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## EXPAND TUITION CREDIT

### House Bill 4191 (Substitute H-2) First Analysis (3-11-97)

**Sponsor: Rep. A.T.Frank**  
**Committee: Tax Policy**

#### ***THE APPARENT PROBLEM:***

Public Act 7 of 1995 (Senate Bill 237) created a nonrefundable income tax credit for tuition and fees paid for undergraduate education. The act permits a resident of the state with household income of \$200,000 or less to claim a credit equal to four percent of tuition and fees paid to a "qualified" institution of higher learning, up to a maximum credit of \$250 per student. The credit can be claimed for no more than four years per student. One of the criteria that makes a school a "qualified" school is a promise that tuition and fees will not be increased in the next academic year by more than the annual average percentage increase in the U.S. consumer price index in the immediately preceding tax year. The promise takes the form of a letter of notification sent to the state treasurer before July 1 of the tax year. (Amendatory legislation, applying to the 1996 tax year only, was enacted late in 1996 and specifies that schools must promise not to raise tuition and fees by more than three percent from the 1995-96 academic year to the 1996-97 academic year.) The credit was designed in this way so that it could serve several purposes. Not only does the credit provide tax relief for Michigan families sending children (or adults) to college and provide an incentive for additional education, but it also aims to encourage colleges and universities to restrain tuition increases. Given the autonomy of public institutions of higher education granted by the constitution (and the independence of private institutions), this approach was seen as a tool the legislature could use to control the cost of higher education.

Some people believe the CPI cap is not a significant factor in determining tuition and fees at colleges and universities, particularly at publicly funded schools, where increases are said to be related primarily to the extent of state support through the appropriations process. The cap does, however, deprive some Michigan families of the tax credit. Since students and parents don't choose schools based on changes in costs from year to year (although overall tuition costs themselves are a factor) and since they have little control over decisions made at the schools students are attending, legislation has been proposed eliminating the restriction on tuition increases. At the same time, some

people believe the maximum credit should be increased to make it a more powerful incentive.

#### ***THE CONTENT OF THE BILL:***

The bill would amend the Income Tax Act to increase the cap on the tuition tax credit from \$250 to \$500 per student per year and to remove the provision that the credit only applies to tuition and fees paid to an institution of higher education that promises not to raise fees and tuition rates by more than the annual average percentage increase in the U.S. consumer price index.

Under current law, a taxpayer who has household income of \$200,000 or less and is a state resident may claim a credit, not to exceed \$250, on his or her state income tax for tuition paid for himself or herself or for any other student equal to four percent of the sum of all fees and tuition paid to a qualified institution of higher learning. The term "tuition" would refer to tuition paid for credits for an in-state public or private undergraduate program and credits granted by a community college or two-year private college toward a degree program or granted for the purposes of transferring those credits toward an undergraduate degree program. A qualifying institution must provide a letter to the state treasurer stating it will not increase fees and tuition rates during the ensuing academic year by more than the annual average percentage increase in the U.S. consumer price index in the immediately preceding tax year. For 1996 only, the institution's letter must state it will not increase fees and tuition rates for the 1996-97 academic year by more than three percent above the rates for 1995-96. The credit is limited to four years for each student.

MCL 206.274

#### ***BACKGROUND INFORMATION:***

The tuition credit at present is equal to four percent of tuition and fees paid, capped at \$250 per student. This means it applies to tuition of up to \$6,250. (Four percent of \$6,250 is \$250.) Under the bill, with a maximum credit of \$500, the credit would apply to

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tuition of up to \$12,500. (Four percent of \$12,500 is \$500.) A credit of \$250 offsets income, for state income tax purposes, of \$5,680. A \$500 credit would offset \$11,360.

According to the Michigan Taxpayer's Guide, published by the Legislative Service Bureau, for the 1996 tax year, the credit could be claimed for tuition and fees paid to the following colleges and universities, based on their keeping their rates in line with inflation. Among state universities: Eastern Michigan, Ferris State, Grand Valley, Northern Michigan, Saginaw Valley, University of Michigan at Dearborn, Western Michigan, and Wayne State. Among private colleges and universities: Detroit College of Business, Hillsdale, Kalamazoo, Kendall College of Art and Design, Reformed Bible College, Spring Arbor, and Suomi. Among community colleges: Bay De Noc, Delta, Jackson, Kirtland, Lansing, Macomb, Mid-Michigan, Montcalm, Mott, Northwestern, Oakland, St. Clair County, and Wayne County. Without a CPI-based cap on tuition and fees, all institutions of higher learning would qualify.

### **FISCAL IMPLICATIONS:**

The House Fiscal Agency reports that the bill would result in a revenue reduction of about \$35.5 million in the 1997-98 fiscal year. (3-3-97)

### **ARGUMENTS:**

#### **For:**

Tying the tax credit to the rate of increase in tuition and fees, while well-intentioned, is unrealistic and unfair. It is not likely to have a significant impact on college tuition costs, but it does manage to exclude many families struggling to send children to school. The tax credit for the 1996 tax year is available for tuition paid to Michigan State but not to the University of Michigan, for Eastern Michigan but not Central Michigan, for Saginaw Valley but not Lake Superior State. Not only is this unfair, but parents who cannot get the credit are as likely to blame the legislature as the schools in question. Students and families do not choose a school based on how rapidly its tuition is increasing from one year to the next and are not likely to switch from one school to another based on the rate at which tuition is increasing. Families and students currently are penalized based on factors over which they have no practical control. (Further, basing eligibility on the rate of increase does not take into account the overall cost of tuition.) Eliminating the CPI cap will mean more Michigan families will receive the tax credit. Increasing the maximum credit will provide greater relief for some families and offer a greater incentive for students to continue in school. There is obvious value in encouraging higher education. The more schooling a

person has the higher their income tends to be through their working life, and higher education is likely to be even more crucial to a person's future in our information economy.

#### **Response:**

The tuition cap is a key feature of this credit. Its aim is to exercise some influence over tuition. If tuition increases are a concern, removing the cap will only make things worse. Without the cap, the income tax credit only provides an incentive for colleges to increase tuition (and soak up the extra available money). A credit of this kind must be accompanied by some tuition cost control if it is to be of real benefit to Michigan families.

#### **Against:**

To make college more affordable it would be better to increase appropriations to the state's public colleges and increase financial aid for students attending public or private colleges. This will have a more direct impact on college costs and will base assistance more directly on need or achievement. A tuition tax credit often sends state dollars to people who would likely send children to school in any case. Moreover, increasing the maximum credit would not appear to help most families, since they must be paying \$6,250 in tuition per child to get the current allowable maximum credit.

#### **Response:**

State support for higher education is important, as is financial aid, and the increase in the credit should not be seen as an alternative to other state funding. The tax credit is meant to be an additional form of assistance and incentive, not a replacement.

#### **Against:**

Why should taxpayers whose children do not go to college (or those without children) essentially help pay for a tax credit for those families whose children do attend? The state already generously supports a system of higher education, paid for by everyone's tax dollars. If such a credit is to be available, why not include the costs of job training and other kinds of valuable, non-degree, education, so that others can benefit as well? Some people would argue that if there is to be a college tax credit, it should be targeted at families with low and moderate incomes.

#### **Against:**

A great many tax reduction proposals are afloat. It would make sense to look at them comprehensively rather than piecemeal. It would also make sense to coordinate the review of tax reduction proposals with budget deliberations, so that the full impact of revenue reductions could be understood, including the impact on the funding of schools and higher education.

**Response:**

Supporters of this and other related proposals say that the tax cuts can be paid for out of anticipated revenue growth for the 1998 fiscal year. Further, they say that there have been numerous tax cuts in recent years, many of which have not benefitted the people targeted by the tax cut provided by this bill and others in the package, aimed at ordinary working families. Tax fairness should not be delayed by budget deliberations

**POSITIONS:**

The Presidents Council of State Colleges and Universities supports the elimination of the CPI cap on eligible institutions but has reservations about increasing the maximum amount of the credit. (3-5-97)

The Association of Independent Colleges and Universities of Michigan supports the lifting of the CPI cap. (3-5-97)

The Department of Treasury is opposed to the bill. (3-5-97)

The Michigan Education Association is opposed to the bill. (3-5-97)

Analyst: C. Couch

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■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.