking into account the same five major tax provisions. The figures show the value of the education benefits for typical families by AGI. As in the examples above, the value of these provisions depends on a student's or family's circumstances: the cost of tuition; family income (including whether the family has any income tax liability); whether the student attends college full-time or part-time; filing status; and for the Hope Credit, whether the student is in the first two years of post-secondary education.

The tax savings for a student or family vary significantly with income and tuition level. At the tuition levels paid by most full-time students whose families are eligible for the credits, the Lifetime Learning Credit offers less assistance than the Hope Credit. The Hope Credit, however, is only available to students in their first two years of college. Thus, the tax value associated with a college freshman or sophomore is larger in many cases than the tax value associated with a college junior or senior.

In general, families with incomes under $100,000 in 2007 owing tuition expenses would have maximized their benefits by claiming an education credit; higher income families would have claimed a tuition deduction. As income rises further, the dependent deduction phases out. Families with no income tax liability receive no benefit from the dependent deduction, the tuition deduction, or education credits. However, a college student may qualify a low-income or moderate-income family for the EITC. Large families may lose the benefit of the dependent deduction because they are more likely to be subject to the alternative minimum tax.

Like the family filing a joint return, higher income individuals who file single returns would have maximized their benefits by claiming the tuition deduction, while individuals with incomes under $50,000 would have claimed a credit. A low-income independent student may be eligible for the EITC, but there is no additional education-related benefit from the EITC and thus, the EITC benefit would be the same as for other low-income individuals. Because independent students receive no benefit from the dependent deduction and no education-related benefit from the EITC, the tax value of the benefits associated with an independent student is smaller than the corresponding tax value for a dependent student.

As illustrated in the examples above and the figures in Table 2, the value of various tax incentives attributable to a student may range from a few hundred to a few thousand dollars depending on filing status and AGI. In addition, a claim of one credit or deduction may adversely affect a taxpayer's eligibility for another credit or deduction. From this variety of incentives, a student or parent must discern the optimal combination of tax benefits, which may require many taxpayers to generate alternative complex computations. As in Example 1 above, taxpayers with dependent students who are eligible for a tuition deduction as well as a Hope or Lifetime Learning Credit must run multiple calculations to determine their maximum benefits. Because a qualified expense may not be eligible for more than one benefit, careful recordkeeping is required to ensure both the optimal distribution of expenses and compliance.

Because of the complexity, it may be difficult for a student or parent to determine the value of the tax incentives. In addition, for incentives based on AGI, their value is necessarily retrospective unless the student or parents can predict their income with precision. The more difficult it is to predict the value of the tax benefit accurately, the less effective these benefits are as incentives for the pursuit of a college education.

In addition to the challenges that students face in navigating the myriad education tax incentives to optimize their use, the complexity of these provisions increases the record-keeping and reporting burden on taxpayers, while making it difficult for the IRS to monitor compliance. For example, to claim an education credit, a taxpayer must file a Form 1040 even if he or she otherwise qualifies to file a Form 1040EZ, and the taxpayer must file an IRS Form 8863, a 17-line form with two pages of instructions.

Observations on Simplification

Despite the complexity, because the tax incentives may provide significant value to a family or individual in pursuit of higher education, it appears the various incentives are widely utilized. Table 3 sets forth statistics on the use of the education credits and the tuition deduction based on the most recent IRS data available (for tax year 2005). In the fall of 2005, more than 17 million students were enrolled in college in the United States. As noted in Table 3, a substantial number of these students claimed some combination of the deduction and credits. Overall, in 2005, more than 11.6 million taxpayers claimed an education credit or tuition deduction. Our data cannot capture whether students and families are utilizing the tax incentives optimally, nor what impact, if any, the tax incentives have on decision-making regarding post-secondary education. However, one would anticipate that the complexity would detrimentally affect the efficient utilization and administration of the benefits.

Because the value of a particular tax incentive may not become apparent until the end of the tax year, which may be months after the tuition or other expense was due, and the tax year does not coincide with the academic year, the tax system is not well suited to provide assistance on the "front end" of funding higher education. Generally, tax benefits become available only after year-end (especially in the case of benefits limited by AGI, which is determined at year-end). As a result, the complexity of the current provisions makes it difficult for even a very sophisticated taxpayer to adjust withholding to "advance" the benefit.

In addition, it is important to remember that recent high school graduates do not constitute the only type of person interested in pursuing a college education. Prospective students also include older persons who entered the job market after high school as well as those who have an interest in pursuing an advanced degree or a career different from the one in which they were originally engaged. The provision of different tax incentives for similar higher education expenses may result in the unequal tax treatment of similarly situated taxpayers.

Suggestions have been offered regarding potential simplifications, primarily along three themes. First, it has been suggested that uniform definitions for operative terms such as "qualified higher education expenses" or "qualified tuition and related expenses" and "eligible education institution" be adopted. For example, currently only tuition may qualify for tuition reduction for college employees and gift tax exclusions; tuition and required fees may qualify for the Hope and Lifetime Learning Credits, tuition deduction, and savings bond interest exclusion; tuition, fees, books, supplies, and equipment may qualify for the scholarship exclusion, employer EAP, and student loan interest deduction; and tuition, fees, books, supplies, equipment (and in the case of a student attending at least half time, room and board) may qualify for penalty-free distributions from IRAs, section 529 accounts, and Coverdell accounts.

A second suggestion has been to conform the phase-out thresholds and ranges and index all amounts for inflation. As noted above, different income thresholds apply to the education credits, dependent deduction, student loan interest deduction, and the different savings provisions.

Third, it has been suggested that the education credits be consolidated along with certain deductions. In particular, the AGI phase-out for the credits could be increased to eliminate the need for the tuition deduction; or a single credit could be designed to cover the same population.

While there is clearly a need to address the complexity concerns arising from the current welter of tax incentives, it is important to remain cognizant that revisions to the tax regime may lead to unintended consequences, and any revision may unsettle taxpayer expectations. Recognizing budgetary constraints, legislative reform of tax incentives will almost invariably result in additional benefits for certain taxpayers and fewer benefits for others. Because of the varying profiles of those who seek the benefits of tax incentives for higher education, it may be challenging to streamline the incentives in a way that would benefit the entire target group. Legislative reform of tax incentives would also need to address transition issues for those students or families who may be planning to rely on relevant provisions under current law.

In contemplating legislative reform of current tax incentives, a good starting point would be to focus on clear, simple ways to help students and their families meet the cost of higher education. While efforts can be made to consolidate and streamline the education tax incentives, to be successful, those efforts should not overlook the non-tax benefits that are available to many students, especially those in low-income and middle-income families, either from Department of Education and other federal and state governmental programs or from private-sector sources. Thank you Mr. Chairman, Ranking Member English, and distinguished Members of the Subcommittee for the opportunity to participate in today's hearing on this important subject. I would be pleased to respond to your questions.

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Table 1. Summary of Tax Provisions Related to Higher Education

	Provision	Tax Benefit	Qualifying Expenses	Eligible Individuals	Maximum Annual Amount	Income Limits	Eligible Institution
1	**Hope Scholarship Credit (§ 25A)**	Per student credit against tax	Tuition and required fees	Taxpayer, spouse or dependent in 1st or 2nd year of higher education enrolled at least half-time	$1,800: 100% of the first $1,200 and 50% of the next $1,200 (indexed for inflation)	Phase-out begins at $48,000 ($96,000 if joint return) and is pro rata over $10,000 ($20,000 if joint return) (indexed for inflation)	Post-secondary school eligible for Federal student aid
2	**Lifetime Learning Credit (§ 25A)**	Per taxpayer credit against tax	Tuition and required fees	Taxpayer, spouse or dependent in post-secondary or professional education	$2,000: 20% of the 1st $10,000 total across all eligible students in household (not indexed for inflation)	Phase-out begins at $48,000 ($96,000 if joint return) and is pro rata over $10,000 ($20,000 if joint return) (indexed for inflation)	Post-secondary school eligible for Federal student aid
3	**Earned Income Tax Credit for dependent children aged 19 through 23 (§ 32)**	Refundable credit for families with dependent children aged 19 through 23	N/A	Dependent student enrolled full-time for at least 5 months of preceding year	$2,917 for families with a single dependent child	Phase-in complete at $8,580 Phase-out begins at $15,740 ($18,740 if joint return) Phase-out complete at $33,995 ($36,995 if joint return) (indexed for inflation)	Educational organization – any level

	Provision	Tax Benefit	Qualifying Expenses	Eligible Individuals	Maximum Annual Amount	Income Limits	Eligible Institution
4	**Employer-reimbursed educational expenses paid through an accountable plan (§ 62(c))**	Exclusion from gross income	Tuition, required fees, non-academic fees, books, supplies, equipment, room and board, special needs, transportation and travel	Employee	None	None	Educational organization – any level
5	**Traditional and Roth IRAs (§ 72(t)(7))**	Exception from 10% additional tax on early distributions	Tuition, required fees, non-academic fees, books, supplies, equipment, room and board, special needs	Taxpayer, spouse, child or grandchild (enrolled at least half-time for room and board)	None	None	Post-secondary school eligible for Federal student aid
6	**Cancellation of debt (§ 108(f))**	Exclusion from gross income for income from cancellation of certain student loans	N/A	Borrower who works for a certain period of time in certain professions for any of a broad class of employers	None	None	Educational organization – any level
7	**Scholarships and fellowships (§ 117)**	Exclusion from gross income	Tuition, required fees, non-academic fees, books, supplies, equipment	Degree candidate	None	None	Educational organization – any level

	Provision	Tax Benefit	Qualifying Expenses	Eligible Individuals	Maximum Annual Amount	Income Limits	Eligible Institution
8	**Tuition reduction (§ 117(d))**	Exclusion from gross income	Tuition	Employee of college, spouse or dependent; graduate student employed in teaching or research	None	None	Educational organization – college or graduate school
9	**Employer provided education assistance program (EAP) (§ 127)**	Exclusion from gross income	Tuition, required fees, non-academic fees, books, supplies, equipment and special needs	Employee receiving higher education	$5,250 (not indexed for inflation)	Limits on share of benefit that can go to the highly compensated; no individual income limits	Educational organization – any level
10	**Savings bond interest (§ 135)**	Exclusion from gross income for U.S. savings bond interest	Tuition and required fees	Taxpayer, spouse, or dependent	None	Phase-out $50 per $1000, from $67,100-$82,100 ($100,650-$130,650 if joint return) (indexed for inflation)	Post-secondary school eligible for Federal student aid
11	**Dependent children aged 19 through 23 (§ 152(c)(3))**	Personal exemption deduction for dependent children aged 19 through 23	N/A	Student enrolled full-time for at least 5 months of preceding year	3500 (indexed)	Phase-out begins at $159,950 ($239,950 if joint return) (indexed for inflation)	Educational organization – any level

	Provision	Tax Benefit	Qualifying Expenses	Eligible Individuals	Maximum Annual Amount	Income Limits	Eligible Institution
12	**Business expense deduction (§ 162)**	Itemized deduction	Most business or work related education expenses including transportation and childcare	Taxpayer or spouse	None	Overall limitation on itemized deductions may apply to AGI over $159,950 (indexed for inflation)	Educational organization – any level
13	**Student loan interest (§ 221)**	Above-the-line deduction	Tuition, required fees, non-academic fees, books, supplies, equipment, room and board	Taxpayer paying interest on a qualified education loan incurred on behalf of self, spouse, or dependent	$2,500	Phase-out over $55,000-$70,000 ($115,000-$145,000 if joint return) (indexed for inflation)	Post-secondary school eligible for Federal student aid
14	**Education expenses (§ 222) (effective through 2007)**	Above-the-line deduction	Tuition and required fees	Taxpayer, spouse or dependent receiving higher education	$4,000 or $2,000 subject to income limits	Deduction limited to $4,000 if AGI is less than $65,000 ($130,000 if joint return); and to $2,000 if AGI is less than $80,000 ($160,000 if joint return)	Post-secondary school eligible for Federal student aid
15	**Qualified Tuition Plan (QTP) (§ 529)**	Exclusion from gross income for distributions from QTP accounts	Tuition, required fees, non-academic fees, books, supplies, equipment, room and board, and special needs	Any post-secondary student (enrolled at least half-time for room and board)	None	None	Post-secondary school eligible for Federal student aid

	Provision	Tax Benefit	Qualifying Expenses	Eligible Individuals	Maximum Annual Amount	Income Limits	Eligible Institution
16	**Coverdell Education Savings Account** (§ 530)	Exclusion from gross income for distributions	Tuition, required fees, non-academic fees, books, supplies, equipment, room and board, and special needs	Any student, including primary and secondary (enrolled at least half-time for room and board)	Contributions limited to $2,000 per year, per recipient	Phase-out of eligibility for contributions from $95,000-$110,000 ($190,000-$220,000 if joint return)	Post-secondary school eligible for Federal student aid, or secondary or primary school
17	**Gift tax exclusion** (§ 2503(e))	Exclusion for tuition paid directly to educational institution	Tuition	Any student	None	None	Educational organization – any level

Table 2. The Tax Value of a Student under 2007 Law

Figures A through C below illustrate the combined value of five major income tax provisions effective in 2007 – the Hope Credit, the Lifetime Learning Credit, the tuition deduction, the dependent exemption, and the Earned Income Tax Credit (EITC) – to families with different levels of income and different education expenses. Families are otherwise typical of families with similar incomes.[2] The tax value of a student is the difference between the taxpayer's income tax liability and what it would have been if the student had not enrolled in school. The no tuition case corresponds to a full scholarship and reflects the value of the tax benefits of the dependent exemption and the EITC.

Figure A. Tax Value of a Full-Time College Freshman or Sophomore under 2007 Law (Joint Filers)

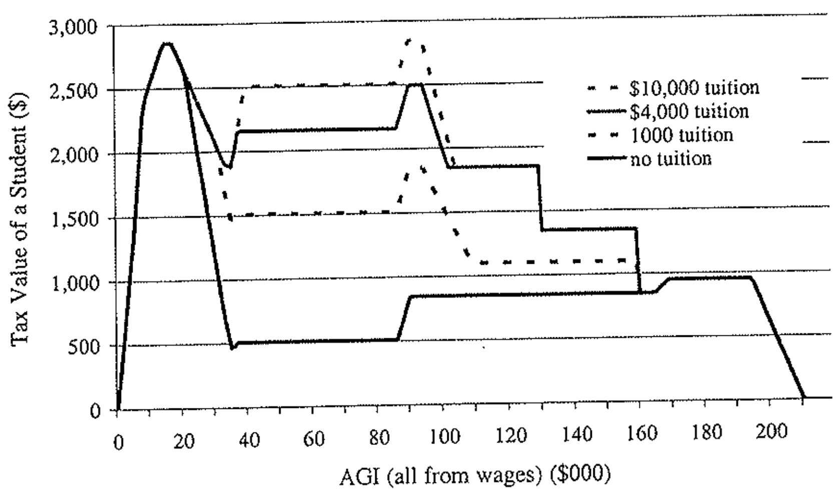
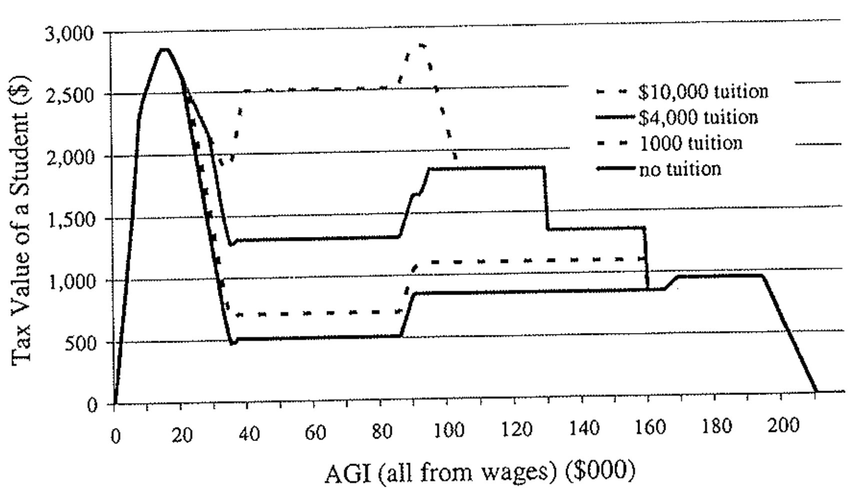


Figure B: Tax Value of a Full-Time College Junior or Senior under 2007 Law (Joint Filers)



[2] The families have average levels of deductible expenses and all income is from wages.

Figure C: Tax Value of an Independent Student Eligible for the Hope Credit under 2007 Law (Single Filers)

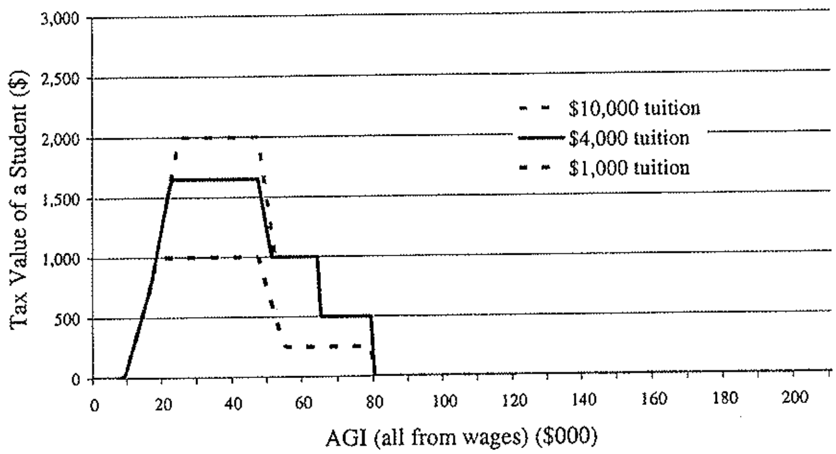


Figure D presents the same information as Figure A, but excludes the benefits of the tuition deduction, which expired on December 31, 20007.

Figure D. Tax Value of a Full-Time College Freshman or Sophomore from Education Credits, Dependent Exemption and EITC (2007 Law, Joint Filers)

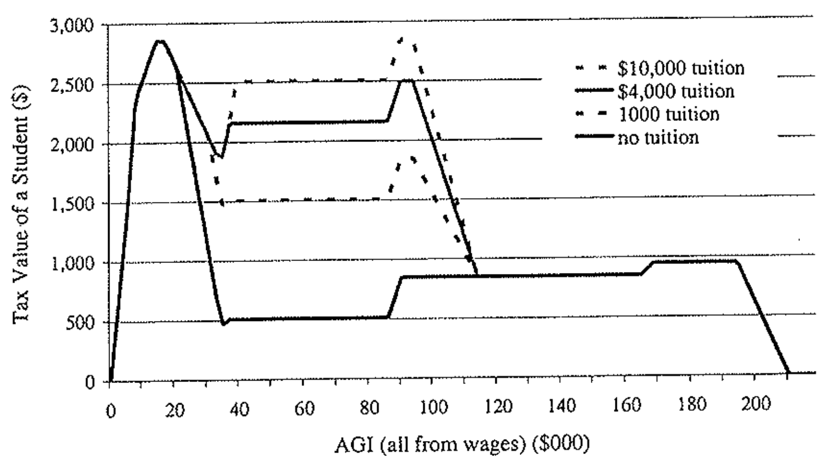


Table 3
Use of Tax Incentives for Higher Education - Tax Year 2005 SOI Data

Education Incentive Claimed		Returns (Thousands)	Dollars (Millions)	Average (Dollars)
Tuition Deduction Only[1]		4,416	10,085	2,284
Hope Credit Only[1]		2,554	2,627	1,029
Lifetime Learning Credit Only[1]		4,011	2,783	694
Any Combination of Above		482	[2]	[2]
	Total	*11,463*		

Department of the Treasury
Office of Tax Analysis

May 1, 2008

Notes:

1 A Hope or Lifetime Learning Credit amount is used to offset individual income tax liability on a dollar-for-dollar basis. In contrast, the tuition deduction is subtracted from the income upon which tax is calculated. Therefore, the value of the deduction to the taxpayer depends on that taxpayer's effective tax rate.

2 The 482,000 returns that claim more than one type of incentive claim a total of $762 million in tuition deductions and $707 million in education credits.