Statement of the
American Association of Community Colleges

For the Hearing of the
Committee on Ways and Means
Subcommittee on Select Revenue Measures
"Tax Incentives for Postsecondary Education"

Presented by
Dr. Wayne Watson
Chancellor, City Colleges of Chicago
Chicago, Illinois

May 1, 2008
10:00 A.M.

Good morning, Chairman Neal, Ranking Member English, and members of the subcommittee, including Chicago's own Representative Rahm Emanuel. I am Dr. Wayne Watson, and I serve as chancellor of the City Colleges of Chicago.

I am here today representing the City Colleges and the American Association of Community Colleges (AACC), on whose board I sit. AACC represents the nation's nearly 1,200 community colleges.

The seven City Colleges enroll more than 110,000 credit and noncredit students annually. Thirty-four percent of our students are African American and 38 percent are Hispanic. Our colleges provide 31 percent of all the adult education in the state of Illinois and enroll more than 27,000 students each year in workforce development programs.

Many policymakers are still surprised to learn that community colleges enroll 47% of all U.S undergraduates. This includes 57% of all Hispanic students and 50% of all African American students in American higher education. These locally oriented institutions have a tremendous economic and social impact and are a prime means of creating upward mobility and a stable middle class. They do this by providing a broad array of offerings: traditional academic transfer courses and occupational programs in areas of demand, as well as developmental education, English as a Second Language, and post-baccalaureate training and certification courses. Community colleges have evolved from being the "Ellis Island" of American higher education—providing higher education access to those who could not otherwise attain it—to serving as a linchpin of 21st-century prosperity for a broad swath of society.

We commend the committee for convening today's hearing. The issues being discussed are of critical importance to American higher education but have been under-emphasized by many policymakers, who tend to focus on the better-known Higher Education Act (HEA) programs.

As I will explain, the Internal Revenue Code is not working for the financially disadvantaged college students who need its help the most; to give one shocking example, a 2003 study by Harvard researcher Bridget Terry Long for the National Bureau of Economic Research showed that the existing tax credits have had *no* impact on increasing college enrollment. However, fairly straightforward policy changes can alter this situation. A tremendous amount is at stake because access and success in college remain highly correlated with family income, and the tax code can help alter that correlation. Such a change would bring a more prosperous, competitive America.

I would like to first offer some general comments on the existing tax provisions and then address the "Universal Higher Education and Lifetime Learning Act" (H.R. 2458), which AACC strongly supports.

1) Higher Education Student Financing Provisions Need to Be Consolidated and Simplified

Currently, the tax code contains two credits (Hope and Lifetime Learning) and a tuition deduction that are designed to help finance undergraduate education. In 2007, tax expenditures of approximately $6 billion will be allocated to these three incentives. Despite the fact that they all have the common goal of helping students meet current college expenses (as its name implies, the Lifetime Learning tax credit also assists more nontraditional students), these programs are structured differently—including the type, amount, and percentage of expenses eligible for inclusion. This framework needs to be overhauled. It simply does not make sense to change the tax assistance available to students as they move through postsecondary education, since during that time their costs largely remain the same. The needlessly complicated and uncoordinated nature of the existing tax incentives led the GAO to conclude in testimony to the Senate Finance Committee that "postsecondary tax preferences are difficult for families to understand and use correctly. Perhaps due to the complexity of the tax provisions, hundreds of thousands of taxpayers fail to claim tax preferences to which they are entitled or do not claim the tax preference that would be most advantageous." Incredibly, the GAO estimated that about 50 percent of the returns with "suboptimal" use of the higher education tax benefits were prepared by professional tax preparers.

Therefore, we strongly support consolidation of the Hope, Lifetime Learning, and tuition deduction tax provisions. Doing so will provide a number of benefits. It will rationalize assistance for a student's entire time in college. It will make the credit more widely accessible by being easier to understand than the current patchwork of programs. And it will bring greater efficiency to the Code. We note that the chairman of the full Ways and Means Committee is pursuing overall reform of the Internal Revenue Code. The higher education tax credits cry out for reform.

2) Higher Education Tax Provisions Must Reflect Total Student Expenses

Currently, the Hope Scholarship and Lifetime Learning tax credits and tuition deduction do not allow students to claim nontuition expenses. This exclusion is profoundly disadvantageous and unfair to community college students and public college students generally, because for them tuition constitutes only a small component of their overall college costs. According to the College Board, in the fall of 2007 the average tuition for a full-time community college student was $2,361. (The corresponding figures for public and private four-year colleges were $6,185 and $23,712, respectively.) However, the total cost of attending a community college was $13,126. This included $921 for books and $1,270 for transportation. Average living expenses were $6,875. The Hope and Lifetime Learning tax credits and tuition deduction ignore these real costs of college attendance.

This exclusion of nontuition expenses is inconsistent with other long-standing federal student aid policies. As the Committee is aware, Coverdell and Section 529 savings accounts both allow funds to be used to pay for nontuition expenses. Just as significantly, the Federal Title IV student financial aid programs cover the nontuition expenses described above. Students use Pell Grants, Stafford loans, Federal Work-Study, and other program funds to cover room and board, books, transportation, etc. This has always been the case and is a fundamental tenet of federal student financial assistance.

It is ironic that at a time of fevered concern over college costs, public policy would disadvantage students who choose to, or must, attend a lower-priced institution. This committee must act to end this unwarranted and short-sighted policy. Community colleges urge Congress to act swiftly to modify the higher education financing vehicles to incorporate the bulk of the nontuition expenses described above.

3) Higher Education Tax Incentives Should Assist Students Most in Need, and Be Refundable

There is overwhelming evidence that student attendance and persistence in college is strongly correlated with family income. Low-ability, high-income students are more likely to enroll in and graduate from college than their high-ability, low-income contemporaries. As of 2005, 40.2% of all high school graduates between the ages of 18 and 24 from the bottom income quartile had enrolled in college, while 80.5%, or twice as many, from the top quartile had enrolled (*Postsecondary Education Opportunity,* September, 2007). And yet, the current tax incentives provide the bulk of their benefits to students coming from middle-income and more affluent, even wealthy, families. Given college attendance patterns, this is a moral and policy outrage.

For example, in tax year 2004, less than one fifth of all the benefits from the Hope tax credits went to individuals with incomes of less than $20,000. Less than one half went to those with incomes below $40,000. In contrast, more than 87% of all awards in the Pell Grant program, the government's basic college access program, are awarded to students with family incomes below $40,000.

Even more troubling is the fact that, according to the Congressional Research Service, in 2004 as much as 57% of all the benefits of the tuition deduction went to families with incomes above $80,000. The median family income that year was $44,483. This distribution pattern is due in part to the phase-out of the tuition deduction at $160,000 for joint filers. The Hope and Lifetime Learning credits phase out at $110,000 for joint filers, which is equitable, as it provides benefits to those earning close to twice the current annual median family income.

A long-standing flaw in the Hope and Lifetime Learning credits is their being nonrefundable. This means that those who need help the most receive little or none. The low-income backgrounds of many community college students make refundability of any higher education tax benefits of critical importance to AACC's members. According to our estimates, between 900,000 and 1.3 million credit community college students did not have any tax liability in 2007. This is about 15 percent of the community college credit population and includes students who head families with children, or have no dependents, regardless of whether they file jointly or are single.

H.R. 2458, Universal Higher Education and Lifetime Learning Act

AACC strongly supports H.R. 2458 and urges its enactment. We thank Representatives Emanuel and Camp for introducing this ambitious legislation, which forcefully addresses most of the policy objectives outlined above. Some of the bill's more important features include:

- *Consolidating the Hope, Lifetime Learning, and tuition deduction tax provisions*: As noted, the consolidation and rationalization of these three student financing vehicles is highly desirable, both in respect to student financing as well as ease of administration and use by beneficiaries. We believe that a broadly publicized, easy to understand, unified tax credit would send a powerful message to millions of Americans of the availability of increased federal support for college.
- *Providing greater financing assistance*: In creating a $3,000 credit, the legislation would enhance the amount of assistance currently available to filers. Considering the substantial cost of higher education, as well as the uncertainty of increases in federal student aid programs, we strongly support this increased assistance, which we believe would help increase access to college and reduce

borrowing. Students in all sectors of higher education would benefit greatly by this enhanced support.

- *Using Title IV Student Aid Budgets for Eligible "Tuition and Related" Expenses*: We strongly support inclusion in the new credit of all expenses currently covered by the Title IV federal student financial assistance programs. This would provide consistent treatment across the major federal funding sources for college and will ensure that students attending colleges with low tuitions, but who inevitably incur substantial non-tuition costs, receive needed support. Using the statutory definition of "cost of attendance" contained in the Higher Education Act will also ease administration of the new credit, since this definition is used on college campuses across the country. We note that a similar position has been taken in H.R 5269, introduced by Representative Kevin Brady, and we commend this legislation. Also, Representative English has introduced legislation that would expand the eligible expenses covered by the Hope tax credit, and we are grateful for this support. Lastly, the initial leadership on this issue that was provided by Representative Camp in previous Congresses remains appreciated.
- *Making the Credit 50% Refundable*: H.R. 2458 takes an important step toward ensuring that the population most in need of support gets it, through instituting 50% refundability for the tax credit. Again, the tax code currently denies support to those who need it most in order to attend college, precisely because they are too poor. Although AACC supports full, 100%, refundability, the legislation's provision would represent a substantial improvement over current law.

Thank you again for giving me the chance to appear today before the subcommittee. I would be happy to answer any questions that you may have on these critical issues.