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Bill Pascrell, Jr.
Member of Congress
Washington, D.C.

Re: Committee on Ways and Means; The Tax Code's Burdens on Individuals and Families Demonstrate the Need for Comprehensive Tax Reform

Dear Mr. Pascrell:

I write this letter in response to your Question for the Record, which you posed in a letter dated April 19, 2011.

I share your conviction that the core concern of American families as they save for the future is the education of their children. Other concerns, such as a secure retirement and access to medical care, are also matters of increasing uncertainty for all but the wealthiest Americans, as you well know. Still, there is nothing more important for our country and for future generations than to guarantee that all young Americans have fair access to a sound, high quality education.

If we fail to provide such an education to all Americans, all of our other problems will only become more difficult to solve. The emergence of the United States as a great power in the 20th Century was driven in large part by our commitment to universal pre-college education, and by our development of an unrivaled system of higher education. Even before the onset of our current economic difficulties, we have failed to maintain the system that our parents and grandparents bequeathed to us. If we continue on this path, we will surely see America fade as an economic power. Fortunately, there is still time to avoid that fate.

In your letter, you point out the current Internal Revenue Code includes a number of programs that past Congresses have created to, at least, stem the tide of reduced expenditures on education. These programs reflect the shift in the responsibility of providing education from society as a whole – even though we all gain when Americans are better educated – onto the people who make individual decisions about whether to advance their educations.

It is important to remember that we could still reverse course, shifting the responsibility for funding education back to the states and the federal government and restoring the funding necessary to allow our schools, colleges, and universities to provide education at affordable prices to all. The tax programs that currently exist are a distant second-best, compared to a system in which the federal government assists the states in making the investments necessary to return our educational system to greatness. Still, in the current political environment, half a loaf is better than none. If it is currently not possible to expand direct funding for public education (at the primary, secondary, or post-secondary levels), then the least the government can do is to assist people through the tax code.

Your letter notes that the current set of tax incentives available to fund education is "overly complicated and overlapping." I completely agree. It is, therefore, a good idea to discuss ways to combine and simplify those programs. I would recommend revamping our approach to providing education incentives by combining all of the current provisions into one simple program. Although no current program is perfect, a starting point would be the so-called 529 Plans, which allow tax-free distributions from savings accounts to pay for qualified tuition and other education-related expenses.

Your letter also asks how to make these accounts accessible to middle-income Americans. This problem bedevils all savings-related accounts, as middle-income Americans are finding it ever more difficult to set aside any money at all for savings. Household budgets are simply so tight that many people cannot find the money to put into even the most generous tax-favored savings accounts. The strain on household budgets is, moreover, only becoming more intense as the economy continues to struggle.

This suggests that even expanded 529-like plans would need to include an income-based formula to supplement any saving that a household is able to set aside. For example, if a middle-income household were able to set aside $1000 in a year for higher education – which is not an easy target to reach, for many Americans – the government could match that contribution, either dollar-for-dollar, or on a sliding scale. Lower-income savers could receive higher matching contributions, which could be phased out as incomes rise.

I have been working on some ideas to create this kind of tax-based education incentive program, and I have been in contact with your staff to discuss some of these issues. I would be happy to work with you and your staff to develop legislation that would meet the goals that we both share. For the purposes of this letter, however, I will simply emphasize that it is important to develop a simplified program that is responsive to differences in people's incomes, to allow the resulting program to be both cost-effective and to help those who most need help.

To summarize my views on your central question, I would say that our legislative priorities should be as follows: (1) Expand direct funding to public education at all levels, (2) If we cannot make education affordable again through direct funding, then we should use the tax code to reduce the net cost of education, and (3) If we are going to use the tax code to reduce education costs, we must supplement middle-income families' education savings with matching funds from the government.

There is, however, a further problem hiding behind the issues that I have discussed above. One surprising development in American education is the increasing cost of public K-12 education. While most American's think of public schools as "free" (that is, carrying no specific costs beyond the taxes that people pay each year to support their schools), the fact is that public education has become an increasingly fee-based enterprise.

A May 25, 2011 article in *The Wall Street Journal* ("Public Schools Charge Kids for Basics, Frills") describes the array of fees that have become part of the landscape of American primary and secondary public education. As the article points out, even though teachers' salaries have failed to keep up with inflation, school districts across the country are facing increasing costs and decreasing support from taxes and state funding. The new fees can add up to thousands of dollars per family. Notably, while some of the fees are charged for arguably "non-essential" educational services, such as extracurricular activities (although I urge you to reject the view that such activities are not an essential part of educating our children), many school districts are now charging fees simply for students even to enroll in school, and for such basics as copier paper, and even imposing "graduation fees."

The emergence of these expenses for pre-college education, of course, makes it that much harder for middle-income families to save to send their children to college. No matter what we do to 529 plans, or any other aspect of our current set of programs to help people pay for higher education, the increased costs of public pre-college education are reducing people's ability to pay for college.

This suggests that Congress's highest priority should be to support parents whose children are not yet in college. Doing so will not only help families today, but it will increase the likelihood that they will be able to afford college later. We should, therefore, consider expanding flexible savings accounts, to allow parents to use tax-free funds to pay for these education expenses that have been increasingly shifted onto parents. Again, the first-best choice would be to give direct support to states and school districts, making it unnecessary for schools to resort to these harmful fees. If we cannot directly increase funding for education, however, we can at least allow parents to use pre-tax dollars to pay for their children's pre-college expenses. (Also, I would urge you to think seriously about a structure to subsidize these costs for people of more modest means. Without a subsidy, even an FSA-style approach only reduces the net costs for a middle-income family by 25 percent.)

If you have any further questions, please do not hesitate to contact me.

Sincerely,

Neil H. Buchanan

Professor Neil H. Buchanan