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How Governments Support Higher Education Through The Tax Code

Federal and state income tax provisions aim to reduce costs for students and families

Contents

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Cover photo: Getty Images

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Overview

To maximize the impact of higher education investments and achieve desired policy goals, policymakers should have knowledge of the full range of assistance provided to institutions and students. This means having an understanding of the billions of dollars made available through spending programs and the tax code. However, too frequently these two types of support are not considered in tandem, and most states lack the cost estimates they would need to determine how tax provisions for higher education compare in size to other postsecondary investments.

The federal government and the states each invested more than $70 billion in higher education-related spending programs, excluding loans, in academic year 2014, the latest year for which data are available. But that figure, as substantial as it is, does not paint a full picture of federal and state investments in higher education. It excludes the billions of dollars that the federal government and the 41 states plus the District of Columbia that levy personal income taxes provide to students and their families through tax expenditures—such as credits for tuition and college savings incentives—to help offset postsecondary costs.

These tax provisions—special deductions, credits, exclusions, and exemptions—allow people to reduce their income tax liability and result in lower federal and state government revenue. They are called tax expenditures because they are similar to direct spending both in their budgetary impacts and in the way they can benefit recipients. The tax code contains many such provisions that support specific policy priorities, of which higher education is just one.

Tax expenditures targeted toward higher education can have substantial costs for governments, but those costs are frequently excluded from federal or state debates about the scale and nature of higher education spending for three main reasons. First, tax expenditures are generally not subject to the same recurring budget procedures as are most spending programs for higher education, which are debated regularly during the appropriations process. Instead, they typically are permanent provisions that are rarely revisited once enacted.[1] Second, spending programs and tax expenditures fall under the jurisdiction of different committees at the federal level—and sometimes in state legislatures as well. As a result, the evaluation and oversight of—and legislative debates about—these programs are generally not coordinated. Third, states rarely compile comprehensive information about the cost of their higher education tax expenditures, making it even less likely that provisions at the state level will be part of budget and policy debates about higher education spending programs.

> “Tax expenditures targeted toward higher education can have substantial costs for governments, but those costs are frequently excluded from federal or state debates about the scale and nature of higher education spending.”

A Note on Terminology

For the purposes of this report, the term "spending program" refers to forms of support for higher education, such as grants provided through appropriations acts, and excludes loans issued by federal and state governments. The term "financial aid" refers to grant aid for individual students and does not include general purpose funding that states provide to institutions.

This report focuses on tax expenditures that directly support students and their families in meeting the costs of postsecondary education. The terms "tax provisions" and "tax benefits" are also used to refer to tax expenditures.

The types of tax expenditures discussed in this analysis are the following:

- **Deductions** are subtracted from gross income and reduce the amount of income subject to tax.
- **Credits** directly lower the tax a filer owes, in contrast to deductions, which reduce taxable income. Tax credits can be nonrefundable—they cannot reduce a filer's taxes below zero—or refundable, which can cut filers' tax liability to less than zero and result in a payment to the taxpayer.
- **Exclusions** reduce taxable income by exempting certain types of income from taxation.
- **Exemptions** allow filers to lower their taxable income by a certain dollar value for each individual whom a tax filer can claim as a dependent—for example, the filer, a spouse, and each dependent child.

To help integrate these tax expenditures into broader discussions of higher education finances and policy, The Pew Charitable Trusts catalogued federal and state higher education income tax provisions and examined their extensive linkages across the levels of government. Other tax expenditures benefit higher education institutions, but this study is limited to tax expenditures that are intended to help students and families. The analysis, which is part of a larger series exploring the full range of federal and state support for higher education, found that:

- **Personal income tax expenditures for higher education have substantial costs at the federal level and are comparable to major spending programs.** The value of federal tax provisions for students and their families totaled nearly $35 billion in fiscal year 2014, 14 percent more than the cost of Pell Grants, a need-based financial aid program and the largest federal higher education spending program.
- **Every state that levies a personal income tax has higher education tax expenditures, and although few states comprehensively estimate the costs, in most that do, the provisions make up a sizable part of the support targeted to students and families.** Forty-one states—plus the District of Columbia—have a broad-based income tax, and all of them provide some tax provisions for higher education. However, Pew was able to obtain cost estimates that include forgone revenue for at least two-thirds of relevant tax expenditures from

only nine states and the District. In eight of those nine states plus the District, forgone revenue was equal to more than 25 percent of the financial aid grant portion of state higher education spending. (For more information, see "Why compare forgone revenue from tax expenditures with financial aid spending?" on Page 7.)

- **Federal and state provisions generally target the three phases of postsecondary education financing: saving for the future, offsetting expenses while enrolled, and paying previously incurred costs.** For example, tax advantaged savings plans, commonly known as 529 plans, facilitate saving for future college expenses; the American opportunity tax credit (AOTC) offsets current-year course-related expenses; and the student loan interest deduction helps pay off loans for past costs.
- **States have implemented most of their higher education tax provisions through two key linkages to the federal tax code.** First, when calculating their state taxes, filers in most states must use one of the federal definitions of income, which already capture the effects of as many as eight federal higher education tax expenditures. Second, many states adopt the federal definition of eligible dependent, which allows parents to claim a personal exemption for each child age 19 to 23—above the standard age cap—who is enrolled in school full time for at least five months of the year. Because of the prevalence of such linkages to federal law, provisions for higher education are fairly common and tend to have similar structures across the states.
- **Several states also have less common higher education tax expenditures.** In many cases, these provisions are unique to one or a handful of states and are independent of federal law. They also sometimes carry substantial costs. New York, for example, allows students and families to choose either a tax credit or deduction for tuition and fees; neither option is based on a linkage to the federal tax code. Together, these credits and deductions resulted in a revenue loss of $240 million in 2013 for the state, accounting for more than half of the revenue loss from the seven provisions for which the state estimated costs that year.

This report explores these findings in greater depth to provide the fullest picture to date of the characteristics and costs of federal and state higher education personal income tax expenditures for students and families. It examines the size of these tax expenditures and their prevalence at the state level, outlines their features, and explains the linkages between state and federal tax codes that generate most of the state-level provisions.

At the federal level, the cost of tax expenditures is similar to that of other major postsecondary programs

The federal government provides a significant share of its support for students and their families through the tax code. In 2014, forgone revenue from federal higher education tax expenditures totaled $34.5 billion, 14 percent more than the cost of the need-based Pell Grant program, the largest federal higher education spending program for that year.[2] (See Figure 1 for federal Pell Grant expenditures and Appendix A for a complete list of tax provisions included in this analysis.)

Forgone revenue from these tax provisions has grown rapidly in recent years, increasing by about 13 times over two decades, from $2.4 billion in 1990 to $34.5 billion in 2014 (adjusted for inflation).[3] (See Figure 2.) To put that in perspective, the number of full-time equivalent (FTE) students grew by just over half over those same 2½ decades.[4] Much of the growth in federal tax expenditures coincides with the creation in 1997 of the Hope scholarship tax credit (effective 1998) and its expansion and renaming to the AOTC in 2009.[5]

Federal and State Government Spending Programs Related to Higher Education

The federal government allocated $75 billion through spending programs related to higher education in academic year 2014 (excluding loans). The largest share of those funds was $30.4 billion in assistance to students based on financial need provided through the Pell Grant program, followed by $25.2 billion for specific research projects and $13 billion in educational aid for veterans. States provided slightly more: $77.7 billion through spending programs that year, including $57.4 billion for general operations of public higher education institutions; $9.9 billion in financial aid grants to students; and $10.4 billion to support research, agricultural, and medical education activities and facilities. (See Figure 1.)

In addition to spending programs and tax expenditures, both levels of government provide student loans, which, unlike grants and tax expenditures, must be paid back with interest. The federal government issued $101 billion in student loans in academic year 2014, while states offered less than half of 1 percent of that amount, $430 million.* All of these figures include funding that flows to public, nonprofit, and for-profit higher education institutions and their students.

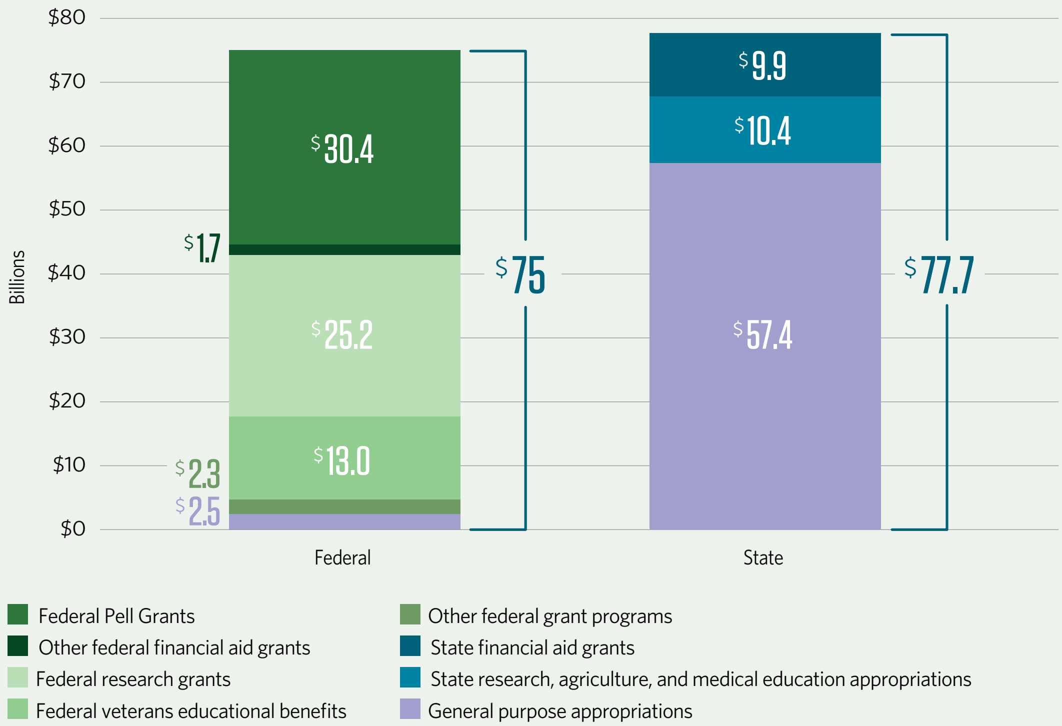
* College Board, Trends in Higher Education, "Student Aid and Nonfederal Loans in Current Dollars Over Time," https://trends.collegeboard.org/student-aid/figures-tables/student-aid-nonfederal-loans-current-dollars-over-time.

Continued on next page.

Figure 1

Federal and State Investments in Higher Education Are Similar in Size, Different in Nature

Spending categories by level of government, academic year 2014



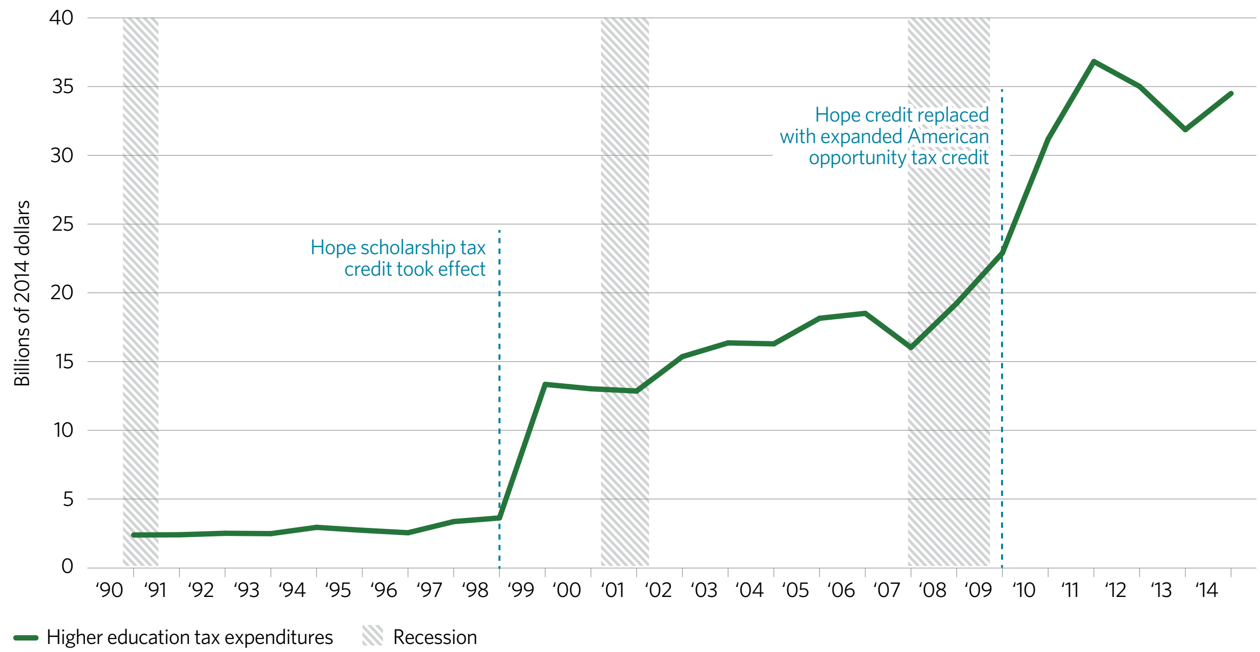
Note: For more information on the underlying methodology for this chart, see The Pew Charitable Trusts, "Federal and State Funding of Higher Education" (June 2015), http://www.pewtrusts.org/~/media/assets/2015/06/federal_state_funding_higher_education_final.pdf.

Sources: Pew's analysis of data from U.S. Department of Education, National Center for Education Statistics' Integrated Postsecondary Education Data System; U.S. Department of Education, FY 2016 Budget Request (2015) and State Funding History Tables (2016); U.S. Department of Veterans Affairs' FY 2016 Budget Submission; National Science Foundation, National Center for Science and Engineering Statistics, "Survey of Federal Funds for Research and Development, FYs 2014-16" (April 2016); State Higher Education Executive Officers Association, "State Higher Education Finance Report: FY2015" (August 2016); and National Association of State Student Grant and Aid Programs, "45th Annual Survey on State-Sponsored Student Financial Aid: 2013-2014 Academic Year"

Figure 2

The Cost of Federal Higher Education Tax Provisions Rose Dramatically Over More Than 2 Decades

Trend in forgone revenue, federal fiscal years 1990-2014, adjusted for inflation



Note: See Appendices A and D for more information on tax expenditures considered in this analysis.

Source: Pew's analysis of data from the U.S. Department of the Treasury as presented in U.S. Office of Management and Budget, "Analytical Perspectives: Budget of the United States Government" (fiscal years 1992-2016), https://www.scribd.com/document_downloads/239368643?extension=pdf&from=embed&source=embed, https://fraser.stlouisfed.org/files/docs/publications/usbanalytical/BUDGET-1995-PER.pdf, https://www.gpo.gov/fdsys/browse/collectionGPO.action?collectionCode=BUDGET

Every state that levies a personal income tax has higher education tax expenditures, and although few states comprehensively estimate the costs, in most that do, the provisions make up a sizable part of the support targeted to students and families

All 41 states and the District of Columbia that levy broad-based personal income taxes provide filers with some type of tax benefit for higher education, but information about the costs of these provisions is limited. Pew was able to obtain cost estimates covering at least two-thirds of the relevant expenditures from only nine states and the District, and in some of those states, the estimates are not produced annually.

A review of the data shows that in eight of the nine states, plus the District, forgone revenue was equivalent to more than 25 percent of the amount provided to students through financial aid grants. (See Table 1 and "Why compare forgone revenue from tax expenditures with financial aid spending?" on Page 7 for more information.)

Table 1

Higher Education Tax Expenditure Costs Exceeded 25% of Financial Aid Spending in Most States With Data

Types of support, various fiscal years

State	Estimated forgone revenue from tax expenditures (in millions)	Financial aid awarded (in millions)	Forgone revenue compared with financial aid grants
California (fiscal 2012)	$443	$1,495	30%
District of Columbia (fiscal 2014)	$9	$32	29%
Georgia (fiscal 2014)	$44	$570	8%
Massachusetts (fiscal 2014)	$121	$91	133%
Minnesota (fiscal 2014)	$51	$182	28%
Missouri (fiscal 2011)	$26	$91	29%
New York (fiscal 2013)	$457	$973	47%
Oregon (fiscal 2014)	$48	$55	87%
Pennsylvania (fiscal 2014)	$167	$459	36%
Wisconsin (fiscal 2014)	$88	$129	68%

Note: See Appendix B for a more detailed breakdown of higher education tax expenditure estimates in each of these states.

Sources: Pew's analysis of data from state tax expenditure reports; direct communication with state personnel; and National Association of State Student Grant and Aid Programs, "Annual Survey Report on State-Sponsored Student Financial Aid" (fiscal 2010-14), Table 6, https://www.nassgap.org/viewrepository.aspx?categoryID=3#

Why compare forgone revenue from tax expenditures with financial aid spending?

At the federal level, comparing higher education personal income tax expenditures with Pell Grant spending is useful not only because of their similar sizes, but also because they provide parallel assistance: Both offset costs for eligible students and their families for education at a range of public and private schools. However, tax expenditures generally benefit households across more income levels than Pell Grants do.[6]

At the state level, using financial aid grants as a benchmark provides a measure of the size of states' higher education tax expenditures. Although financial aid is neither the only nor the largest form of state spending on higher education, it is a useful point of comparison because it is the type of spending most similar to the tax expenditures discussed in this analysis: Both reduce higher education costs for eligible students and their families and, in many instances, can be used for enrollment and/or related costs at public or private institutions. Financial aid makes up 13 percent, on average, of state higher education spending, ranging from nearly 40 percent in South Carolina to zero in New Hampshire in state fiscal year 2014.[7]

The largest component of state higher education spending, by contrast, provides general purpose funding to public colleges and universities. These programs can help reduce costs for students who attend those schools, but because they do not support students directly, they are not included in Table 1. For additional detail on the breakdown of state spending, see "Federal and State Government Spending Programs Related to Higher Education" on Page 4.

The comparison between tax expenditures and financial aid in this analysis provides a frame of reference for how costs contrast across different types of support with similar goals; it does not suggest an ideal level of investment or argue for a certain division of resources among tax expenditures and financial aid programs.

However, the findings do highlight the importance of integrating tax expenditures into debates over higher education finance and policy and suggest that many state policymakers lack important information they need to fully understand their states' support for higher education. More complete estimates of the value of state higher education tax expenditures could allow them to better include those provisions in broader discussions of higher education financing policy.

Federal and state tax expenditures target 3 phases of higher education financing

Whereas financial aid grants traditionally help reduce the costs students incur while enrolled in a postsecondary education program, tax expenditures at both the federal and state levels are intended to offset students' and families' costs associated with three phases of the process of paying for college: saving for future costs, paying costs while enrolled, and paying off loans.[8]

Federal provisions

Saving for future costs

At the federal level, most of the forgone revenue associated with tax expenditures for future costs results from the provisions related to qualified tuition programs, commonly known as 529 plans, which are designed to encourage people to save and invest for future higher education expenses. Contributions to 529 plans are allowed to grow and can be withdrawn tax-free if used for qualified higher education expenses on behalf of a designated beneficiary. The exclusion of investment earnings from 529 plans, along with two smaller provisions for higher education savings,[9] constituted about 6 percent, or $1.9 billion, of the total cost of federal higher education tax expenditures.

Paying for current-year expenses

Provisions that help reduce an enrolled student's costs constituted 89 percent (nearly $31 billion) of the total cost of higher education tax expenditures in fiscal 2014. The revenue loss largely comes from four provisions, which offset costs for students and their families in different ways:

- The **AOTC** is by far the largest federal higher education tax expenditure, more than four times the size of the next-largest provision in terms of forgone revenue, at $20 billion in fiscal 2014. It provides up to $2,500 per student annually to help cover undergraduate tuition and other educational expenses during the first four of years of postsecondary education.[10] (See Figure 3.)
- The **lifetime learning credit** provides up to $2,000 per tax return to offset tuition and educational expenses for students taking classes that enhance job skills, regardless of how many years of schooling they have had.

- The **parental personal exemption for dependent students** allows parents to claim 19- to 23-year-old children as dependents—which exceeds the standard age cap of 18 for a nonstudent dependent—if they are enrolled full time in school, reducing the taxable income of many families supporting children in higher education.
- The **exclusion of qualified scholarships, fellowship grants, and tuition reductions** exempts from taxation certain awards that assist students in paying for their education.

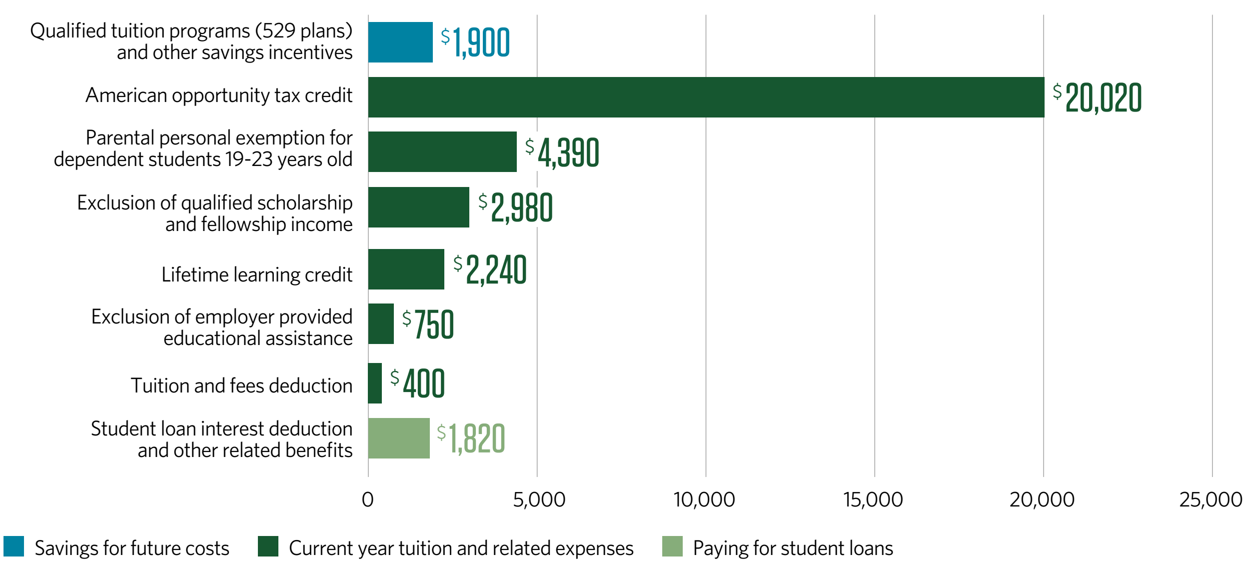
Repaying student loans

The federal tax provisions that target paying off previously incurred loans include a deduction for up to $2,500 in interest annually. Additionally, under certain conditions, the federal government does not tax student debt that has been forgiven. By contrast, most other canceled debt is taxable.[11] The forgone revenue from this category is similar to that from provisions aimed at saving for future college costs, at about $1.8 billion in 2014. See Figure 3 for estimates of each federal tax expenditure, and Appendix A for a descriptive list of federal higher education tax provisions and associated costs.

Figure 3

Among Federal Tax Provisions for Higher Education, Those for Current Expenses Cost the Most

Forgone revenue (millions of dollars) by college cost phase, FY 2014



Source: Pew's analysis of data from the U.S. Department of the Treasury as presented in U.S. Office of Management and Budget, "Analytical Perspectives (Fiscal Year 2016)," https://www.gpo.gov/fdsys/pkg/BUDGET-2016-PER/pdf/BUDGET-2016-PER.pdf

State provisions

State higher education tax provisions support the same three phases in the process of paying for postsecondary schooling. For example:

- **Saving for future costs.** All 41 states plus the District that levy personal income taxes follow the federal exclusion of 529 plan earnings, and 33 states and the District offer an additional deduction or credit for contributions to these plans. (See "Provisions for 529 Plan Contributions Vary by State" on Page 14 for more details.)
- **Paying current-year tuition and expenses.** Thirty-eight states and the District allow filers to claim an exemption for dependents age 19 to 23—above the standard age cap—if they are full-time students.
- **Repaying student loans.** Thirty-seven states and the District allow the federal deduction of student loan interest, with the same general parameters as the federal tax code.

States have implemented most of their higher education tax provisions through 2 key linkages to the federal tax code

The most commonly offered higher education tax provisions at the state level result from linkage to the federal tax code in two main ways.

First, most states use one of the federal definitions of income, which capture several federal higher education provisions, as the starting point for their tax calculations. These federal exclusions and adjustments are applied to gross income and so are reflected in both federal adjusted gross and taxable income.[12] (See Appendix A for more information on these provisions.)

Exclusions:

- Qualified scholarships, fellowships, and tuition reductions.
- Investment earnings from qualified tuition programs (529 plans).
- Employer-provided educational assistance.
- Qualified canceled student loans.
- Investment income from Coverdell Education Savings Accounts.

Deductions:

- Interest paid on student loans.
- Qualified tuition and fees.
- Parental personal exemption for dependent students age 19 to 23 (passed on through federal taxable income only).

States that use one of the federal definitions of income conform to these tax expenditures unless they selectively disallow or modify them. For example, at least eight states that link to the federal definition of adjusted gross income actively disallow at least one of the federal provisions listed above. However, many states allow all the provisions; more than half of the states that link to a federal definition of income permit all seven of the provisions incorporated within federal adjusted gross income without any modifications.

Second, the 38 states plus the District that allow filers to claim a dependent exemption for full-time students age 19 to 23 do so either by adopting the federal definition of dependents, which includes the special rule for students, or by starting their calculations with federal taxable income. Table 2 offers a state-by-state look at the most common state-level higher education income tax expenditures and indicates whether each benefit is provided by linking to the federal tax code.

Federal changes could affect states

The links between federal and state tax codes mean that changes to federal tax provisions could affect those provided at the state level, requiring states to decide whether to adopt the federal revisions into their own tax codes. In addition, understanding how and to what extent federal modifications could affect states provides important context for federal policymakers as they evaluate tax proposals.

Table 2

Most States Link to Federal Higher Education Tax Expenditures

Provisions by state, 2014

State	Deductions		Exclusions					Parental personal exemption for dependent students age 19–23
	Student loan interest	Tuition and fees	Qualified scholarships, fellowship grants, and tuition reductions	Earnings in qualified tuition programs (529 plans)	Employer-provided educational assistance	Earnings in Coverdell Education Savings Account	Qualifying cancelled student loans	
Alabama*				×		×		
Alaska	*No personal income tax*							
Arizona	×	×	×	×	×	×	×	×
Arkansas	×		×	×	×	×	×	×
California	×		×	×	×	×	×	×
Colorado	×	×	×	×	×	×	×	×
Connecticut	×	×	×	×	×	×	×	
Delaware	×	×	×	×	×	×	×	×
District of Columbia	×	×	×	×	×	×	×	×
Florida	*No personal income tax*							
Georgia	×	×	×	×	×	×	×	×
Hawaii	×		×	×	×	×	×	×
Idaho	×	×	×	×	×	×	×	×
Illinois	×	×	×	×	×	×	×	×
Indiana	×	×	×	×	×	×	×	×

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State	Deductions		Exclusions					Parental personal exemption for dependent students age 19–23
	Student loan interest	Tuition and fees	Qualified scholarships, fellowship grants, and tuition reductions	Earnings in qualified tuition programs (529 plans)	Employer-provided educational assistance	Earnings in Coverdell Education Savings Account	Qualifying cancelled student loans	
Iowa[†]	X	X	X	X	X	X	X	X
Kansas	X	X	X	X	X	X	X	X
Kentucky	X	X	X	X	X	X	X	X
Louisiana	X	X	X	X	X	X	X	X
Maine[‡]	X		X	X	X	X	X	X
Maryland	X		X	X	X	X	X	X
Massachusetts	X		X	X	X	X	X	X
Michigan	X	X	X	X	X	X	X	X
Minnesota	X	X	X	X	X	X	X	X
Mississippi			X	X	X	X		X
Missouri	X	X	X	X	X	X	X	X
Montana	X	X	X	X	X	X	X	X
Nebraska	X	X	X	X	X	X	X	X
Nevada	*No personal income tax*							
New Hampshire[§]				X				
New Jersey			X	X		X	X	X
New Mexico	X	X	X	X	X	X	X	X
New York	X	X	X	X	X	X	X	X
North Carolina	X		X	X	X	X	X	
North Dakota	X	X	X	X	X	X	X	X
Ohio	X	X	X	X	X	X	X	X
Oklahoma	X	X	X	X	X	X	X	X

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State	Deductions		Exclusions					Parental personal exemption for dependent students age 19-23
	Student loan interest	Tuition and fees	Qualified scholarships, fellowship grants, and tuition reductions	Earnings in qualified tuition programs (529 plans)	Employer-provided educational assistance	Earnings in Coverdell Education Savings Account	Qualifying cancelled student loans	
Oregon	X	X	X	X	X	X	X	X
Pennsylvania[‖]			X	X				X
Rhode Island	X	X	X	X	X	X	X	X
South Carolina	X	X	X	X	X	X	X	X
South Dakota	*No personal income tax*							
Tennessee[§]				X		X		
Texas	*No personal income tax*							
Utah	X	X	X	X	X	X	X	X
Vermont	X	X	X	X	X	X	X	X
Virginia	X	X	X	X	X	X	X	X
Washington	*No personal income tax*							
West Virginia	X	X	X	X	X	X	X	X
Wisconsin	X		X	X	X	X	X	X
Wyoming	*No personal income tax*							

Offered through a link to federal taxable income
Offered through a link to federal adjusted gross income
Offered through a link to federal definition of dependents

* Alabama's standard rules for dependent exemptions allow a filer to claim as a dependent an individual of any age who satisfies established support and family-relation criteria. Although this provision can include students, it is not specific to students and so was not considered a higher education provision for purposes of this study.

† Iowa has its own definition of adjusted gross income, but it closely mirrors federal AGI.

‡ In 2016, Maine began linking to the federal deduction for tuition and fees.

§ State personal income tax applies to interest and dividends only.

‖ Pennsylvania does not allow a deduction from income for personal exemptions but does permit a tax forgiveness credit for low-income taxpayers that accounts for a filer's dependents, and full-time students over 18 may qualify if claimed as dependents on taxpayers' federal returns.

Provisions for 529 Plan Contributions Vary by State

There are two types of 529 plans: savings and prepaid. Savings plans allow people to make contributions to an investment account to help pay the future higher education expenses of a designated beneficiary. Prepaid plans allow contributors to pay part or all of the cost of tuition ahead of time, potentially shielding beneficiaries from rising tuition costs.*

Nearly every state, plus the District, sponsors at least one type of 529 plan, and those with an income tax generally follow the federal policy of exempting plan earnings from tax.† In addition, 33 of those states and the District offered deductions or credits for contributions to 529 plans in 2014, but the characteristics of those provisions varied widely. (See Table 3.)

In the case of deductions, the value is usually capped at a particular dollar amount, ranging from $250 in Maine to $14,000 in Pennsylvania for single filers.‡ Six states—Colorado, Michigan, New Mexico, South Carolina, Virginia, and West Virginia—offer deductions without explicit maximums in certain cases.§ In Michigan, the unlimited deduction is available only for the state's prepaid plan, while Virginia's deduction for plan contributions is capped at $4,000, except when the filer is 70 or older, in which case it is unlimited. Three states—Indiana, Utah, and Vermont—offer credits instead of deductions with values for single filers ranging from $93 in Utah to $1,000 in Indiana.

* This report uses the terms "529 plan" and "qualified tuition plan" interchangeably to refer to both savings and prepaid plans.

† Most states offer at least one savings plan, and at least six states have prepaid plans that were still accepting new enrollments in 2014. Consumers generally are able to purchase plans regardless of their state of residence. For a current list of 529 plans, see Savingforcollege.com, "Compare 529 Plans," http://www.savingforcollege.com/compare_529_plans/.

‡ Maine's deduction for contributions to 529 plans was repealed beginning in the 2016 tax year.

§ Even in cases where state law does not explicitly limit deductions, they are constrained by federal law, which requires 529 plans to prevent contributions "in excess of those necessary to provide for the qualified higher education expenses of the beneficiary." To satisfy this mandate, 529 plans generally accept contributions only until the combined balances, including earnings, for a given beneficiary reach a threshold determined by the state. See U.S. Code Title 26 (Internal Revenue Code), Subtitle A, Chapter 1, Subchapter F, Part VIII, Section 529.

Continued on next page.

Table 3

33 States and the District Offer Deductions or Credits for 529 Plan Contributions

Maximum values, by state, 2014

State	Maximum deduction for a single filer	Maximum credit for a single filer
Alabama	$5,000	
Arizona	$2,000	
Arkansas	$5,000	
Colorado	Unlimited	
Connecticut	$5,000	
Georgia	$2,000	
Idaho	$4,000	
Illinois	$10,000	
Indiana		$1,000 nonrefundable
Iowa	$3,098	
Kansas	$3,000	
Louisiana	$2,400	
Maine*	$250	
Maryland	$2,500	
Michigan†	$5,000 for 529 savings only	
Mississippi	$10,000	
Missouri	$8,000	
Montana	$3,000	
Nebraska	$10,000	
New Mexico	Unlimited	
New York	$5,000	
North Dakota	$5,000	
Ohio	$2,000	

Continued on next page.

State	Maximum deduction for a single filer	Maximum credit for a single filer
Oklahoma	$10,000	
Oregon	$2,265	
Pennsylvania	$14,000	
Rhode Island	$500	
South Carolina	Unlimited	
Utah		$93 nonrefundable
Vermont		$250 nonrefundable
Virginia‡	$4,000	
West Virginia	Unlimited	
Wisconsin	$3,050	
District of Columbia	$4,000	

Note: Some details are omitted for brevity. For example, many states allow a larger deduction or credit for married joint filers, and some states do not allow a deduction for contributions to out-of-state plans.

* The state's deduction was repealed as of tax year 2016.

† Filers may deduct the full price of a Michigan Education Trust prepaid tuition plan.

‡ Contributors who are 70 or older are not subject to the deduction limit of $4,000 per prepaid tuition contract or college savings trust account and may instead deduct the full amount paid or contributed, less any amounts previously deducted.

Source: Pew review of state tax forms, instructions, codes, and tax expenditure reports, as well as correspondence with state officials. See Appendix D for further explanation.

Several states also have less common provisions

Although the vast majority of state higher education tax expenditures are common across the states because of their links to the federal tax code, several states have their own distinct provisions, which in some cases carry substantial costs:

- New York allows students and families to choose either a tax credit or deduction for tuition and fees. Neither option is based on a linkage to the federal tax code. Together, these credits and deductions resulted in an estimated revenue loss of $240 million in 2013 for the state, accounting for more than half of the revenue loss from the seven provisions for which the state estimated costs that year. (See Appendices B and C for more details.)

- Kentucky offers its own versions of the AOTC and lifetime learning credit that are linked to the federal credits. Filers who qualify for the federal benefits can also take a state credit equal to 25 percent of the federal provisions.
- Maine offers a tax credit to offset student loan payments for residents who receive an associate or bachelor's degree from a Maine institution and subsequently live and work in the state.[13]
- Ohio and Oregon allow students to deduct certain scholarship and fellowship funds used to pay for housing (Oregon) and room and board (Ohio). These provisions expand on the federal tax exclusion, which both states also offer but which applies only to scholarship and fellowship income that is used for certain tuition and course-related expenses.
- South Carolina provides a tuition tax credit for students who attend an eligible in-state institution within 12 months of graduating from a high school in the state. The credit is up to $850 for a four-year college or university or $350 for a two-year institution.

Some states offer provisions that closely parallel federal tax expenditures but with noteworthy differences. For example, Massachusetts allows taxpayers to deduct tuition payments—minus any grants, scholarships, and financial aid—that exceed 25 percent of a filer's state adjusted gross income, rather than using the federal dollar-value maximum of $4,000. Wisconsin offers a deduction of up to $6,940 per student for tuition and mandatory fees paid to qualifying Wisconsin and Minnesota postsecondary schools. (See Appendix C for more information.)

Conclusion

To make fully informed policy choices, state and federal leaders need a clear picture of how spending programs and tax expenditures work together to deliver the billions of dollars in support that both levels of government provide to higher education students and institutions, and how those forms of support affect budgets.

At the federal level, the forgone revenue from higher education tax expenditures has grown rapidly in recent years and is now comparable in cost to the largest postsecondary spending programs. At the same time, every state with a broad-based income tax provides at least some provisions intended to help students and their families offset the costs of higher education, but only a handful of these states compile comprehensive information on the forgone revenue from those tax expenditures. The available estimates show that the provisions represent a sizable share of the support those states direct to students and families.

Many state policymakers do not have the information they need to fully understand their states' support for higher education. To begin to solve this problem, these states should consider assessing the costs of their higher education tax expenditures.

In addition, more effective integration of these tax provisions into deliberations about how to support higher education at the state and federal levels—looking at spending and tax provisions together as a single government investment—will require a concerted effort to coordinate spending and tax policy. This, in turn, would necessitate increased collaboration across legislative committees.

Taking these steps would help policymakers answer key questions, such as whether overall support for higher education is structured to maximize its impact or set at appropriate levels, so they can more effectively marshal the full spectrum of assistance toward achieving key policy goals.

Appendix A: U.S. Treasury tax expenditure descriptions

This report adopts the U.S. Treasury Department's framework for defining a federal tax expenditure. Treasury lists and describes the provisions in the president's annual budget. The fiscal 2016 budget—the most recent to contain tax expenditure estimates for fiscal 2014—includes 11 active higher education income tax expenditures. (See Table A.1 and Appendix D for more information.)

Table A.1

Federal Higher Education Income Tax Expenditures

Federal tax expenditure	Explanation	Income phaseout range for tax year 2014* (in thousands)	Expiration	Estimate of forgone revenue, FY 2014 (in millions)
For saving for future college costs				
Exclusion of earnings in qualified tuition programs (529 plans) **Internal Revenue Code § 529**	Investment earnings in qualified tuition programs, known as 529 plans, can accumulate tax-free and distributions are tax-free if used for qualified education expenses. Contributions are not tax deductible at the federal level.	None	None	$1,820
Exclusion of earnings in Coverdell Education Savings Accounts **IRC § 530**	Coverdell accounts are savings vehicles designed to pay qualified education expenses for K-12 and higher education for a designated beneficiary. Investment earnings accumulate tax-free and distributions are tax-free if used for qualified education expenses. Contributions are not tax deductible at the federal level. Annual contributions are limited to $2,000 per beneficiary. Coverdell accounts were formerly known as education individual retirement accounts.	$95-$110; $190-$220 (married joint)	None	$60
Exclusion of interest on savings bonds redeemed to finance educational expenses **IRC § 135**	Interest earned on qualified U.S. Series EE savings bonds issued after 1989 is excluded from gross income if the proceeds from the redemption are used to pay for qualified higher education tuition and related expenses for the taxpayer, a spouse, or an eligible dependent.	$76-$91; $113.95-$143.95 (married joint)	None	$20
For current-year tuition and related expenses				
American opportunity tax credit **IRC § 25A (i)**	A credit for current-year qualified tuition and related expenses during the first four years of postsecondary education. The credit is 100 percent of the first $2,000 of expenses, plus 25 percent of the next $2,000, for a maximum total of $2,500 per student. Forty percent, or $1,000, of the credit is refundable.	$80-$90; $160-$180 (married joint)	None	Nonrefundable portion: $15,710 Refundable portion: $4,310

Continued on next page.

Federal tax expenditure	Explanation	Income phaseout range for tax year 2014* (in thousands)	Expiration	Estimate of forgone revenue, FY 2014 (in millions)
Lifetime learning credit **IRC § 25A (c)**	A nonrefundable credit available for an unlimited number of years for taxpayers taking at least one postsecondary education course that enhances job skills. The value of the credit is 20 percent of the first $10,000 paid toward qualifying tuition and fees, for a maximum of $2,000 annually per tax return.	$54-$64; $108-$128 (married joint)	None	$2,240
Tuition and fees deduction **IRC § 222**	A deduction from gross income up to $4,000 for qualified tuition and related expenses, such as enrollment fees. The maximum deduction is reduced to $2,000 for filers with income within the phaseout range and is disallowed above that range.	$65-$80; $130-$160 (married joint)	Dec. 31, 2016†	$400
Exclusion of qualified scholarships, fellowship grants, and tuition reductions **IRC § 117**	Income received in the form of a scholarship or fellowship grant is excluded from gross income if it is used for qualified tuition and related expenses. Amounts used for room and board are taxable. Tuition reductions for employees of educational institutions and their families also are not included in gross income. In most cases, scholarships that are payment for services are taxable.	None	None	$2,980
Exclusion of employer-provided educational assistance **IRC § 127**	Employer-provided educational assistance benefits are excluded from employee's gross income. Up to $5,250 per taxpayer is permitted.	None	None	$750
Parental personal exemption for dependent students 19-23 years old **IRC § 151 and 152**	In general, to be considered a dependent, a child must be under age 19. However, a dependent exemption is allowed for a child age 19 to 23 who is enrolled as a full-time student at a qualifying institution for at least five months of the tax year.‡	None	None	$4,390
For student loans				
Student loan interest deduction **IRC § 221**	A deduction from gross income of up to $2,500 for interest paid on an education loan incurred exclusively to pay qualified higher education expenses.	$65-$80; $130-$160 (married joint)	None	$1,730

Continued on next page.

Federal tax expenditure	Explanation	Income phaseout range for tax year 2014* (in thousands)	Expiration	Estimate of forgone revenue, FY 2014 (in millions)
Exclusion of qualifying canceled student loans **IRC § 108(f)**	Exclusion from gross income of any amount resulting from the discharge of a higher education loan if the debt was discharged after an individual worked for a set period of time in certain professions for any of a broad class of employers. The exclusion also applies to the repayment of student loans by third parties under either the National Health Service Corps loan-repayment program or some state programs geared toward health care professionals working in underserved areas.	None	None	$90

Notes: For more background on these provisions, see Congressional Research Service, "Higher Education Tax Benefits: Brief Overview and Budgetary Effects" (Feb. 1, 2016), https://fas.org/sgp/crs/misc/R41967.pdf; and Committee on the Budget, United States Senate, "Tax Expenditures: Compendium of Background Material on Individual Provisions" (December 2014), https://www.gpo.gov/fdsys/pkg/CPRT-113SPRT91950/pdf/CPRT-113SPRT91950.pdf. Treasury uses two concepts to determine which tax provisions would constitute tax expenditures. For more information, see U.S. Office of Management and Budget, "Analytical Perspectives: Budget of the United States Government (Fiscal Year 2016)." A taxpayer cannot claim more than one benefit for the same higher education expense. Generally, only one person—the student or the parent—may claim a given expense. A parent may claim a student's relevant expenses if the parent also claimed the student as a dependent. Eligible expenses must be incurred at a college, university, vocational school, or other postsecondary institution that is qualified to participate in a student aid program run by the U.S. Department of Education. Generally, such institutions are accredited public, nonprofit, and private for-profit postsecondary institutions. This table differs from the Treasury's tax expenditure report with respect to the status of two provisions because of law changes that occurred after the release of Treasury's report: The AOTC was made permanent in 2015, and the tuition and fees deduction was extended through 2016. (Treasury's report stated that the AOTC was set to expire at the end of 2017 and that the deduction had expired at the end of 2013.)

* The first income phaseout range applies to all filing statuses other than married filing jointly.

† This deduction is part of a package of temporary provisions that have historically been renewed for one or two years at a time. At the time of publication, this provision had expired.

‡ This provision interacts with other portions of the tax system in ways that can reduce tax liability but are not discussed in this analysis. For instance, the expansion of the dependent definition allows some filers to file as head of household who would otherwise have to use the single status. However, Treasury considers the benefit of the different filing status to be part of standard tax law, not a tax expenditure. Similarly, the ability to claim these students as dependents increases some filers' earned income tax credit, but Treasury does not estimate this separately from the overall credit.

Source: Forgone revenue estimates are from U.S. Office of Management and Budget, "Analytical Perspectives, Budget of the United States Government (Fiscal Year 2016)"

Appendix B: State estimates of forgone revenue from higher education tax expenditures

Table B.1

California

Tax expenditure	Forgone FY 2012 revenue (in millions)	Percentage of total higher education tax expenditures estimated
Parental personal exemption for dependent students 19-23 years old*	$190	43%
Exclusion of qualified scholarships, fellowship grants, and tuition reductions*	$100	23%
Exclusion of employer-provided educational assistance*	$55	12%
Student loan interest deduction*	$55	12%
Exclusion of earnings in qualified tuition programs (529 plans)*	$31	7%
Exclusion of qualifying canceled student loans*	$8	2%
Exclusion of earnings in Coverdell Education Savings Accounts*	$3	1%
Total	$443	100%

* Linked to the federal provision.

Notes: The state starts its calculation of income from federal adjusted gross income. Numbers may not add up because of rounding.

Sources: Pew's analysis of "California Income Tax Expenditures: Compendium of Individual Provisions, Report for 2012 Tax Year Data"; and Allen Prohofsky, Economic and Statistical Research Bureau under the California Franchise Tax Board, email messages to Pew staff, February 2016

Table B.2

District of Columbia

Tax expenditure	Forgone FY 2014 revenue (in millions)	Percentage of total higher education tax expenditures estimated
Exclusion of qualified scholarships, fellowship grants, and tuition reductions*	$3.5	38%
Student loan interest deduction*	$1.7	18%
Exclusion of earnings in qualified tuition programs (529 plans)*	$1.1	12%
Exclusion of employer-provided educational assistance*	$1.1	12%
Deduction for 529 savings plan contributions	$1.1	12%
Tuition and fees deduction*	$0.3	3%
Exclusion of qualifying canceled student loans*	$0.2	3%
Exclusion of earnings in Coverdell Education Savings Accounts*	$0.1	1%
Deduction for public school teacher expenses	$0.1	1%
Exclusion of loan repayment under the DC Health Professional Recruitment Program for health professionals working in designated underserved areas	$0.1	1%
Parental personal exemption for dependent students 19-23 years old*	No estimate	N/A
Total	$9.2	100%

* Linked to the federal provision.

Notes: The District starts its calculation of income from federal adjusted gross income. Numbers may not add up because of rounding.

Source: "District of Columbia Tax Expenditure Report," May 2014

Table B.3

Georgia

Tax expenditure	Forgone FY 2014 revenue (in millions)	Percentage of total higher education tax expenditures estimated
Exclusion of scholarship and fellowship income*	$14	32%
Student loan interest deduction*	$9	20%
Exclusion of employer-provided educational assistance and tuition reductions for employees of educational institutions*	$8	18%
Exclusion of earnings in qualified tuition programs (529 plans)*	$5	11%
Deduction for contributions to state 529 plan	$4	9%
Tuition and fees deduction*	$3	7%
Exclusion of qualifying canceled student loans*	$1	2%
Exclusion for earnings in Coverdell Education Savings Accounts and interest on educational savings bonds*†	Less than $1 million	N/A
Parental personal exemption for dependent students 19-23 years old*	No estimate	N/A
Total	$44	100%

Note: The state starts its calculation of income from federal adjusted gross income. Numbers may not add up because of rounding.

* Linked to the federal provision.

† Although the exclusion of interest from U.S. savings bonds redeemed to pay higher education expenses was not considered to be a state tax expenditure in this analysis, Georgia combines this provision and the exclusion of earnings on Coverdell Education Savings Accounts into a single estimate. See Appendix D for more information on education savings bonds.

Source: Pew's analysis of data from the Georgia Tax Expenditure Report for Fiscal Year 2014, Fiscal Research Center of the Andrew Young School of Policy Studies, Georgia State University, December 2012

Table B.4

Massachusetts

Tax expenditure	Forgone FY 2014 revenue (in millions)	Percentage of total higher education tax expenditures estimated
Tuition deduction	$45.5	37%
Student loan interest deduction *†	$30.9	25%
Exclusion of qualified scholarships, fellowship grants, and tuition reductions*	$20.1	17%
Exclusion of employer-provided educational assistance*	$11.6	10%
Parental personal exemption for dependent students age 19 or over*	$9.0	7%
Exclusion of earnings in qualified tuition programs (529 plans)*	$4.3	4%
Exclusion of earnings in Coverdell Education Savings Accounts*	No estimate	N/A
Exclusion of qualifying canceled student loans*	No estimate	N/A
Total	$121.4	100%

* Linked to the federal provision.

† This estimate includes forgone revenue from Massachusetts' additional nonfederal deduction for undergraduate loan interest. See Appendix C for more information on this provision.

Notes: The state starts its calculation of income from federal adjusted gross income. Numbers may not add up because of rounding.

Source: Pew's analysis of data from the Massachusetts Tax Expenditure Budget for Fiscal Year 2017, Executive Office for Administration and Finance, Commonwealth of Massachusetts, January 2016

Table B.5

Minnesota

Tax expenditure	Forgone FY 2014 revenue (in millions)	Percentage of total higher education tax expenditures estimated
Exclusion of qualified scholarships, fellowship grants, and tuition reductions*	$25.6	51%
Student loan interest deduction*	$10.2	20%
Exclusion of earnings in qualified tuition programs (529 plans)*	$6.9	14%
Tuition and fees deduction*	$5.6	11%
Exclusion of qualifying canceled student loans*	$1.5	3%
Exclusion of earnings in Coverdell Education Savings Accounts*	$0.6	1%
Deduction of AmeriCorps postservice education award	$0.2	0.4%
Exclusion of employer-provided educational assistance*	No estimate	N/A
Parental personal exemption for dependent students 19-23 years old*	No estimate	N/A
Total	$50.6	100%

* Linked to the federal provision.

Notes: The state starts its calculation of income from federal taxable income. Numbers may not add up because of rounding.

Sources: Pew's analysis of data from "Minnesota Tax Expenditure Budget, Fiscal Years 2014-2017"; and Minnesota Department of Revenue, Tax Research Division, email exchanges with Pew staff, February 2016

Table B.6
Missouri

Tax expenditure	Forgone FY 2011 revenue (in millions)	Percentage of total higher education tax expenditures estimated
Exclusion of qualified scholarships and fellowship grants*	$9.2	35%
Parental personal exemption for dependent students 19-23 years old*	$7.8	30%
Exclusion of earnings in qualified tuition programs (529 plans)*	$5.5	21%
Student loan interest deduction*	$2.3	9%
Exclusion of earnings in Coverdell Education Savings Accounts*	$1.5	6%
Exclusion of qualifying canceled student loans*	$0.1	0%
Tuition and fees deduction*	No estimate	N/A
Exclusion of employer-provided educational assistance*	No estimate	N/A
Deduction for 529 savings plan contributions	No estimate	N/A
Total	$26.4	100%

* Linked to the federal provision.

Notes: The state starts its calculation of income from federal adjusted gross income. Numbers may not add up because of rounding. At the time of the publication of Missouri's tax expenditure report, the tuition and fees deduction and the exclusion of employer-provided educational assistance were scheduled to sunset, so the state did not project revenue for those two provisions for 2011.

Source: Pew's analysis of data from the University of Missouri, Columbia's "Tax Expenditure Report: January 2009"

Table B.7

New York

Tax expenditure	Forgone FY 2013 revenue (millions)	Percentage of total higher education tax expenditures estimated
College tuition credit/deduction	$240.3	53%
Exclusion of qualified scholarships, fellowship grants, and tuition reductions*	$63	14%
Deduction for 529 savings plan contributions	$61.3	13%
Exclusion of earnings in qualified tuition programs (529 plans)*	$38	8%
Student loan interest deduction*	$37	8%
Exclusion of employer-provided educational assistance*	$16	4%
Exclusion of earnings in Coverdell Education Savings Accounts*	$1.3	0.3%
Tuition and fees deduction*	No estimate	N/A
Exclusion of qualifying canceled student loans*	No estimate	N/A
Parental personal exemption for dependent students 19-23 years old*	No estimate	N/A
Total	$456.9	100%

* Linked to the federal provision.

Notes: The state starts its calculation of income from federal adjusted gross income. Numbers may not add up because of rounding.

Source: Pew's analysis of data from "Annual Report on New York State Tax Expenditures"

Table B.8

Oregon

Tax expenditure	Forgone FY 2014 revenue (in millions)	Percentage of total higher education tax expenditures estimated
Student loan interest deduction*	$14.5	30%
Exclusion of qualified scholarships, fellowship grants, and tuition reductions*	$11.8	24%
Deduction for 529 savings plan contributions	$8.9	18%

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Tax expenditure	Forgone FY 2014 revenue (in millions)	Percentage of total higher education tax expenditures estimated
Exclusion of employer-provided educational assistance*	$5.1	11%
Tuition and fees deduction*	$3.3	7%
Exclusion of earnings in qualified tuition programs (529 plans) and Coverdell Education Savings Accounts*	$3.3	7%
Exclusion of qualifying canceled student loans*	$0.8	2%
Deduction for scholarship awards used for housing expenses	$0.6	1%
Parental personal exemption for dependent students 19-23 years old*	No estimate	N/A
Total	$48.3	100%

* Linked to the federal provision.

Notes: The state starts its calculation of income from federal taxable income. Numbers may not add up because of rounding.

Sources: Pew's analysis of data from the State of Oregon "Tax Expenditure Report, 2013-15"; Jonathan Hart, Oregon Department of Revenue, email exchanges with Pew staff, August 2015 and February 2016

Table B.9
Pennsylvania

Tax expenditure	Forgone FY 2014 revenue (in millions)	Percentage of total higher education tax expenditures estimated
Exclusion of qualified scholarships, grants, fellowships, and stipends	$141.8	85%
Exclusion of income earned in qualified tuition programs (529 plans), and deduction for contributions	$25.6	15%
Parental personal exemption for dependent students 19-23 years old*	No estimate	N/A
Total	$167.4	100%

* Linked to the federal provision.

Notes: The state does not start its calculation from a federal income definition. Numbers may not add up because of rounding.

Source: Pew's analysis of "Pennsylvania 2016-2017 Pennsylvania Executive Budget"

Table B.10
Wisconsin

Tax expenditure	Forgone FY 2014 revenue (in millions)	Percentage of total higher education tax expenditures estimated
Deduction for higher education tuition expenses	$23.6	27%
Exclusion of qualified scholarships, fellowship grants, and tuition reductions*	$18.9	22%
Student loan interest deduction*	$17.1	19%
Deduction for 529 savings plan contributions	$11.4	13%
Exclusion of earnings in qualified tuition programs (529 plans)*	$11.1	13%
Exclusion of employer-provided educational assistance*	$4.7	5%
Exclusion of qualifying canceled student loans*	$0.6	1%
Exclusion of earnings in Coverdell Education Savings Accounts*	$0.5	1%
Parental personal exemption for dependent students 19-23 years old*	No estimate	N/A
Total	$87.9	100%

* Linked to the federal provision.

Notes: The state starts its calculation of income from federal adjusted gross income. Numbers may not add up because of rounding.

Sources: Pew's analysis of "State of Wisconsin Summary of Tax Expenditure Devices, February 2015"; Michael Wagner, Wisconsin Department of Revenue, email exchanges with Pew staff, December 2016

Appendix C: Less common state provisions

Although the vast majority of state-level higher education tax expenditures are common across the states because of their links to the federal tax code, several states offer some additional provisions that are unique to that state or a small number of states.[14]

Table C.1

Tax Expenditures Offered by a Small Number of States

Benefit type	Description	States
Tuition and fees deduction that is different from the federal provision	These state provisions are similar but not linked to the federal tuition and fees deduction. Arkansas offers an itemized tuition and fees deduction of up to 50 percent of tuition paid by the filer or the weighted average of tuition at postsecondary institutions, whichever is less. Massachusetts allows a deduction for tuition and fees in excess of 25 percent of the filer's state adjusted gross income. New York provides a tuition and fees deduction that is separate from the federal benefit and equal to the amount of qualified college tuition expenses paid, up to a maximum of $10,000 per undergraduate student. The filer must itemize deductions to claim this benefit and cannot also take the state's college tuition credit. (See "Postsecondary education tuition credits" below.) Wisconsin offers a deduction of up to $6,940 per student for tuition and mandatory fees paid to certain Wisconsin and Minnesota postsecondary institutions. The maximum deduction is adjusted annually to equal twice the average cost of undergraduate tuition in the University of Wisconsin system for the most recent fall semester.	Arkansas, Massachusetts, New York, Wisconsin
Deduction for earnings from family education account (not recognized as a 529 plan or Coverdell account)	Rhode Island allows a deduction of earnings from a Rhode Island Family Education Account, which is distinct from a Coverdell account or 529 plan. Taxpayers who set up family education accounts under section 44-30-25 of the state's General Laws at a qualified depository are allowed to reduce their state adjusted gross income by the amount earned in the account.	Rhode Island
Postsecondary education tuition credits	Kentucky offers its own versions of the AOTC and lifetime learning credit that are linked to the federal credits. Filers who qualify for the federal benefits can also take a state credit equal to 25 percent of the federal provisions. New York offers a college tuition credit of up to $400 per undergraduate student for state residents. South Carolina allows a tuition credit for students who attended an eligible four-year public, four-year independent, or two-year college in the state within 12 months of graduating from a high school in the state. The credit limit is $850 for a four-year college or university or $350 for a two-year institution.	Kentucky, New York, South Carolina

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Benefit type	Description	States
Deduction or exclusion of scholarships used for housing expenses	A taxpayer is allowed to subtract from taxable income scholarship and fellowship dollars used to pay for housing expenses while attending classes full time at a qualifying institution. This benefit expands upon the federal exclusion of scholarship, grant, and fellowship dollars used for qualified tuition and related expenses, which does not include room and board. Ohio permits this deduction for the federally taxable portion of Pell and Ohio College Opportunity grants used to pay room and board. Oregon allows a deduction for any federally taxable portion of a scholarship used for housing.	Ohio, Oregon
Home mortgage interest deduction for mortgages taken out to cover tuition costs, among other nonhome-related costs	Hawaii expands its mortgage interest deduction to allow for filers to deduct interest paid on mortgages taken out to pay for expenses other than home expenses, including postsecondary education tuition.	Hawaii
Student loan repayment credit or exclusion of repayment assistance for students who stay and/or work in state or in certain professions	Maine offers a credit to offset student loan payments for people who receive a bachelor's or associate degree from a Maine postsecondary institution and subsequently live and work in the state. The credit is refundable for those who graduate with a science, technology, engineering, or math-related (STEM) undergraduate degree.* Federal law excludes from taxable income third-party repayments of student loans made by certain federal and state programs for health care professionals working in underserved areas. Montana extends this benefit to include qualified private loan repayment programs. The District of Columbia excludes loan repayment awards made by its government agencies for certain health care professionals and poverty lawyers working in the public interest.	Maine, Montana, District of Columbia
Tax provisions for professional development in specific occupations	The District allows a deduction from adjusted gross income for tuition and fees for postgraduate education, professional development, or state licensing examination and for testing to improve teaching credentials or maintain professional certification, up to $1,500 per person. Louisiana allows certain law enforcement officers and employees of the state's Department of Public Safety and Corrections pursuing an undergraduate degree related to criminal justice to claim a nonrefundable tax credit equal to the amount of qualifying expenses, including tuition, fees, and textbooks, up to $750.	District of Columbia, Louisiana
Deduction of AmeriCorps postservice education award	Iowa and Minnesota offer a deduction for postservice education awards for participants in an AmeriCorps national service program. The awards are intended to help repay student loans and would otherwise be taxable.	Iowa, Minnesota

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Benefit type	Description	States
Student loan interest deduction that is different from the federal provision	Massachusetts allows an unlimited deduction for interest paid on undergraduate student loans with certain restrictions regarding how the debt is administered and what types of expenses loan proceeds can be used for, among other conditions. The deduction is not allowed for interest that is claimed for the federal student loan interest deduction and therefore already incorporated in the federal adjusted gross income, which the state uses as the starting point for its tax returns.	Massachusetts
Exclusion of retirement plan distributions used for higher education tuition expenses	Distributions received from qualified retirement plans and related savings vehicles may be excluded from Delaware adjusted gross income if they have been included in federal adjusted gross income and are used in the same tax year for tuition and associated expenses paid by the taxpayer or his or her dependents who have not reached age 26.	Delaware

* The state expanded this credit beginning in tax year 2016 to include those who received an associate or bachelor's degree from a non-Maine institution or a graduate degree from a Maine institution. The credit was also made refundable for all associate degree recipients, regardless of whether their degree is in the STEM fields.

Source: Pew review of state tax forms, instructions, codes, and tax expenditure reports, as well as correspondence with state officials. See Appendix D for further explanation.

Appendix D: Methodology

Scope of tax expenditures included in this report

Although a wide array of tax expenditures relate to higher education, this study focuses on federal and state personal income tax provisions that directly support students and their families in meeting the costs of postsecondary education.

This analysis excludes certain tax provisions that pertain to higher education either because they are not personal income tax provisions or are not directly targeted toward reducing postsecondary education costs for individual filers or their designated beneficiaries, such as:

- Business, sales, and gift tax provisions, some of which may reduce the cost of pursuing postsecondary education.
- Special income tax benefits offered by a few states to individuals who contribute to programs that provide scholarships.
- The tax-exempt status of education organizations and their investment income, under Internal Revenue Code section 501(c)(3).

Notes on state tax expenditures

The state tax provisions identified in this report are based on tax year 2014 and do not reflect changes made after that year unless otherwise noted. Unlike the federal government, most states do not publish a comprehensive list of their tax expenditures, and states may differ in their definitions of a tax expenditure. Therefore, to compile a comprehensive set of state provisions, Pew proceeded in two stages:

1. Review state tax forms, instructions, and codes

The analysis began by reviewing each state's income tax forms, instructions, schedules, and if necessary, tax codes to catalogue the provisions offered. The researchers then identified which of these state provisions correspond to federal education-related tax expenditures listed by Treasury. In cases where states provisions derive from the use of a federal definition of income as their starting points, the tax expenditures may not be specifically listed on the tax return.

The exclusion of interest from United States savings bonds used to finance higher education expenses was an exception to the general rule of including all state provisions that correspond to a Treasury-listed tax expenditure. Although states do not tax this income and some identify it as a tax expenditure, this analysis did not include it because federal law prohibits states from taxing interest earned on any U.S. Treasury-issued savings bonds.

The researchers also identified stand-alone state provisions that are not linked to federal tax expenditures but fall within the scope of the paper because they directly assist students and their families in meeting the costs of postsecondary education. The analysis excluded state provisions that would not be considered tax expenditures under Treasury's framework, such as deductions for expenses for employer-required education.

2. Verify the accuracy and completeness of the information gathered

Pew then contacted personnel in each state—including those in revenue departments and agencies tasked with producing state tax expenditure reports—to confirm that the set of provisions identified in the review was accurate and complete for tax year 2014. Respondents were asked to verify and comment on the information gathered, such as highlighting provisions that were missed or inaccurately identified. Some state contacts did not respond; in those cases, the relevant findings are based on Pew's review of the provisions.

Researchers also asked states with comprehensive estimates of the revenue impacts of their tax expenditures to verify those estimates. For California, Minnesota, Oregon, and Wisconsin, some or all of the estimates were provided to Pew through direct communication rather than identified in a publicly available tax expenditure report.

Adding tax expenditure estimates

Although totaling estimates for separate tax expenditures often provides a reasonably good estimate of the total cost of groups of tax expenditures, it does not capture potential interactions among them or behavioral responses if any single one is modified or repealed.

Endnotes

1 Michael Leachman, Dylan Grundman, and Nicholas Johnson, "Promoting State Budget Accountability Through Tax Expenditure Reporting," Center on Budget and Policy Priorities (May 2011), http://www.cbpp.org/research/state-budget-and-tax/promoting-state-budget-accountability-through-tax-expenditure; and U.S. Government Accountability Office, "Tax Expenditures: Opportunities Exist to Use Budgeting and Agency Performance Processes to Increase Oversight," GAO-16-622 (July 2016), http://www.gao.gov/products/GAO-16-622.

2 Throughout this paper unless otherwise noted, the costs of tax expenditures are based on Pew's analysis of U.S. Treasury Department data as presented in U.S. Office of Management and Budget, "Analytical Perspectives, Budget of the United States Government (Fiscal Year 2016)," https://www.gpo.gov/fdsys/pkg/BUDGET-2016-PER/pdf/BUDGET-2016-PER.pdf. Treasury notes that, for several reasons, its tax expenditure estimates do not necessarily equal the increase in federal revenue or the change in the budget balance that would result from repealing these provisions. Similarly, the estimated revenue impact of a given tax expenditure may not be equivalent to an outlay through a spending program. Similarly, Pell Grant costs throughout this analysis are based on Pew's analysis of data from the U.S. Department of Education, "Budget History Tables, State Funding History Tables: FY 1980—FY 2014," http://www2.ed.gov/about/overview/budget/history/index.html.

3 Pew's analysis of U.S. Treasury Department data as presented in U.S. Office of Management and Budget, "Analytical Perspectives, Budget of the United States Government" (fiscal 1992 and 2016), https://www.gpo.gov/fdsys/browse/collectionGPO.action?collectionCode=BUDGET, https://www.scribd.com/document_downloads/239368643?extension=pdf&from=embed&source=embed.

4 Pew's analysis of data from the Delta Cost Project Database (May 2015), based on original data from the U.S. Department of Education, National Center for Education Statistics' Integrated Postsecondary Education Data System; and fiscal year 2014 data from U.S. Department of Education, National Center for Education Statistics' Integrated Postsecondary Education Data System (accessed November 2016), http://nces.ed.gov/ipeds/datacenter/. "Full-time equivalent" (FTE) is a measure used by the U.S. Department of Education to account for students who are enrolled either full time or part time as defined by each institution and make enrollment numbers comparable across institutions. The department's definition can be found here: http://nces.ed.gov/ipeds/glossary/index.asp?id=854. At the time of publication, Delta Cost data were available only through 2012, and IPEDS does not provide a fall FTE count going back to 1990. As a result, this value takes the Delta Cost fall FTE count for 1990 and compares it with the IPEDS count for 2014.

5 Internal Revenue Service, "American Opportunity Tax Credit," https://www.irs.gov/uac/american-opportunity-tax-credit.

6 Eligibility criteria for the Pell Grant program involve multiple considerations beyond family income levels, such as assets and family size. However, according to the U.S. Department of the Treasury, most Pell funding goes to dependent students whose parents have incomes of less than $60,000 or to nondependent students with incomes under $30,000. Higher education tax provisions generally benefit a wider range of income levels. Income phaseout ranges for the various higher education tax expenditures are shown in Appendix A, and more information on the income levels of Pell recipients is available from U.S. Department of the Treasury, "Report to Congress on Coordinating the American Opportunity Tax Credit and the Federal Pell Grant" (May 5, 2014), https://www.treasury.gov/resource-center/tax-policy/Documents/Report-Coordinating-AOTC-2014.pdf.

7 National Association of State Student Grant and Aid Programs, "45th Annual Survey Report on State-Sponsored Student Financial Aid, 2013-14 Academic Year," Table 14, https://www.nassgap.org/viewrepository.aspx?categoryID=3#.

8 A taxpayer generally cannot use more than one tax provision for the same expense. For instance, earnings from 529 plans may not be fully excluded from taxable income if they are used to pay tuition costs for which another higher education tax benefit was also claimed, such as the tuition-and-fees deduction.

9 In addition to the exclusion of earnings from 529 plans, the other two tax expenditures that target savings for future costs are Coverdell Education Savings Accounts and the exclusion of interest from U.S. savings bonds used for higher education expenses.

10 U.S. Department of the Treasury, "Report to Congress on Coordinating the American Opportunity Tax Credit and the Federal Pell Grant," 25. Generally, the AOTC is limited to undergraduate students, but some graduate students who have not taken four years of postsecondary education may be eligible.

11 Internal Revenue Service, "Topic 431—Canceled Debt—Is it Taxable or Not?" http://www.irs.gov/taxtopics/tc431.html.

12 Tax expenditures that result from linking to a federal definition of income do not include two of the four largest (in terms of impact on federal revenue) federal higher education tax expenditures (the AOTC and the lifetime learning credit). This is due to the nature of credits, which do not reduce federal adjusted gross or taxable income but instead are directly subtracted from the amount of taxes owed. For the purpose of this analysis, a small number of states that do not direct filers to enter gross or taxable income directly from their federal returns are still considered to start from a federal definition of income if their calculations of income mirror the steps taken at the federal level.

13 Beginning in tax year 2016, eligibility for the credit has been expanded to include those who received an associate or bachelor's degree from an out-of-state institution or a graduate degree from a Maine institution.

14 Several states, including Alabama, Louisiana, Maryland, Pennsylvania, and Virginia, offer adjustments—such as deductions—for expenses incurred by professionals in specific occupations who are required by law or by an employer to obtain the education to maintain employment or professional status. At the federal level, Treasury generally does not consider deductions for such expenses to be tax expenditures; states may or may not consider them tax expenditures. These provisions have been omitted from this analysis.

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