New Tax Bill and Higher Education

BY GARY M. ROSS

Capitol Hill ironies are commonplace. Here is a big one: Legislative threats to higher education currently spring from a largely unexpected source. At one time spending cuts required by federal deficit reduction constituted the likeliest risk. Now, mercifully spared in that arena, higher education faces a major setback from income-tax reform.

This generalization should be taken with caution. On the one hand, House/Senate legislation to reauthorize federal aid to higher education, including popular grants and loans for tuition, remains tentative. But it has always held that cutbacks in student aid should come from more stringent income tests for recipients, not elimination of the truly needy. Education is popular with the public and generally fares well when the members of Congress face reelection. Therefore, major direct assaults seem unlikely.

On the other hand, inasmuch as tax reform threatens higher education, it must be admitted that this happens partly in ways that will not affect most schools. For instance, the tax bill caps the issuance of tax-exempt construction bonds, but at a level that would curtail only the 20 or 30 largest private universities in the country.

In other areas, however, the tax agreement hits higher education very hard. Here are some little-noticed ways:

1. Currently, donors of appreciated property, such as real estate or stocks, can deduct from their gross income the full market value of such gifts. The new tax bill taxes the increased value of the charitable donation at a minimum rate of 21 percent. Forty percent of all gifts above $5,000 to public and nonprofit colleges consist of appreciated property.

2. The interest on consumer loans, including widely used college loans, has been fully deductible. That will no longer be the case. However, homeowners can borrow against their equity and deduct the interest if the loan is for home improvement, medical, or education costs. Remortgaging a house is a drastic and costly action. Homeowners would do this only to free up large sums of money. Very likely they would not immediately spend all of such money on tuition costs. Profits on any portion that is invested must, of course, be reported as conventional income.

3. Up to now, graduate students who received aid packages that exceeded the costs of their tuition and equipment did not have to report the excess as taxable income. Now they must do so.

This has the peculiar effect of penalizing the needy student who struggles along on a combination of jobs, loans, and scholarships. Such a person now faces the additional burden of taxation, while the affluent student whose tuition is paid by his or her parents has no tax liability at all.

Loss of the charitable deduction by nonitemizers, however, dwarfs all of the above. Its expiration at the end of 1986 despite intense lobbying efforts threatens to reduce charitable giving by an estimated $6 billion annually. Americans will have increased spendable income resulting from tax reform. However, many of them will give less to charities because of the repeal of the nonitemizer deduction.

This dismal result occurs simultaneously with the charities’ loss of another $6 billion annually because of the lowered marginal tax rates. As the number of tax brackets decreases and the tax rates become lower, the tax advantages of giving decline. To put it another way, the “cost of giving” increases.

At present, nearly 70-80 percent of all taxpayers do not itemize. This number will grow if, as the tax bill provides, the standard deduction rises and is indexed for inflation.

Although they may be overstating the situation, academic officials predict a catastrophic for higher education unequalled in 25 years.

The implications of recent tax revisions are certainly relevant to higher education. However, colleges must not underestimate the blessing of having escaped, at least for the time being, the brute of spending cuts.

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