About NACUBO:

The National Association of College and University Business Officers, founded in 1962, is a nonprofit professional organization representing chief administrative and financial officers at more than 1,900 colleges and universities across the country. NACUBO’s mission is to advance the economic vitality, business practices, and support of higher education institutions in pursuit of their missions.

QUESTIONS ABOUT TAX REFORM?

Contact NACUBO’s federal affairs team at advocacy@nacubo.org.
Dear NACUBO Member:

The House of Representatives has passed H.R. 1, which includes provisions that change how students and families pay for college; eliminates workforce benefits; and makes the way we do business (as nonprofit and public entities) costlier—at a time when lawmakers, the public, and colleges themselves are keenly focused on lowering college costs and student debt burdens.

While the version of the Tax Cuts and Jobs Act now headed to the Senate floor does not alter the student education provisions that were so alarming in H.R. 1, in its current shape, the bill that will go before the full United States Senate next week does not offer an overall significant improvement for higher education.

The following pages include background information and talking points on NACUBO’s top issues of concern. As amendments are offered during the debate on the Senate floor, the shape of the legislation may change and we will continue to analyze the legislation.

I urge you to share stories with your Senators about how the proposed changes in the Senate bill will impact your students, workforce, and institution. You should also work with your campus president, trustees, and communications and government relations team to publicly amplify your concerns—today—consider:

- Writing an opinion piece for publication in your student, local, or regional newspaper.
- Organizing campus leaders to visit with the editorial boards of local or national news outlets.
- Developing a website, blog, video, or Twitter campaign that communicates your concerns.

The Senate Tax Cut and Jobs Act in its current form could have profound effects on colleges and universities, and indeed all nonprofit, tax-exempt organizations across the country.

Sincerely,

John Walda
President and CEO
CHARITABLE GIVING

Charitable donations help colleges and universities achieve their teaching, research, and public service missions. For the past 100 years, the charitable deduction has encouraged individuals to make significant, transformational gifts to educational institutions.

It is unlikely that the government could find a better way to leverage private investment than with the charitable deduction. With limited funding from federal and state governments and pressure to limit tuition increases, raising private support is crucial for colleges and universities. From small colleges to large universities, charitable giving helps fuel commitments to provide an affordable, quality education.

Tax Cuts and Jobs Act H.R. 1 Proposal:
With changes to the standard deduction, which would be effectively doubled by H.R. 1, an estimated 6 percent of taxpayers would itemize their tax returns. Roughly 30 percent of taxpayers, many who claim the charitable deduction, currently itemize their tax returns.

This provision would effectively eliminate the charitable deduction for more than 90 percent of Americans. H.R. 1 also:

- Repeals the special rule that provides a charitable deduction of 80 percent of the amount paid for the right to purchase tickets for athletic events.
- Increases the 50-percent limitation for cash contributions to public charities and certain private foundations to 60 percent.
- Establishes new requirements for donor-advised funds.
- Phases-in a repeal of the estate tax.

Senate Proposal:

- Proposes a change similar to H.R. 1 for the standard deduction, altogether the thresholds in the Senate bill are slightly higher in the Senate version ($12,200 for individuals/$24,400 for couples).
- Preserves the estate tax but doubles the exemption level. Fewer individuals will pay the tax, and they will pay less.
- Repeals the special rule that provides a charitable deduction of 80 percent of the amount paid for the right to purchase tickets for athletic events.
- Increases the 50-percent limitation for cash contributions to public charities and certain private foundations to 60 percent.

The Joint Committee on Taxation has estimated that H.R. 1 would spur a dramatic drop in the amount of charitable giving in the U.S. with 32 million fewer people eligible to claim the deduction. Additionally, since the value of the charitable deduction is tied to a taxpayer’s marginal tax rate, tax rate cuts would automatically increase a donor’s cost of giving. However, a study by Indiana University’s Lilly Family School of Philanthropy and the Independent Sector found that the inclusion of a universal charitable deduction in tax reform would result in a $4.8 billion increase in charitable giving at a modest cost to the federal government.

Instead of curtailing the charitable deduction—which effectively imposes a tax on dollars donated to charities—lawmakers should strive to expand it. Enactment of a universal, or above-the-line, charitable deduction would provide a giving incentive to all American taxpayers by allowing them to subtract their charitable gifts from their income before they determine whether to take the standard deduction or itemize their tax returns.
Endowed funds—at colleges, universities, and many other private 501(c)3 organizations—represent the institution or organization’s promise to donors to use income and investment gains generated by their gifts to support an aspect of the university’s mission, usually in perpetuity. Colleges and universities, large and small, maintain endowments or other reserves that enable them to respond to unforeseen changes or seize new opportunities in pursuit of their respective missions.

At postsecondary institutions, endowments are critical for student financial aid (scholarships), but they also serve as funding sources for faculty, libraries, laboratories, campus housing, student services, and other components that are key to a student’s education. Endowments also support research and public service missions, such as innovations in nanotechnology, medical research, or university-based youth and community development programs.

There has been a focus in the tax reform process on endowment spending for student aid, with little recognition that endowment spending on other operational areas relieves tuition pressure. Covering non-scholarship institutional costs with endowment payouts eases pressure to increase tuition revenue.

Endowment managers are legally obligated to support current students and operations, while balancing asset management goals to ensure financial soundness for the institution in the future.

Lawmakers should reject proposals to impose an excise tax on endowments.

Such a tax, as well as other emerging proposals, would result in fewer dollars available for scholarships, student services, research, and college and university operating expenses. Further, the proposals represent a departure from the current federal commitment to philanthropic freedom—the right of Americans to choose how and where to spend their charitable assets.
Institutions should consider these talking points:

- Our foundation raises funds in excess of $_____ per year to support the university’s strategic priorities and manages an endowment of more than $_____.

- Our most recent comprehensive fundraising campaign engaged more than donors who made gifts exceeding $_____ to advance our school’s priorities.

- The annual endowment impact is significant and growing, totaling nearly $_____ for the university this year and more than $_____ in the past five years combined.

- Charitable giving is fueling our commitment to providing an affordable, quality education.

- Studies of charitable giving indicate that tax deductions are an important factor leading donors to make gifts. We ask Congress not to impose barriers that may limit charitable giving.

- Endowments are critical for student financial aid (scholarships), but they also provide important funding sources for faculty, libraries, laboratories, student services, and other components that are key to a student’s education.

- Endowments also support research and public service missions, such as innovations in nanotechnology, medical research, or university-based youth and community development programs.

- Endowments are an instrument of good financial planning for nonprofit entities—large and small. They are not a savings account or rainy day fund. They are managed to provide a steady, stable, reliable funding source over the long term.

The NACUBO-Commonfund Study of Endowments shows that 74 percent of institutions increased dollar spending in 2016, and the median increase was 8.1 percent—despite overall negative returns for that year. This spending increase is attributable in large part to the way endowments are managed for the long term.
Also consider:

- Endowments are a collection of funds—often comprised of 100s, or even 1000s, of individual funds that range in size from below $10,000 to over $1 million—managed for both future needs as well as current needs.

- Most college and university endowment funds have a specific, donor-directed purpose (e.g., research, financial aid, public service).

- Endowed funds represent the school’s promise to donors to use income and investment gains generated by their gift into perpetuity.

- Donors often stipulate the purpose for which funds can be spent and expect funds to last into perpetuity.

- An institution’s governing board determines the appropriate spending distribution policy. Spending policies strive to balance two primary investment objectives:
  1. The need for current operating income.
  2. The need to preserve the endowment’s future purchasing power.

There are more than 3,300 public and nonprofit colleges and universities in the U.S. educating nearly 19 million students, engaging in more than $67 billion in research and development, and contributing to a vast array of public service endeavors.

Public colleges and universities are typically a component of state or local governments, while private institutions are recognized as tax-exempt organizations under section 501(c)(3) of the Internal Revenue Code. Tax-exempt bond financing available to public institutions is also referred to as municipal bonds; similar financing is currently available to nonprofit colleges and universities (and some public institutions) as qualified 501(c)(3) private activity bonds.

Private nonprofit colleges and universities, just like their public counterparts, rely on these financial instruments to acquire, construct, renovate, and expand capital infrastructure such as academic buildings, residence halls, modern energy plants, and more.

For these schools, the interest rate on municipal bonds is significantly lower than on taxable bonds, thus creating beneficial financial terms. Indeed, the interest rate spread between taxable and tax-exempt bonds typically ranges between 150 and 200 basis points. The lower interest rates create significant savings by lowering the financing cost of multi-million dollar construction projects, often financed over a 30-year period. The lower financing cost allows colleges and universities to keep tuition lower than would be the case if taxable financing was used.

For many institutions, revenue from tuition or from restricted gifts simply does not provide sufficient funds to build, expand, and renovate as is necessary to meet their respective missions, and taxable debt is costlier, often by a material amount.

Lawmakers should protect and maintain qualified 501(c)(3) private-activity bonds and advance refunding. Access to these bonds contributes significantly to the financial health of colleges and universities across the United States.
SECTION 127

Not only do institutions of higher education prepare tomorrow’s workforce, but they must also attract qualified employees and maintain skilled workforces of their own. Proposals in the Tax Cuts and Jobs Act would severely limit this ability of both higher education institutions and employers in all other sectors by eliminating employer-provided tax-exempt tuition assistance.

Section 127 allows employers to offer employees up to $5,250 annually in tuition assistance, which is excluded from taxable income. Employers are never required to provide assistance under Section 127; however, if an employer chooses to do so, the benefit must be offered to all employees on a non-discriminatory basis to ensure that the benefit cannot favor the highly compensated.

Tax Cuts and Jobs Act H.R. 1 Proposal:
H.R. 1 repeals Section 127 and would be effective after 2017.

Senate Proposal:
The Senate does not include this provision.

When it was enacted as an expiring tax benefit in 1978, Section 127 was intended to allow employers to completely cover the cost of higher education. Unfortunately, the benefit amount of $5,250 annually has not been increased in almost 40 years, and now its elimination has been included in tax reform legislation.

NACUBO not only opposes the elimination of Section 127 but urges lawmakers to expand and improve the benefit. Specifically, we recommend that the $5,250 annual limit be significantly increased with an automatic adjustment for inflation and that Section 127 be expanded to permit employers to provide educational assistance to an employee’s partner and dependents. This change would generate more private sector funds for financial aid, particularly for low- and middle-income students.

Lawmakers should oppose H.R. 1’s elimination of Section 127. Further, proposals that emerged in the current session of Congress to expand and improve the benefit by increasing the $5,250 limit, expanding the eligible uses to include loan repayment, and allowing the benefit to be available to spouses and children of employees should be supported.

The benefits offered by Section 127 are an important tool for employers to attract the best possible employees and build a skilled workforce. It is not a benefit largely used by traditional students, but rather students working to build their skills while also employed. Section 127 helps support U.S. competitiveness and could, if strengthened, become the benefit of choice for tuition assistance and loan repayments among employers.
SECTION 117(d)

Section 117(d) – The Qualified Tuition Reduction

Section 117(d) permits educational institutions, including colleges and universities, to provide employees and their spouses or dependents with tuition reductions that are excluded from taxable income.

If an institution chooses to offer this benefit, then all employees must be able to receive it. As a result, Section 117(d) provides a particularly important benefit to many middle- and low-income college employees. In fact, the majority of employees benefiting from the provision are low- and middle-income.

According to a 2017 survey of nearly 300 institutions by the College and University Professional Association for Human Resources, 50 percent of employees receiving tuition reductions for themselves or family members earned $50,000 or less, and 78 percent earned $75,000 or less.

In addition, Section 117(d) gives colleges and universities an important tool for recruiting and retaining valued employees, which is particularly important for many small, private schools in their efforts to compete for top employees.

Tax Cuts and Jobs Act H.R. 1 Proposal:
H.R. 1 repeals Section 117(d) and would be effective after 2017.

Senate Proposal:
The Senate does not include this provision.

Section 117(d)(5) reduces the cost of graduate education and mitigates the tax liability of graduate students engaged in teaching and/or research as part of their academic programs. Without this provision thousands of graduate students would be subjected to either a major tax increase or a significant increase in tuition as universities would be forced to curtail tuition reductions. This would likely lead to increased student debt as many of these students might consider borrowing to pay these taxes or their tuition bills.

Lawmakers should oppose elimination of Section 117(d), which permits educational institutions, including colleges and universities, to provide employees and their spouses and dependents with tuition reductions that are excluded from taxable income.
PAYING FOR HIGHER EDUCATION

American Opportunity Tax Credit & Lifetime Learning Credit

NACUBO has supported simplification of the current system of education incentive tax credits through the creation of a single, permanent tax credit with automatic inflation adjustments, making it easier to use and more effective. A single, permanent, refundable credit, available beyond the first four years of college, and to both full-time and part-time learners, would negate the need for the separate higher education provisions, which currently include the American Opportunity Tax Credit (AOTC) and the Lifetime Learning Credit. However, H.R. 1 proposes to repeal the Lifetime Learning Credit, while only expanding AOTC to include a reduced fifth year of support.

Currently, the student loan interest deduction allows certain individuals to deduct up to $2,500 in student loan interest, with a phase-out for certain taxpayers. Recent federal actions have already increased the borrowing costs for students and recent graduates by implementing interest charges for graduate students while they are in school and by eliminating the six-month interest forgiveness college graduates have traditionally received. H.R. 1 calls for the elimination of the student loan interest deduction altogether.

Tax Cuts and Jobs Act H.R. 1 Proposal:
H.R. 1 eliminates the student loan interest deduction.

Senate Proposal:
The Senate does not include this provision.

In 2014, 12 million taxpayers benefited from the student loan interest deduction. Eliminating this provision would mean that, over the next decade, the cost of student loans for borrowers would increase by roughly $13 billion.

Lawmakers should seek to simplify and adjust the incentives that help students and families pay for college and employers build a skilled workforce by creating a single, permanent tax credit with automatic inflation adjustments and expanding the student loan interest deduction.
Tax Cuts and Jobs Act H.R. 1 Proposal:
Exclusion of research income limited to publicly available research. Exempt organizations could exclude from UBTI only income from fundamental research where the results are freely available to the public.

Senate Proposal:
The Senate draft does not include this provision.
However, the Senate includes two UBIT provisions that do not appear in H.R. 1:

- **Name and Logo Royalties Treated and Unrelated Taxable Income.** The proposal modifies the UBIT treatment of the licensing of an organization’s name or logo generally to subject royalty income derived from such a license to UBIT. Specifically, the proposal amends section 513 (regarding unrelated trades or businesses) to provide that any sale or licensing by an organization of any name or logo of the organization (including any trademark or copyright related to a name or logo) is treated as an unrelated trade or business that is regularly carried on by the organization. In addition, the proposal amends section 512 (regarding unrelated business taxable income) to provide that income derived from any such licensing of a name or logo of the organization is included in the organization’s gross unrelated business taxable income, notwithstanding the provisions of section 512 that otherwise exclude certain types of passive income (including royalties) from unrelated business taxable income.

- **Unrelated business taxable income separately computed for each trade or business.** For an organization with more than one unrelated trade or business, the proposal requires that unrelated business taxable income (UBTI) first be computed separately with respect to each trade or business and without regard to the specific deduction generally allowed under section 512(b)(12). The organization’s unrelated business taxable income for a taxable year is the sum of the amounts (not less than zero) computed for each separate unrelated trade or business, less the specific deduction allowed under section 512(b)(12). A net operating loss (NOL) deduction is allowed only with respect to a trade or business from which the loss arose.

Contrary to the term **tax-exempt organization**, nonprofit entities are subject to normal corporate tax rates on certain activities defined as “unrelated business income.” Whether an activity is subject to the unrelated business income tax (UBIT) is determined through a three-part test that asks: is it a trade or business; is it regularly carried on; and is it substantially related to the exempt organization’s mission? There are also several categories of activities that, by statute, are not treated as unrelated business income.

Colleges and universities, whose primary missions are related to education, research, and community service, should pay taxes on unrelated business activities as set forth/defined by the statute.

However, recordkeeping and reporting guidelines must be fair and not unduly burdensome. Any changes to such guidelines should not result in disparate treatment for nonprofit organizations by holding them to standards and rules not applicable to corporations—this is the impact of two Senate
provisions: Name and Logo Royalties Treated as Unrelated Taxable Income and Unrelated Business Taxable Income separately computed for each trade or business (basketing).

This “basketing” proposal would require all losses and gains to be calculated by activity rather than in the aggregate – this concept is not present in corporate taxation. For example, General Motors can apply Chevrolet losses against Cadillac division gains. Other companies may employ a “loss leader” strategy, enabled by the ability to offset gains with losses.

Nonprofits need revenues to operate—just like private businesses or government agencies. It is unclear why tax writers propose to subject nonprofit organizations to a special standard that, for colleges and universities, will likely result in a higher tax burden and fewer resources for serving students.
ON THE RADAR

**NACUBO is continuing to examine the impact of a number of additional provisions.**

**Pressure on State Budgets**

- **State and Local Tax Deduction (SALT):**
  Under current law, taxpayers can deduct their state income taxes or sales taxes and local property taxes. H.R. 1 would permit, but cap, the deduction for property taxes but eliminate the deduction for income and sales taxes.

  States, cities, counties, school districts, and other special districts have established tax rates that assumes the federal tax code provides deductibility. Many expect these jurisdictions to face pressure to lower tax rates—which would put downward budget pressure on state and local government spending.

- **State Pensions.** In H.R. 1, all entities exempt from tax under section 501(a), notwithstanding the entity’s exemption under any other provision of the Code, would be subject to the UBIT rules. Previously, state and local entities (such as public pension plans) may not have been subject to the UBIT rules.

  Any state pensions that have not been previously subject to the UBIT rules will likely face significant new tax liabilities.

  There is no similar provision in the Senate draft.

**Executive Compensation Excise Tax**

- **Under a House provision, a tax-exempt organization—and most public entities—would be subject to a 20-percent excise tax on compensation in excess of $1 million paid to any of its five highest paid employees for the tax year. The excise tax would apply to all remuneration paid to a covered person for services, including cash and the cash value of all remuneration (including benefits) paid in a medium other than cash, except for payments to a tax-qualified retirement plan, and amounts that are excludable from the executive’s gross income. Once an employee qualifies as a covered person, the excise tax would apply to compensation in excess of $1 million paid to that person so long as the organization pays him remuneration. The excise tax also would apply to excess parachute payments paid by the organization to such individuals. Under the provision, an excess parachute payment generally would be a payment contingent on the employee’s separation from employment with an aggregate present value of three times the employee’s base compensation or more.**

- **The Senate includes substantially more provisions related to executive compensation.**

- **Currently, nonprofits must adhere to a rigorous process prescribed by the Internal Revenue Service when setting executive compensation. The current process enables organizations to attract the best talent based in the marketplace. Presently, compensation decisions are made by board or committee members vetted for conflict of interest. The provisions related to executive compensation**
in both H.R.1 and the Senate plan are punitive and will simply serve to increase costs for all affected organizations.

### Housing Tax

- Under a House provision, the exclusion for housing provided for the convenience of the employer and for employees of educational institutions would be limited to $50,000 ($25,000 for a married individual filing a joint return) and would phase out for highly compensated individuals (income of $120,000 for 2017, as adjusted for inflation) at a rate of one dollar for every two dollars of adjusted gross income earned by the individual beyond the statutory threshold of being highly compensated. The exclusion also would be limited to one residence. The provision would be effective for tax years beginning after 2017.

There is no similar provision in the Senate draft.

### Fringe Benefits

- Both the Senate and the House include numerous provisions that would tax or eliminate favorable treatment of fringe benefits.
THE VALUE OF HIGHER EDUCATION

According to the College Board’s “Education Pays 2016,” college graduates in 2015 earned markedly more than high school graduates:

- Median annual earnings, college graduates: $61,400
- Median annual earnings, high school graduates: $36,800

Further college graduates earn a median of $1 million more over the course of their lives than those with only a high school diploma – $2.3 million in lifetime earnings versus $1.3 million according to the Georgetown Center on Education and the Workforce report, “The College Payoff,” 2014.

College graduates are much more likely to be employed than high school graduates; recent data from the National Center for Education Statistics show that even for students who graduated into the Great Recession, their college degrees helped them to fare better in the economy than those with no higher education.

While it is tempting to see these numbers and reflect upon them only as a private good, greater earnings and lower unemployment rates reflect increased productivity of the economic system overall.

College-going benefits society in other ways as well, the College Board research shows. College graduates are more likely to vote in elections and give back to their communities. They are also more likely to lead healthy lifestyles—exercising more, smoking less—and enjoy longer life spans, on average, than their counterparts who earned only a high school diploma.

The federal tax code has long recognized the value of education as public good, not only in preventing or relieving poverty and adverse social conditions for individuals, but also in advancing knowledge and research for society at large, fostering the productive and civic capacities of citizens, which is fundamental to our democratic society.

Teaching, research, and public service have been recognized in federal law as critical to the well-being of our democratic society. Higher education institutions are in turn exempted from income tax so they can make the most of their revenues. Colleges and universities are able to use more resources than would otherwise be available to fund academic programs, student financial aid, research, public extension activities, and their overall operations. As nonprofits, they are uniquely different from corporations that pay out profits to executives and shareholders and they are accountable to donors and trustees that operate as fiduciaries, and public colleges are further governed by state government oversight.