Statement of the
American Association of Community Colleges

For the
Senate Finance Committee Hearing
“Realizing a Competitive Education: Identifying Needs, Partnerships and Resources”

Presented by
Dr. Jane Karas
President, Flathead Valley Community College
Kalispell, Montana

March 20, 2007
10:00 A.M.

Good morning. My name is Jane Karas and I am president of Flathead Valley Community College in Kalispell, Montana. I am pleased to be here to present testimony on behalf of the American Association of Community Colleges (AACC). AACC represents 1,202 community colleges from across the country.

The American Association of State Colleges and Universities (AASCU) represents 430 public colleges and universities, and systems of higher education throughout the United States and its territories. AASCU supports the basic principles cited in this statement and will work with congress to achieve the positive impact that implementing these principles could have on needy students.

Many policymakers are still surprised to learn that community colleges enroll 46% of all U.S undergraduates. 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.

Today’s hearing is of unusual importance to our colleges and 12 million students. Over the last two decades, Congress has created a variety of tax incentives designed to help facilitate college attendance. Unfortunately, these incentives have failed community college students. As Dr. Susan Dynarksi told this Committee last December, “The education tax incentives do just about nothing for low-income students at inexpensive public colleges.” It bears emphasizing that access to and persistence in college remains highly correlated with income—to cite just one of many disturbing statistics, in 2004 the college continuation rate for high school graduates from families with incomes between $20,000 and $30,000 was 41.6%; the rate for those with incomes between $100,000 and $150,000 was 86.8%, more than twice as high (*Postsecondary Education Opportunity*, June 2006). As they review higher education financing incentives, we urge committee members to keep this stark reality squarely in their sights.

Fortunately, a few simple changes to the Internal Revenue Code, informed by a few basic principles, can have a tremendous positive impact on needy students trying to finance their college educations. The stakes are large: For the 2002 tax year, more than 10 million students claimed a Hope Scholarship tax credit, Lifetime Learning tax credit, or tuition deduction. This figure represents approximately two-thirds of all the credit students enrolled in higher education. Total expenditures for these provisions were estimated to exceed $6 billion, more than half the amount spent that year on Pell Grants.

Principles for Reforming Higher Education Tax Financing Provisions

As mentioned, the application of few basic principles to the college financing provisions in the Internal Revenue Code can have a dramatic positive impact on community college students. The code should be amended along the following lines:

1) Non-Tuition Expenses Must be Included in Eligible Expenses

Currently, the Hope Scholarship and Lifetime Learning tax credits, and tuition deduction, all prohibit students from claiming non-tuition expenses. This exclusion is profoundly disadvantageous to community college students and public college students generally for the obvious reason that, for them, tuition only comprises a small component of their overall college costs. According to the College Board, in the fall of 2006 the average tuition for a full-time community college student was $2,272. However, the total cost of attending a community college was $12,294. This included $850 for books and $1,197 for transportation. Average living expenses (room and board) were $6,299. At AASCU's four-year public colleges, non-tuition expenses in the current academic year average $9,996. The two tax credits and tuition deduction simply ignore these expenses.

The exclusion of non-tuition costs from tax eligibility directly contradicts other long-standing student aid policies. As the Committee is aware, Coverdell and Section 529 savings accounts both allow the use of funds for non-tuition expenses. Even more significantly, the Federal Title IV student financial aid programs cover all the non-tuition 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 the student financial assistance programs.

It is ironic that at a time of fevered concern over college tuition, public policy would disadvantage students who choose to, or have no choice but to, attend a lower-priced institution. Consequently, AACC cannot support any modifications to these higher education financing vehicles that do not include as allowable expenses at least some of the non-tuition expenses described above.

2) Higher Education Tax Incentives Should Assist Those Who Most Need Them

The distribution of tax benefits via the Internal Revenue Code needs adjustment. A far too large share of the subsidies is going to upper-middle income and even wealthy individuals, and too small a share is being delivered to individuals for whom government assistance might actually impact college attendance. For tax year 2004, for example, 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. By way of contrast, more than 80% of all beneficiaries of the Pell Grant program, the government's basic college access program, were 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. Further confusing policy in this area is the fact that the tuition deduction fully phases out for joint filers with an income of $160,000, while the Hope credits phase out at $110,000. There is no apparent reason for this inconsistency, but we believe that the tuition deduction phase-out level is too high.

Making the Hope tax credit refundable will help deliver benefits to students who greatly need assistance. This lack of refundability, coupled with the item outlined in the next paragraph, is a primary reason why less than one-fifth of all Hope tax credit benefits go to those with incomes of less than $20,000 (2004 data). Although refundability carries with it administrative complexities, the case for adding this feature to the Hope credit, or any credit that replaces it, is so overwhelming that we urge the Committee to take this step. This action should be taken in the name of equity and with the aim of helping our country take advantage of every individual who might potentially benefit from postsecondary education. Generally speaking, the individuals who would benefit from refundability are the type of people who could be motivated to attend college if they were given appropriate incentives.

It is critical that the language in the Hope statute, or its successor, that reduces an individual's tax credit eligibility ("tuition and related expenses") by any Pell Grant or Supplemental Educational Opportunity Grant (SEOG) funds received be eliminated. The current provision denies Hope benefits to the neediest college students. The provision may have been designed to preclude "double-dipping," i.e., using grant funds and a tax credit to cover the same expenses. In practice, however, this provision simply denies the reality of non-tuition college expenses. It also contradicts longstanding Higher Education Act (HEA) policy. As stated, the HEA allows Pell Grants, SEOG, Federal Work-Study, loans and other programs to be used for a wide array of expenses beyond tuition, including room and board—and we repeat that for community college students, as well as four-year public college students, these expenses almost always exceed tuition. We note that there is virtually no chance that our recommended change would result in students getting more federal aid, in the form of grant aid and tax credits, than their total cost of attending college. However, to ensure against that remote possibility, statutory language can be written to definitively prohibit this occurrence.

3) <u>Simplification of Financing Incentives Needs a Focus on Access-Oriented Colleges</u>

AACC supports consolidation or simplification of the existing Hope and Lifetime Learning tax credits as long as the resulting financing vehicle adheres to the basic principles articulated above. Our other primary concern focuses on the metric used to determine eligibility. Any new formula should generally follow the principle used for the Hope tax credit, in which a high percentage of the first "X" dollars of tuition, fees, and other eligible expenses would be covered, with a slightly declining percentage used for the next increment of expenditures. A formula with these characteristics would ensure that students who choose to attend lower-cost institutions such as community colleges (and who, not surprisingly, tend to be less affluent than those attending four-year colleges) receive a fair level of benefit—not the same benefit, but not a radically smaller one. Approximately 80% of the students enrolled in American higher education attend public colleges.

4) Recognize the Needs of Non-Credit/Continuing Education Students

The current Lifetime Learning tax credit, in which 20% of tuition expenses can be claimed, makes a mockery of its name, since it provides only paltry benefits to individuals wishing to use the credit to help finance post-college studies. There is strong evidence that as the global economy further integrates and expands, Americans will increasingly need to acquire greater skills in order to be competitive within this market. (A full 28% of community college non-credit students hold B.A. degrees.) Therefore, as the Committee considers reform of the existing tax credits, it should look for ways to provide helpful benefits to this growing segment of the higher education population.

Comments on Pending Legislation

The following are brief comments on some of the pending pieces of legislation in this area. We hope Committee members find them useful.

1) S. 360, the "Greater Access to Education Act," (Bingaman, Smith)

AACC supports this legislation. It adds to Hope tax credit eligibility the full range of expenses that are covered under Section 529 and Title IV student aid programs. It also makes the Hope and Lifetime Learning credits refundable. Finally, it removes the current Hope provision that subtracts from a student's "tuition and related expenses" any Pell Grant and Supplemental Educational Opportunity Grant amounts received. This policy, coupled with the non-refundability of the Hope credit, conspires to prevent low-income students from benefiting from the Hope scholarship.

2) S.97, the "College Opportunity Tax Credit Act of 2007" (Kerry)

There is much to commend in this legislation. It increases the amount of assistance provided to students and it makes the credit refundable. However, it does not include non-tuition expenses, which is a shortcoming for community college students, as outlined above. The legislation creates a credit for those students who are not enrolled at least half-time as an undergraduate, and this idea holds great promise; over time it might greatly enhance the overall skill level of the nation's workforce.

3) S. 851, "Higher Education Opportunity Act of 2007" (Schumer)

The legislation provides a potentially helpful framework for dramatically simplifying and improving the current higher education financing tax provisions. However, by limiting non-tuition eligibility to $250 for books, it insufficiently recognizes the financing realities facing community college and other students. Each year, community college students spend an average of $850 on books alone. Also, as with the current Hope tax credit, Pell Grant and SEOG awards would be subtracted from eligible tuition amounts when the credit is calculated. As explained, community colleges oppose this policy.

4) S. 301, the "Nontraditional Student Success Act" (Clinton)

This legislation is generally focused on the Higher Education Act, but it also includes an expansion of the Lifetime Learning credit that would dramatically expand benefits to those attending lower-cost programs. It would add non-tuition expenses such as books, supplies, and equipment, and would make the credit refundable. Therefore, it could have a strong positive impact in encouraging people to enroll in non-credit courses that improve their job skills. AACC supports these provisions and hopes that their basic features can be worked into any legislation the committee considers.

Thank you for inviting me to testify this morning and to explain the community college perspective on these issues. There is a great opportunity for significant improvement in the important tax provisions that provide assistance to America's college students and their families. America's community colleges and their students are looking to this Committee to provide the necessary leadership. The AACC stands ready to work with the Committee in this endeavor.