

# **FAMILIES, EDUCATION AND OPPORTUNITIES**

## **Senate Finance Committee Staff Tax Reform Options for Discussion**

**April 18, 2013**

*This document is the third in a series of papers compiling tax reform options that Finance Committee members may wish to consider as they work towards reforming our nation's tax system. This compilation is a joint product of the majority and minority staffs of the Finance Committee with input from Committee members' staffs. The options described below represent a non-exhaustive list of prominent tax reform options suggested by witnesses at the Committee's 30 hearings on tax reform to date, bipartisan commissions, tax policy experts, and members of Congress. For the sake of brevity, the list does not include options that retain current law. The options listed are not necessarily endorsed by either the Chairman or Ranking Member.*

*Members of the Committee have different views about how much revenue the tax system should raise and how tax burdens should be distributed. In particular, Committee members differ on the question of whether any revenues raised by tax reform should be used to lower tax rates, reduce deficits, or some combination of the two. In an effort to facilitate discussion, this document sets this question aside.*

### **CURRENT CHALLENGES AND POTENTIAL GOALS FOR TAX REFORM**

The tax rules should be designed to equitably and efficiently collect revenue. In addition, while some disagree with this practice, the tax rules are often used to promote other policy objectives, such as incentivizing certain economic behavior that policymakers consider socially valuable.

The current tax code inherently affects decisions about whether to work, marry, have children, and pursue an education. It does so by deciding how to adjust tax burdens in light of these different circumstances. Tax reform provides an opportunity to rethink how and to what degree the tax code should reflect Americans' values regarding families, work, and education.

Following are some potential broad principles for reform in this area:

- Account for the costs of raising children in a manner that is equitable, efficient, simple, promotes opportunity, and takes spending programs into consideration
- Ensure that the tax code does not create large disincentives to work, taking into account tax rates, the phase-out of tax expenditures and means-tested transfer programs, and dependent care costs
- Carefully consider the existing tax incentives and disincentives to marry
- If the tax system includes education incentives, maximize their effect on educational attainment
- Carefully consider the implications of demographic trends
- Simplify the tax code and provide certainty by making temporary provisions permanent, eliminating them, or allowing them to expire

Some specific concerns about the taxation of families and education today include the following:

- **Complexity:** There are a large number of tax provisions related to children, work, and education. Many have different requirements and definitions, and some are temporary. This complexity and uncertainty results in confusion, unintended errors, large costs to taxpayers of complying with the tax code, and a weaker response to any tax provisions that policymakers intend to influence taxpayers' decisions.
- **Work disincentives:** The effective marginal tax rate at many income levels is sometimes surprisingly high because of various phase-outs (e.g., Earned Income Tax Credit, personal exemptions, child tax credit, Supplementary Nutrition Assistance Program, Temporary Assistance for Needy Families, and Medicaid) as well as the explicit statutory rates in the income and payroll taxes. A recent Congressional Budget Office (CBO) analysis found that some workers near the poverty line face effective marginal tax rates as high as 60%, and closer to 100% when one also considers phase-outs in the transfer system.
- **Work disincentives for primary caregivers and secondary earners:** Primary caregivers are adults with primary responsibility for caring for a dependent, such as a child or elderly parent. Some research suggests that primary caregivers have less of an incentive to work than others earning similar wages because of the cost of child and dependent care. According to the U.S. Census, in 2011, the average cost of full-time child care was about \$7,400 per year, while median household income was \$50,100. In addition, among married couples, joint filing and the graduated structure of the income tax

system reduce the incentive for the lower-paid spouse (sometimes called the “secondary earner”) to work. This is because the lower-paid spouse’s earnings are effectively taxed at a higher marginal rate because of the other spouse’s earnings.

- **Marriage incentives and disincentives:** Marriage penalties and bonuses exist in the current tax code, meaning that, depending on their marital status, individuals may pay more or less income tax. As long as the tax code is progressive and married couples are taxed jointly rather than as individuals, there will be marriage penalties, marriage bonuses or both. According to the Congressional Research Service (CRS), roughly 20% of married couples pay a marriage penalty, while roughly 60% receive a marriage bonus.
- **Low bang-for-the-buck for tax incentives:** Some argue that tax incentives in this area, for example for higher education, could achieve more at a lower cost. For example, research by the CRS suggests that education tax incentives are smaller for those least likely to attend college. In addition, students often do not receive tax benefits for college until months (or even years, for example, in the case of the student loan interest deduction) after their tuition is due. The delay may result in education tax benefits having less impact on the decision of whether to attend or complete college than some would like.
- **Increasing cost of higher education:** Some are concerned that the existence of federal subsidies for education, including tax expenditures, drives up the cost of college and post-graduate education. According to Moody’s, the cost of tuition and fees has more than doubled since 2000, outstripping the growth of real estate during the housing bubble.
- **Duplication with spending programs:** Some argue that the tax system should not subsidize the cost of children or education because direct spending programs can be more narrowly targeted and are more transparent. At a minimum, many believe that tax benefits and direct spending benefits should be more coordinated.
- **Fairness:** Some think that the tax code should do more to address increasing income disparities in the U.S. Others think the tax code is not a significant cause of increasing income disparities and should not be used to reduce these disparities as the tax code is already too progressive. Similarly, some think that the tax code should treat taxpayers raising children more favorably than it currently does compared to taxpayers who are not raising children. Others believe that the current tax code provides sufficient resources for the costs of raising children or should be revised to reduce or eliminate such tax benefits.

## **REFORM OPTIONS**

### **I. CHILDREN AND WORK**

The Internal Revenue Code currently provides several benefits to families related to the cost of raising children. These benefits may incentivize various behaviors within the family. The code contains an exemption for dependents, various credits for having or adopting children, and credits to assist with the cost of care for parents with employment-related expenses. The code also provides work incentives that are tied to not only work, but also the number of children in the household. The following table briefly summarizes these tax benefits.

**Current Tax Provisions for Children and Work**

| <b>Provision</b>                       | <b>Eligible income range</b>                                                                                                                                                                                                                            | <b>Maximum tax benefit in 2013</b>                                                                                                                                                                                     |
|----------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Child tax credit (CTC)</b>          | Refundable portion of credit available only to those with earnings above \$3,000. Credit reduced by \$50 for each \$1,000 or portion thereof taxpayer's AGI exceeds \$75,000 (single) or \$110,000 (married filing jointly), not indexed for inflation. | \$1,000 credit/child, (not indexed)                                                                                                                                                                                    |
| <b>Earned income tax credit (EITC)</b> | The credit amount begins to phase out at an income level of \$17,530 (\$7,970 for taxpayers with no qualifying children). These amounts are indexed. In 2018, the phase out threshold for joint returns will be reduced to its 2007 levels (indexed).   | \$6,044 for taxpayers with more than two qualifying children, \$5,372 for taxpayers with two qualifying children, \$3,250 for taxpayers with one qualifying child, and \$487 for taxpayers with no qualifying children |
| <b>Child and dependent care credit</b> | Credit is reduced for taxpayers as AGI increases from \$15,000 to \$42,000, at which point it reaches its minimum level for all taxpayers, for a minimum benefit of \$600/\$1,200. (Not indexed)                                                        | \$1,050 credit for one child or \$2,100 credit for two or more children                                                                                                                                                |
| <b>Adoption credit</b>                 | Non-refundable credit that phases out between \$194,580 and \$234,580                                                                                                                                                                                   | \$12,970 credit                                                                                                                                                                                                        |
| <b>Dependent exemption</b>             | Exemptions phase out between \$250,000 and \$372,500 for single filers, and between \$300,000 and \$422,500 for joint filers                                                                                                                            | \$3,900 deduction per qualifying child                                                                                                                                                                                 |

|                                               |                                                                                                                                                                                                                                                                                                                                        |                                             |
|-----------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------|
| <b>Employer-provided child care exclusion</b> | Available to all taxpayers, but exclusion may not exceed earnings                                                                                                                                                                                                                                                                      | \$5,000 exclusion from income (not indexed) |
| <b>Head of household filing status</b>        | Available to single filers with dependents. For head of household filers, standard deduction and thresholds for rate brackets and income phase-outs are generally between those for single and joint filers. The tax brackets converge at the 35-percent bracket breakpoint, and diverge again at the 39.6-percent bracket breakpoint. | N/A                                         |

Note: Unless otherwise noted, all dollar amounts in table are inflation-adjusted.

1. **Eliminate all tax expenditures for children and work** ([“Zero-Plan” in The National Commission on Fiscal Responsibility and Reform, “The Moment of Truth,” 2010](#); [S.173 \(113<sup>th</sup> Congress\)](#), the [Simplified Manageable and Responsible Tax Act](#), sponsored by Sen. Shelby)
  - a. Repeal all provisions listed in table above
  - b. If members would like to maintain the current level of progressivity, a challenge with this option would be how to do so, given that these provisions are a significant source of progressivity in the tax code.
2. **Simplify tax provisions related to children and work through some or all of the following reforms**
  - a. Make permanent the expansions to the EITC and CTC that are scheduled to expire in 2017 (FY14 Administration Budget Proposal, estimated to cost \$68 billion over 10 years to extend from 2018-2023; [S.A.4727 to H.R.4853 \(111<sup>th</sup> Congress\)](#), [The Middle Class Tax Cut Act of 2010](#), sponsored by Sen. Baucus; [“Illustrative-Plan” in The National Commission on Fiscal Responsibility and Reform, “The Moment of Truth,” 2010](#))
  - b. Simplify the EITC and reduce its error rate through the following reforms:
    - i. Simplifying rules governing which parent can claim the EITC when parents are separated ([President’s Economic Recovery Advisory Board \(PERAB\), “The Report on Tax Reform Options,” 2010](#))
    - ii. Eliminating restriction for certain workers living with other peoples’ qualifying children ([FY14 Administration Budget Proposal, estimated to cost \\$5.4 billion over 10 years](#); [PERAB](#))
    - iii. Simplifying or eliminating investment income test ([PERAB](#))

- c. Harmonize definitions across tax benefits by, for example, unifying the definition of a qualifying child or making the age of the child the only difference across tax benefits ([Tax Policy Center \(TPC\), “Tax Simplification: Clarifying Work, Child, and Education Incentives,” 2011](#))
  - d. Simplify head of household filing status by either:
    - i. Simplifying requirements, for example, by eliminating household maintenance test for unmarried or estranged taxpayers with dependents who live apart on the last day of the year ([PERAB; National Taxpayer Advocate, “Annual Report to Congress,” 2012](#))
    - ii. Repealing head of household filing status and increasing standard deduction for single parents ([President’s Advisory Panel on Tax Reform \(PAPTR\), “Final Report,” 2005](#))
  - e. Harmonize or eliminate rules permitting divorced or separated parents to agree through legal settlement that non-custodial parent can claim child tax benefits ([PERAB](#))
  - f. Index CTC amount ([H.R.769 \(113<sup>th</sup> Congress\), Child Tax Credit Permanency Act of 2013, sponsored by Rep. DeLauro](#))
- 3. Consolidate existing tax expenditures for children and work** ([CBO, “Budget Options,” 2003; American Enterprise Institute, “Moving Toward a Unified Credit for Low-Income Workers,” 2009; PERAB; Brookings Institution, “Tax Reform for Families: An Earned Income Child Credit,” 2003; PAPTR; Stein, “Taxes and the Family,” 2010](#))
- a. Replace some or all of the following tax expenditures: EITC, CTC, dependent exemption, standard deduction, head of household filing status, child and dependent care credit, and exclusion for employer-provided child care with either:
    - i. Single refundable tax credit for children and work
    - ii. Two refundable credits—one for children and one for work
  - b. Index credit amount and any income thresholds
  - c. Design credit(s) to replicate distribution of existing tax benefits for children and work
- 4. Simplify and better target tax benefits for child care through one or more of the following reforms**
- a. Improve existing child and dependent care credit by, for example:
    - i. Making the child and dependent care credit fully refundable and indexing the parameters for inflation ([S.56 \(113<sup>th</sup> Congress\), Right Start Child Care](#))

[and Education Act of 2013, sponsored by Sen. Boxer; Tax Policy Center \(TPC\), “Tax Subsidies to Help Low-Income Families Pay for Child Care,” 2005\)](#)

- ii. Increasing the beginning of the phase down income threshold from \$15,000 to, for example, \$75,000 ([FY14 Administration Budget Proposal, estimated to cost \\$9 billion over 10 years to extend from 2018-2023](#))
- b. Allow a deduction for child and dependent care costs ([National Women’s Law Center, “Making Care Less Taxing,” 2011; Faulhaber, “How the IRS Hurts Mothers,” 2013](#); deductions are available instead of credits in Idaho, Massachusetts, Montana and Virginia; both a credit and a deduction are in place in Maryland)
- c. Repeal exclusion for employer-provided child care ([Dept. of Treasury, “Tax Reform for Fairness, Simplicity, and Economic Growth,” 1984](#))

## **5. Reduce work disincentives created by phase-outs of tax expenditures and means-tested transfer programs**

- a. Coordinate phase-outs of tax expenditures with each other and means-tested transfer programs to eliminate overwhelming implicit marginal tax rates ([Urban Institute, “The Twice Poverty Trap,” April 1995; Urban Institute, “Considerations in Efforts to Restructure Refundable Work-Based Credits,” November 2009](#))
  - i. Potential tax expenditures affected: EITC, CTC, personal exemption, health insurance affordability credits, adoption tax credit
  - ii. Potential means-tested transfer programs affected: SNAP, TANF, CHIP, Medicaid
- b. Eliminate phase-outs for many tax expenditures, such as the EITC, CTC, and personal exemption ([Fred Goldberg testimony before the Finance Committee, 2005](#))

## **6. Other potential changes for targeted groups**

- a. Modify EITC for childless workers through one or more of the following reforms ([Georgetown Center on Poverty, Inequality and Public Policy, “Expanding the EITC to Help More Low-Wage Workers,” 2009; S.1333 \(110<sup>th</sup> Congress\), Strengthen the Earned Income Tax Credit Act of 2007, sponsored by Sen. Kerry; H.R.3970 \(110<sup>th</sup> Congress\), The Tax Reduction and Reform Act of 2007, sponsored by Rep. Rangel](#)):
  - i. Reduce age cut-off from 25 to 21

- ii. Increase phase-in rate to 15.3% to fully offset payroll tax liability; increase income threshold at which phase-in ends so that a full-time minimum wage worker earns, for example, 150% of poverty line after tax
- b. Make WOTC permanent ([FY14 Administration Budget Proposal, estimated to cost \\$9 billion over 10 years](#)) and potentially expand it ([H.R.2101 \(106<sup>th</sup> Congress\), Work Opportunity Tax Credit Reform and Improvement Act of 1999, sponsored by Rep. Houghton](#))
  - i. Could add in new targeted credits, such as credits for high poverty areas or caretakers reentering the labor force
- c. Streamline WOTC employer certification requirement by, for example, allowing employers to certify employees as members of targeted groups in some circumstances ([S.140 \(113<sup>th</sup> Congress\), Veteran Employment Transitions Act of 2013, sponsored by Sens. Baucus and Hatch](#); [H.R.2082 \(112<sup>th</sup> Congress\), Work Opportunity Credit Improvements Act, sponsored by Rep. Schock](#))
- d. Replace WOTC with payroll credit tied to unemployment rate
  - i. Credit could be a percentage of increase in payroll over a base period ([similar to proposal in FY14 Administration Budget Proposal, estimated to cost \\$26 billion over 10 years](#), and [S.2237 \(112<sup>th</sup> Congress\), Small Business Jobs and Tax Relief Act, sponsored by Sen. Reid](#))
- e. Create tax incentives for job training
  - i. Establish allocable tax credit program to businesses that invest in apprenticeships or to encourage partnerships between businesses and colleges to provide job training ([S.3466 \(112<sup>th</sup> Congress\), Better Education and Skills Training for America's Workforce Act, sponsored by Sen. Menendez](#); [similar to Jobs Training Tax Credit in Rhode Island](#))
  - ii. Create employer-matched, portable, employee-owned savings accounts to finance education and training ([S.26 \(110<sup>th</sup> Congress\), Lifetime Learning Accounts Act, sponsored by Sens. Cantwell, Collins, Smith, and Snowe](#))

## II. MARRIAGE

The federal income tax applies to all citizens and residents of the United States. Individual taxpayers file as single, head of household, married filing jointly or married filing separately. While married couples can file separate returns, the law is carefully structured so that filing separate returns almost always leads to a tax increase for couples compared to a joint return. Couples face a marriage penalty when they pay more income tax filing jointly than they would if

they were single. Conversely, a marriage bonus occurs if a couple pays less tax filing jointly than they would if they were single. For example, as shown in the table below, a single individual with \$50,000 in taxable income is in the 25% marginal income tax bracket. If this individual marries a partner with no income, the new couple would face a 15% marginal income tax rate and would receive a marriage bonus.

**Individual Income Tax Rates by Taxable Income, 2013**

|              | <b>Single</b>          | <b>Head of Household</b> | <b>Married Filing Jointly</b> |
|--------------|------------------------|--------------------------|-------------------------------|
| <b>10%</b>   | \$0 to \$8,925         | \$0 to \$12,750          | \$0 to \$17,850               |
| <b>15%</b>   | \$8,926 to \$36,250    | \$12,751 to \$48,600     | \$17,851 to \$72,500          |
| <b>25%</b>   | \$36,251 to \$87,850   | \$48,601 to \$125,450    | \$72,501 to \$146,400         |
| <b>28%</b>   | \$87,851 to \$183,250  | \$125,451 to \$203,150   | \$146,401 to \$223,050        |
| <b>33%</b>   | \$183,251 to \$398,350 | \$203,151 to \$398,350   | \$223,051 to \$398,350        |
| <b>35%</b>   | \$398,351 to \$400,000 | \$398,351 to \$425,000   | \$398,351 to \$450,000        |
| <b>39.6%</b> | Over \$400,000         | Over \$425,000           | Over \$450,000                |

- 1. Reduce marriage penalties and/or marriage bonuses for all** (following options are mutually exclusive)
  - a. Eliminate marriage penalties (but create sizable marriage bonuses) through either of the following reforms:
    - i. Make tax brackets and other income thresholds for married couples twice the amount for single filers ([PAPTR](#))
    - ii. Allow married couples to elect single filing where more favorable ([S.1429 \(106<sup>th</sup> Congress\)](#), [Taxpayer Refund Act of 1999](#), sponsored by Sen. Roth)
  - b. Eliminate marriage bonuses (but create sizable marriage penalties for some)
    - i. Make tax brackets and other income thresholds for married couples identical to those for single filers (as was the law before 1948)
  - c. Eliminate marriage penalties and bonuses and reduce work disincentives for secondary earners by:
    - i. Repealing married filing jointly filing status ([Alstott, "Updating the Welfare State: Marriage, the Income Tax, and Social Security in the Age of the New Individualism," 2013](#); [CRS, "The Marriage Penalty and Other Family Tax Issues," 1998](#); also the practice in many other countries including Canada, Australia, Italy, and Japan)
      1. All taxpayers would have to file as single
      2. Only the higher earner would be eligible to claim dependents and other non-dividable tax benefits.

3. Could provide that some or all community property rules ignored for tax purposes
- ii. Adopting a flat or flatter tax rate structure to eliminate or reduce distortions in the decision to marry ([S.722 \(104<sup>th</sup> Congress\), USA Tax Act of 1995, Sens. Nunn and Domenici](#); Dick Armey testimony before the Senate Appropriations Committee Subcommittee on the District of Columbia (Mar. 8, 2006); [Snyder, "Taxation of the New Era 'Family Unit'," Tax Notes 417 \(Jan. 21, 2008\)](#))

## **2. Create parity for non-traditional households**

- a. Repeal DOMA for tax purposes ([S.598 \(112<sup>th</sup> Congress\), Respect for Marriage Act sponsored by Sens. Feinstein, Bennett, Bingaman, Brown, Cantwell, Cardin, Kerry, Menendez, Schumer, and Wyden](#))
- b. Allow domestic partners to file as married filing jointly and be treated as spouses for purpose of tax expenditures in certain circumstances ([S.1171 \(112<sup>th</sup> Congress\), Tax Parity for Health Plan Beneficiaries Act of 2011, sponsored by Sens. Schumer, Brown, Cantwell, Cardin, Casey, Collins, Kerry, Menendez, Stabenow, and Wyden](#))
- c. Eliminate a benefit of single filing by domestic partners in community property states by codifying Office of Chief Counsel, IRS Memorandum 200608038

## **3. Provide targeted marriage penalty relief ([S.A.3865 to H.R.4810 \(106<sup>th</sup> Congress\), introduced by Sen. Moynihan](#))**

- a. Eliminate current EITC marriage penalty relief by making income thresholds identical for married and singles
- b. Instead allow lower-earning spouse to claim smaller childless worker EITC

## **III. EDUCATION**

The Internal Revenue Code contains tax benefits for education expenses. The code excludes from income certain education debt forgiveness and provides a deduction for student loan interest. Students are allowed to exclude from income scholarships and fellowships for current expenses. The code also provides several tax credits and a deduction for certain current education expenses. For future expenses, families can save in tax-preferred savings accounts. Definitions and qualifications differ across these tax provisions. For example, most of the tax

provisions contain a phase-out that takes away some or all of the benefit of the provision based on the taxpayer's income. The following table briefly summarizes some of the tax benefits for education.

### Current Tax Provisions for Education

| Provision                                                   | Eligible income                                             | Eligible expenses                                                                                                                            | Max. benefit in 2013                                                                                                         |
|-------------------------------------------------------------|-------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------|
| <b>American Opportunity Tax Credit</b>                      | Below \$90,000 (single filers) and \$180,000 (joint filers) | Tuition, fees, and required course materials for first four years of undergraduate education                                                 | \$2,500 partially refundable credit per year per student<br>\$1,800 nonrefundable credit per student (Estimated 2013 levels) |
| <b>HOPE Credit<br/>(Replaced by AOTC from 2009-17)</b>      | Below \$63,000 (single) and \$126,000 (joint) in 2008       | Tuition and fees for first two years of undergraduate education                                                                              | \$2,000 nonrefundable credit per year per return                                                                             |
| <b>Lifetime Learning Credit</b>                             | Below \$63,000 (single) and \$127,000 (joint)               | Tuition and fees for higher education and courses to improve job skills                                                                      | \$4,000 above-the-line deduction                                                                                             |
| <b>Deduction for Tuition and Fees</b>                       | Below \$80,000 (single) and \$160,000 (joint)               | Tuition and fees for higher education (Graduate and Undergraduate)                                                                           | \$2,500 above-the-line deduction                                                                                             |
| <b>Student Loan Interest Deduction</b>                      | Below \$75,000 (single) and \$155,000 (joint)               | Interest paid on loans taken for higher education tuition, fees, books, supplies and equipment, room and board, and other necessary expenses | \$3,900 deduction per dependent                                                                                              |
| <b>Personal Exemption for Full Time Students Ages 19-23</b> | Below \$372,500 (single) and \$422,500 (joint)              | N.A.                                                                                                                                         | None                                                                                                                         |
| <b>Exclusion for Scholarship Income</b>                     | No income restrictions                                      | Primary, undergraduate, and graduate education tuition, fees, and required course materials                                                  | None                                                                                                                         |
| <b>Exclusion for discharge of student loans</b>             | No income restrictions                                      | Loans taken for higher education tuition, fees, course-related books, supplies, equipment, room and board, and other necessary expenses      | None                                                                                                                         |

|                                          |                                                |                                                                                                                                                                                      |                                      |
|------------------------------------------|------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------|
| <b>Qualified Tuition Programs (529s)</b> | No income restrictions                         | Higher education tuition, fees, books, supplies, equipment, special needs services, and room and board (if at least half-time student)                                               | None                                 |
| <b>Coverdell Savings Accounts</b>        | Below \$110,000 (single) and \$220,000 (joint) | Higher education and K-12: tuition, fees, books, supplies, special needs equipment, and room and board<br>K-12 only: uniforms, transportation, required items and services, computer | \$2,000 contribution per beneficiary |
| <b>Teacher expense deduction</b>         | No income restrictions                         | Books, supplies, computer equipment and software, and supplementary materials                                                                                                        | \$250 deduction per teacher          |

**1. Repeal all education tax expenditures, except the exclusion for scholarships, fellowships, and grants** ([Tax Foundation, “Education Tax Subsidies – Justified or Not?,” 2008](#); [Scott Hodge testimony before the Finance Committee on July 25, 2012](#))

**2. Expand tax expenditures for higher education**

- a. Expand tax credit(s) for higher education tuition through some or all of the following reform options: ([New America Foundation, “Enhancing Tax Credits to Encourage Saving for Higher Education,” 2010](#); [The National Community Tax Coalition, “A Single Higher Education Tax Credit,” 2011](#); [Stegmaier, “Tax Incentives for Higher Education in the Internal Revenue Code,” 2008](#); [CLASP, “Reforming Student Aid,” 2013](#); [S.3267 \(112<sup>th</sup> Congress\), The American Opportunity Tax Credit Permanence and Consolidation Act of 2012, sponsored by Sens. Schumer, Kerry, Menendez, and Stabenow](#))
  - i. Make credit fully refundable
  - ii. Increase maximum credit amount
  - iii. Expand definition of qualified expenses to be similar or identical to Department of Education student grant and loan programs
- b. Expand tax expenditures for education savings account through some or all of the following reforms ([Center for Social Development, “College Savings Match Programs: Design and Policy,” 2011](#); [Heritage Foundation, “Education Savings Accounts: Giving Families Ownership in Education,” 2006](#); [H.R.529 \(113<sup>th</sup> Congress\), Savings Enhancement for Education in College Act, sponsored by Rep. Jenkins](#)):

- i. Allow taxpayers to claim Saver's Credit for contributions to such accounts
  - ii. Provide a tax incentive for employers to contribute to employees' accounts
- c. Expand income exclusion for Pell Grants to cover all education expenses ([The Institute for College Access & Success, "Aligning the Means and the Ends: How to Improve Federal Student Aid and Increase College Access and Success," 2013](#))
- d. All options can be combined with sub-sections (3) and (4) above

### **3. Consolidate and simplify tax expenditures for education**

- a. Repeal most or all of the provisions listed in the table above
- b. Replace repealed provisions with one of the following:
  - i. Single refundable tax credit for tuition for higher education ([S.1501 and H.R.2458 \(110<sup>th</sup> Congress\), Universal Higher Education and Lifetime Learning Act of 2007, sponsored by Sen. Bayh and Reps. Emanuel and Camp; American Bar Association \(ABA\), "Tax Simplification Recommendations," 2001; CLASP, "Reforming Student Aid," 2013; PERAB; Americans for Tax Reform, "The American Opportunity Credit," 2012; Dr. Susan Dynarski testimony before the Finance Committee, 2012](#))
  - ii. Refundable tax credit for college tuition, plus tax-preferred education savings accounts ([Dr. Waded Cruzado testimony before the Finance Committee, 2012; Finance Committee Chairman's Mark of proposals relating to education incentives, 1999](#))
  - iii. Deduction for higher education tuition and expenses ([Heritage Foundation, "Saving the American Dream: The Heritage Plan to Fix the Debt, Cut Spending, and Restore Prosperity," 2011](#))

### **4. Conform thresholds and revise definitions**

- a. If multiple education provisions remain, conform definitions and income thresholds ([TPC, "Tax Simplification: Clarifying Work, Child and Education Incentives," 2011; ABA, "Tax Simplification Recommendations," 2001](#))
- b. Provide that only payments to a qualifying educational institution must be reported to the IRS, rather than payments or billed amounts ([Government Accountability Office, "Opportunities to Reduce Potential Duplication in](#)

**5. Attempt to increase effect of higher education tax expenditures on college enrollment and completion**

- a. Provide education tax credits at time tuition is due to attempt to heighten effect on educational attainment ([CLASP, "Reforming Student Aid," 2013](#); [Dr. Susan Dynarski testimony before the Finance Committee, 2012](#))
  - i. Base credit on prior year's income (with no true-up) so that the credit can be calculated when tuition is due
  - ii. Pay credit directly to college or university so that it reduces tuition directly and there is no need to recapture from student if he or she drops out
  - iii. Credit could be based on FAFSA and paid by Department of Education (DOE) with Pell grants (Note: Payment by DOE is outside of the Finance Committee's jurisdiction)
- b. Encourage DOE to educate junior high and high school students about college affordability ([CLASP, "Reforming Student Aid," 2013](#))
  - i. Permit the IRS to share taxpayer data with DOE so that it can provide each junior high and high school student with an estimate of the cost of attending local colleges, after accounting for tax benefits and direct grants
- c. Better target tax expenditures for education to those least likely to attend college
  - i. Disallow further contributions to education savings accounts once combined balance exceeds a certain threshold and enhance information reporting requirements ([Dept. of Treasury, "An Analysis of Section 529 College Savings and Prepaid Tuition Plans," 2009](#))
  - ii. Limit qualified distributions from education savings accounts to tuition for post-secondary education ([The Institute for College Access & Success, "Aligning the Means and the Ends: How to Improve Federal Student Aid and Increase College Access and Success," 2013](#))
  - iii. Limit tax benefits or apply an excise tax to colleges that engage in legacy admissions ([Kahlenberg, "The Legacy Racket," The Century Foundation, 2010](#))

- 6. Provide tax credit to help pay for some private school and post-secondary school costs** ([General Explanations of the Bush Administration's Fiscal Year 2003 Revenue Proposals; S.550 \(97<sup>th</sup> Congress\), Tuition Tax Relief Act of 1981, sponsored by Sens. Packwood and Moynihan](#))
- a. Provide a tax credit to parents who send their children to private school
    - i. Credit could be limited to cases where taxpayer's child attended a public school that had failed to make "adequate yearly progress" for at least two consecutive years
    - ii. Credit could be, for example, 50% of eligible costs incurred up to \$5,000
    - iii. Eligible costs could include tuition and transportation; could also apply to costs of vocational education
    - iv. Credit could be refundable or non-refundable
- 7. Expand educational access through tax credit for certain K-12 teachers** ([S.378 \(112<sup>th</sup> Congress\), Incentives to Educate America's Children, sponsored by Sen. Rockefeller](#))
- a. Provide a credit to teachers in Title I schools and special education teachers
  - b. Potentially limit credit to first three years of teaching in rural schools and second three years of teaching in urban schools to address different needs (recruitment versus retention)
  - c. Potentially provide a larger credit for teachers in science, technology, engineering, and math (STEM)