United States Government Accountability Office

GAO

Testimony

Before the Committee on Finance, U.S. Senate

For Release on Delivery
Expected at 10:00 a.m. EST
Tuesday, December 5, 2006

POSTSECONDARY EDUCATION

Multiple Tax Preferences and Title IV Student Aid Programs Create a Complex Education Financing Environment

Statement of Michael Brostek
Director, Tax Issues
Strategic Issues Team

George A. Scott
Acting Director
Education, Workforce, and Income Security Issues

GAO
Accountability * Integrity * Reliability

GAO
Accountability·Integrity·Reliability

Highlights

Highlights of GAO-07-262T, testimony before the Committee on Finance, U.S. Senate

Why GAO Did This Study

Federal assistance helps students and families pay for postsecondary education through several policy tools—grant and loan programs authorized by title IV of the Higher Education Act of 1965 and more recently enacted tax preferences. This testimony summarizes and updates our 2005 report on (1) how title IV assistance compares to that provided through the tax code (2) the extent to which tax filers effectively use postsecondary tax preferences, and (3) what is known about the effectiveness of federal assistance.

This hearing is an opportunity to consider whether any changes should be made in the government's overall strategy for providing such assistance or to the individual programs and tax provisions that provide the assistance. This statement is based on previously published GAO work and reviews of relevant literature.

What GAO Recommends

GAO does not make new recommendations in this testimony. In 2002, GAO recommended, among other things, that the Department of Education sponsor research into key aspects of effectiveness of title IV programs. In April 2006, Education announced it would make multiyear grants available starting in 2007 to conduct research on topics addressed in this statement.

www.gao.gov/cgi-bin/getrpt?GAO-07-262T.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Michael Brostek at (202) 512-9039 or George Scott at (202) 512-7215.

December 2006

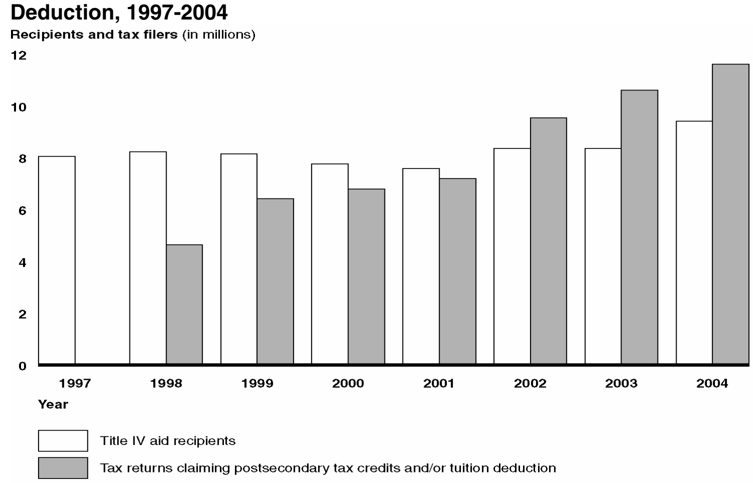
POSTSECONDARY EDUCATION

Multiple Tax Preferences and Title IV Student Aid Programs Create a Complex Education Financing Environment

What GAO Found

Title IV student aid and tax preferences provide assistance to a wide range of students and families in different ways. While both help students meet current expenses, tax preferences also assist students and families with saving for and repaying postsecondary costs. Both serve students and families with a range of incomes, but some forms of title IV aid—grant aid, in particular—provide assistance to those whose incomes are lower, on average, than is the case with tax preferences. Tax preferences require more responsibility on the part of students and families than title IV aid because taxpayers must identify applicable tax preferences, understand complex rules concerning their use, and correctly calculate and claim credits or deductions. While the tax preferences are a newer policy tool, the number of tax filers using them has grown quickly, surpassing the number of students aided under title IV in 2002.

Recipients of Title IV Assistance and Tax Filers Claiming an Education Tax Credit or Tuition Deduction, 1997-2004



Sources: GAO analysis of Budget of the United States Government and Internal Revenue Service data.

Some tax filers do not appear to make optimal education-related tax decisions. For example, among the limited number of 2002 tax returns available for our analysis, 27 percent of eligible tax filers did not claim either the tuition deduction or a tax credit. In so doing, these tax filers failed to reduce their tax liability by $169, on average, and 10 percent of these filers could have reduced their tax liability by over $500. One explanation for these taxpayers' choices may be the complexity of postsecondary tax provisions, which experts have commonly identified as difficult for tax filers to use.

Little is known about the effectiveness of title IV aid or tax preferences in promoting, for example, postsecondary attendance or school choice, in part because of research data and methodological challenges. As a result, policymakers do not have information that would allow them to make the most efficient use of limited federal resources to help students and families.

Chairman Grassley, Senator Baucus, and Members of the Committee:

We are pleased to be here this morning to discuss the federal government's efforts to financially support attendance at postsecondary education institutions. American higher education has long been crucial to the development of our nation's cultural, social, and economic capital. At the dawn of the 21st Century, changing workforce demographics, a more integrated global economy, and numerous technological advances are placing new demands on our colleges and universities. For the United States to remain competitive in the rising global knowledge economy, its citizens will need both the ways and means to endow themselves with the tools necessary for the task. However, rising tuition has become a disconcertingly fixed feature of our higher education system, and in recent months concerns about postsecondary access and affordability have received notable attention through the findings of the Secretary of Education's Commission on the Future of Higher Education and the Comptroller General's recent forum on the Global Competitiveness of the Nation's Higher Education System.

This hearing is an opportunity to consider whether any changes should be made in the government's overall strategy and the individual programs and tax provisions that provide financial assistance to students and families saving or paying for postsecondary education or repaying student loans. This opportunity to review the programs and tax provisions is important for several reasons. The fact that we face large and growing structural deficits in the future—primarily driven by demographics and rising health care costs—emphasizes the need to consider how the government allocates resources. In addition, GAO has noted that fundamental reexamination of government programs, policies, and priorities is necessary to assure that they match the needs of the 21st Century. GAO has identified the coordination of student aid programs[1] and the effectiveness of those programs[2] both as key topics needing congressional oversight.

My statement today will focus on three issues that emerged in our 2005 report on student grant and loan assistance made available under Title IV

[1] GAO, *21st Century Challenges: Reexamining the Base of the Federal Government*, GAO-05-325SP (Washington, D.C.: February 2005).

[2] GAO, *Suggested Areas for Oversight for the 110th Congress*, GAO-07-235R (Washington, D.C.: Nov. 17, 2006).

of the Higher Education Act and postsecondary education tax preferences.[3]

- Postsecondary student financial assistance provided through programs authorized under title IV and the tax code differ in three key ways. First, title IV grant and loan programs traditionally provide aid to students and families while students are in college, whereas tax preferences help both during the college years as well as before and after college by assisting with saving for or repaying college costs. Additionally, while student aid programs and tax preferences serve students and families across a wide range of income groups, some title IV programs—particularly the Pell grant program—provide much of their financial assistance to students and families whose incomes are lower, on average, than students and families who receive student loans, tax credits, and deductions, or who make use of tax-exempt saving vehicles. Last, students and families have more responsibility for appropriately using and thereby obtaining the benefits of tax preferences than they do with title IV aid.
- Second, postsecondary tax preferences are difficult for families to understand and use correctly. Perhaps due to the complexity of the tax provisions, hundreds of thousands of taxpayers fail to claim tax preferences to which they are entitled or do not claim the tax preference that would be most advantageous to them.
- Finally, we found that Congress has received little evidence concerning the effectiveness of assistance provided under title IV or through tax preferences, including whether such assistance increases attendance or choice.

Our statement today is drawn from previous GAO reports and testimonies covering postsecondary title IV programs and tax preferences, which were done in accordance with generally accepted government auditing standards, as well as reviews of relevant literature.

Background

Financial assistance to help students and families pay for postsecondary education has been provided for many years through student grant and loan programs authorized under title IV of the Higher Education Act of 1965, as amended. Examples of these programs include Pell Grants for low-income students, PLUS loans to parents and graduate students, and

[3] See GAO, *Student Aid and Postsecondary Tax Preferences: Limited Research Exists on Effectiveness of Tools to Assist Students and Families through Title IV Student Aid and Tax Preferences*, GAO-05-684 (Washington, D.C.: July 29, 2005).

Stafford loans.[4] Much of this aid has been provided on the basis of the difference between a student's cost of attendance and an estimate of the ability of the student and the student's family to pay these costs, called the expected family contribution (EFC). The EFC is calculated based on information provided by students and parents on the Free Application for Federal Student Aid (FAFSA). Statutory definitions establish the criteria that students must meet to be considered independent of their parents for the purpose of financial aid, and statutory formulas establish the share of income and assets that are expected to be available for the student's education.[5] In fiscal year 2005, the Department of Education made approximately $14 billion in grants, and title IV lending programs made available another $57 billion in loan assistance. Title IV also authorizes programs funded by the federal government and administered by participating higher education institutions, including the Supplemental Educational Opportunity Grant (SEOG), Perkins loans, and federal work-study aid, collectively known as campus-based aid. Table 1 provides brief descriptions of the title IV programs that we reviewed in our 2005 report and includes two programs—Academic Competitiveness Grants and National Science and Mathematics Access to Retain Talent Grants—that were created since that report was issued.[6]

[4]Consolidation loans are also authorized under title IV. These loans allow borrowers to combine multiple student loans, possibly from different lenders and from different loan programs, into a single new loan with extended repayment periods. Because consolidation loans do not generally result in an increase in loan principal, they are not addressed in this testimony.

[5]To be classified as an independent student for the purpose of receiving title IV financial aid, students must meet one of the following criteria: (1) be a veteran of the armed services, (2) be age 24 years or older by December 31st of the award year, (3) be married, (4) be enrolled in a graduate or professional education program, (5) have legal dependents other than a spouse, or (6) be an orphan or ward of the court. Financial aid administrators may also classify students as independent through the exercise of their professional judgment.

[6] For greater detail on federal spending through title IV postsecondary education assistance programs reviewed in our 2005 report, see app. I.

Table 1: Description of Federal Student Aid Programs Authorized under Title IV of the Higher Education Act

Title IV student aid program	Program description
Pell Grant	Grants are awarded on the basis of the difference between the EFC and the maximum Pell award or the student's cost of attendance, whichever is less. Grants are not available for postgraduate study.
Supplemental Educational Opportunity Grant	Schools administer grant funds, which are awarded to undergraduates with exceptional financial need; priority is given to Pell Grant recipients. Institutions must match a portion (at least 25 percent) of the federal funds allocated.
Academic Competitiveness Grant	Available to first- and second-year students who have completed a rigorous course of study in high school. To be eligible, students must also be eligible to receive a Pell Grant. Second-year students must also maintain at least a 3.0 grade-point average.
National Science and Mathematics Access to Retain Talent (SMART) Grant	Available to third- and fourth-year students pursuing a major in mathematics, science, or a foreign language deemed critical to national security. To be eligible, students must also be eligible to receive a Pell Grant and maintain at least a 3.0 grade-point average in their major.
Federal Work-Study	Schools administer funds, which are used to provide part-time jobs for undergraduate and graduate students with financial need. Participating schools or nonprofit employers generally contribute at least 25 percent of student's earnings (50 percent in the case of for-profit employers).
Federal Perkins Loan	Schools administer funds, comprised of federal capital contributions and school matching funds (at least 1/3 of federal contributions), to make low-interest (5 percent) loans for both undergraduate and graduate students with exceptional financial need. Borrower repayments are owed to the school.
Subsidized Federal Family Education Loan (FFEL) or Direct Stafford Loan	Loans made on the basis of financial need to undergraduate and graduate students who are enrolled at least half-time. The federal government pays the interest costs on subsidized loans while the student is in school, for the first 6 months after the student leaves school, and during a period of deferment.
Unsubsidized FFEL or Direct Stafford Loan	Loans made to undergraduate and graduate students who are enrolled at least half-time. Unlike subsidized loans, the federal government does not pay the interest costs on unsubsidized loans while the student is in school, for the first 6 months after the student leaves school, and during a period of deferment. Otherwise, the terms and conditions of unsubsidized loans are the same as those for subsidized loans.
FFEL or Direct PLUS Loan	Loans made to parents on behalf of dependent undergraduate students enrolled at least half-time. The Higher Education Reconciliation Act of 2005 makes both graduate and professional students eligible for these loans as well. Borrowers are subject to a credit check for adverse credit history and may be denied a loan.

Source: GAO analysis of applicable laws and regulations.

Postsecondary assistance also has been provided through a range of tax preferences,[7] including postsecondary tax credits, tax deductions, and tax-exempt savings programs. For example, the Taxpayer Relief Act of 1997 allows eligible tax filers to reduce their tax liability by receiving, for tax year 2006, up to a $1,650 Hope tax credit or up to a $2,000 Lifetime Learning tax credit for tuition and course-related fees paid for a single student. The fiscal year 2005 federal revenue loss estimate of the postsecondary tax preferences that we reviewed was $9.15 billion dollars. Tax preferences discussed as part of our 2005 report include the following:[8]

- Lifetime Learning Credit—income-based tax credit claimed by tax filers on behalf of students enrolled in one or more postsecondary education courses.
- Hope Credit—income-based tax credit claimed by tax filers on behalf of students enrolled at least half-time in an eligible program of study and who are in their first 2 years of postsecondary education.
- Student Loan Interest Deduction—income-based tax deduction claimed by tax filers on behalf of students who took out qualified student loans while enrolled at least half-time.
- Tuition and Fees Deduction—income-based tax deduction claimed by tax filers on behalf of students who are enrolled in one or more postsecondary education courses and have either a high school diploma or a General Educational Development (GED) credential.[9]
- Section 529 Qualified Tuition Programs—College Savings Programs and Prepaid Tuition Programs—non-income-based programs that provide favorable tax treatment to investments and distributions used to pay the expenses of future or current postsecondary students.
- Coverdell Education Savings Accounts—income-based savings program providing favorable tax treatment to investments and distributions used to pay the expenses of future or current elementary, secondary, or postsecondary students.

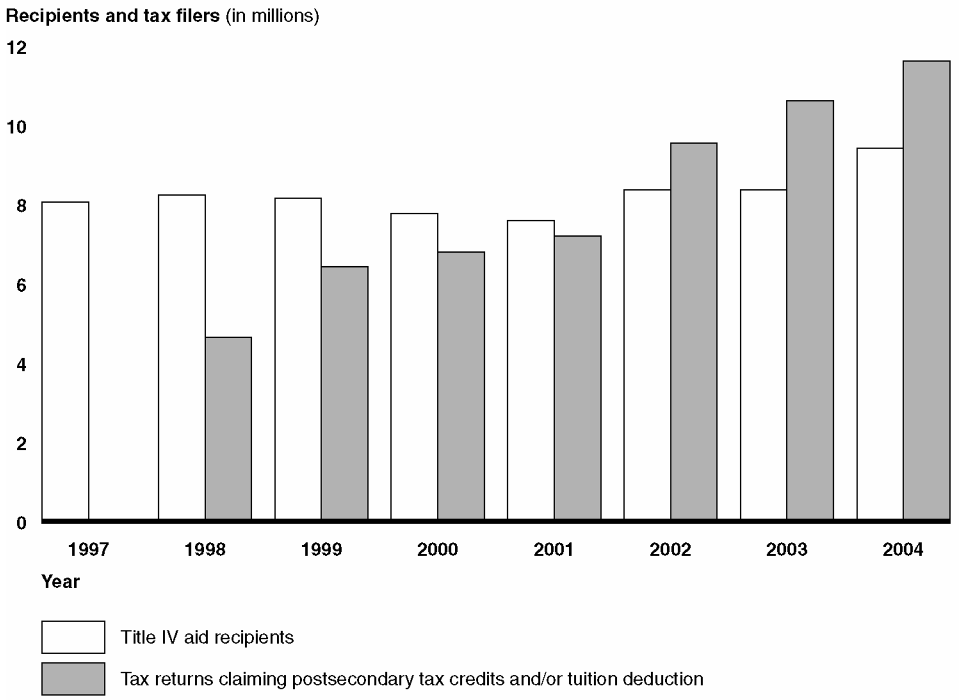
As figure 1 demonstrates, the use of tax preferences has increased since 1997, both in absolute terms and relative to the use of title IV aid.

[7] Tax preferences—also known as tax expenditures—are reductions in tax liabilities that result from preferential provisions in the tax code, such as exemptions and exclusions from taxation, deductions, credits, deferrals, and preferential tax rates.

[8] For expanded descriptions of postsecondary education-related tax preferences, see app. I.

[9] The Tuition and Fees Deduction expired on December 31, 2005. Legislation has been introduced to reinstate the deduction.

Figure 1: Recipients of Title IV Assistance and Tax Filers Claiming an Education Tax Credit or Tuition Deduction, 1997-2004



Sources: GAO analysis of Budget of the United States Government and Internal Revenue Service data.

Note: See app. IV for confidence intervals associated with these estimates.

Tax Preferences Differ from Title IV Assistance in Timing, Distribution, and Students' and Families' Responsibility for Obtaining Benefits

Postsecondary student financial assistance provided through programs authorized under title IV of the Higher Education Act and the tax code differ in timing of assistance, the populations that receive assistance, and the responsibility of students and families to obtain and use the assistance.

Title IV and Tax Programs Differ in Benefit Timing

Title IV programs and education-related tax preferences differ significantly in when eligibility is established and in the timing of the assistance they provide. Title IV programs generally provide benefits to students while they are in school. Education-related tax preferences, on the other hand, (1) encourage saving for college through tax-exempt saving, (2) assist enrolled students and their families in meeting the current costs of postsecondary education through credits and tuition deductions, and (3) assist students and families repaying the costs of past postsecondary education through a tax deduction for student loan interest paid.[10]

Beneficiaries of Title IV Programs and Tax Preferences Differ

While title IV programs and tax preferences assist many students and families, program and tax rules affect eligibility for such assistance. These rules also affect the distribution of title IV aid and the assistance provided through tax preferences. As a result, the beneficiaries of title IV programs and tax preferences differ.

Title IV programs generally have rules for calculating grant and loan assistance that give different consideration to family income, assets, and college costs in the award of financial aid.[11] For example, Pell Grant awards are calculated by subtracting the student's EFC from the maximum Pell Grant award ($4,050 in academic year 2006-2007), or the student's cost of attendance, whichever is less. Because the EFC is closely linked to family income and circumstances (such as the size of the family and the number of dependents in school), and modest EFCs are required for Pell eligibility, Pell awards are made primarily to families with modest incomes. In contrast, the maximum unsubsidized Stafford loan amount is calculated without direct consideration of financial need: students may borrow up to their cost of attendance, minus the estimated financial assistance they will receive.[12] As table 2 shows, 92 percent of Pell financial support in 2003-2004 was provided to dependent students whose family incomes were $40,000 or below, and the 38 percent of Pell recipients in the

[10] Additional details on the differences in timing are available in app. II.

[11] Campus-based aid programs authorized under title IV differ from these programs in funding and eligibility: institutions provide matching funding for federal spending, and participating institutions distribute aid using institution-specific criteria consistent with federal program requirements. Because they have institution-specific criteria, the relationship between program rules and the distribution of benefits is more complex and was excluded from the analysis of our 2005 report.

[12] Additionally, loan amounts for both subsidized and unsubsidized loans are subject to statutory limits on annual and cumulative borrowing.

lowest income category ($20,000 or below) received a higher share (48 percent) of Pell financial support.

Table 2: Percentage of Aid Recipients and Dollars of Aid by Income Category for Dependent Students Served by Selected Title IV Programs, 2003-2004

Program	Dependent students	$0-20,000	$20,001-40,000	$40,001-60,000	$60,001-80,000	$80,001-100,000	More than $100,000
Pell Grant	Recipients	38	47	14	2	0	0
	Dollars	48	44	8	1	0	0
Stafford Subsidized Loan	Recipients	16	28	23	17	9	7
	Dollars	16	28	24	17	9	6
Stafford Unsubsidized Loan	Recipients	7	14	14	19	18	28
	Dollars	7	12	12	18	19	32

Source: GAO analysis of 2003-2004 NPSAS data.

Note: See app. IV for confidence intervals associated with these estimates. Numbers in rows may not add to 100 percent because of rounding.

Because independent students generally have lower incomes and accumulated savings than dependent students and their families, patterns of program participation and dollar distribution differ. Participation of independent students in Pell, subsidized Stafford, and unsubsidized Stafford loan programs is heavily concentrated among those with incomes of $40,000 or less: from 74 percent (unsubsidized Stafford) to 95 percent (Pell) of program participants have incomes below this level. As shown in table 3, the distribution of award dollars follows a nearly identical pattern.

Table 3: Percentage of Aid Recipients and Dollars of Aid by Income Category for Independent Students Served by Selected Title IV Programs, 2003-2004

Program	Independent students	$0-20,000	$20,001-40,000	$40,001-60,000	$60,001-80,000	$80,001-100,000	More than $100,000
Pell Grant	Recipients	67	28	5	0	0	0
	Dollars	73	25	3	0	0	0
Stafford Subsidized Loan	Recipients	51	29	12	5	2	1
	Dollars	52	28	12	5	2	2
Stafford Unsubsidized Loan	Recipients	46	28	14	6	3	3
	Dollars	46	24	13	7	3	5

Source: GAO analysis of 2003-2004 NPSAS data.

Notes: See app. IV for confidence intervals associated with these estimates.

Numbers in rows may not add to 100 percent because of rounding.

Many education-related tax preferences have both de facto lower limits created by the need to have a positive tax liability to obtain their benefit and income ceilings on who may use them. For example, the Hope and Lifetime Learning tax credits require that tax filers have a positive tax liability to use them and income-related phase-out provisions in 2005 that began at $45,000 and $90,000 for single and joint filers, respectively. Furthermore, tax-exempt savings are more advantageous to families with higher incomes and tax liabilities because, among other reasons, these families hold greater assets to invest in these tax preferences and have a higher marginal tax rate, and thus benefit the most from the use of these tax preferences. Table 4 shows the income categories of tax filers claiming the three tax preferences available to current students and/or their families along with the reduced tax liabilities from those preferences in 2004.

Table 4: Percentage of Tax Filers Claiming Hope and Lifetime Learning Credits and Tuition Deduction and Tax Preference Dollars by Income Category, Tax Year 2004

Type of aid		$0-20,000	$20,001-40,000	$40,001-60,000	$60,001-80,000	$80,001-100,000	More than $100,000
Hope Credit	Tax filers	18	34	19	16	12	2
	Dollars	16	33	20	16	12	2
Lifetime Learning Credit	Tax filers	17	32	20	19	10	2
	Dollars	15	30	20	20	13	2
Tuition Deduction	Tax filers	24	13	15	10	13	25
	Dollars	11	7	18	12	15	37

Source: GAO analysis of 2004 SOI data.

Notes: See app. IV for confidence intervals associated with these estimates.

Numbers in rows may not add to 100 percent because of rounding.

Students and Families Have More Responsibility for Obtaining Benefits of Tax Preferences in Comparison to Title IV Aid

The federal government and postsecondary institutions have significant responsibilities in assisting students and families in obtaining assistance provided under title IV programs but only minor roles with respect to tax filers' use of education-related tax preferences. To obtain federal student aid, applicants must first complete the FAFSA, a form which required students to complete up to 100 fields in 2006-2007. Submitting a completed FAFSA to the Department of Education largely concludes students' and families' responsibility in obtaining aid. The Department of Education is responsible for calculating students' and families' EFC on the basis of the FAFSA, and students' educational institutions are responsible for determining aid eligibility and the amounts and packaging of awards.

In contrast, higher education tax preferences require students and families to take more responsibility. Although postsecondary institutions provide students and IRS with information about higher education attendance, they have no other responsibilities for higher education tax credits, deductions, or tax-preferred savings. The federal government's primary role with respect to higher education tax preferences is the promulgation of rules; the provision of guidance to tax filers; and the processing of tax returns, including some checks on the accuracy of items reported on those tax returns. The responsibility for selecting among and properly using tax preferences rests with tax filers. Unlike title IV programs, users must understand the rules, identify applicable tax preferences, understand how these tax preferences interact with one another and with federal student aid, keep records sufficient to support their tax filing, and correctly claim the credit or deduction on their return.

Some Tax Filers May Not Effectively Use Postsecondary Tax Preferences, Possibly Due to Complexity

According to our analysis of IRS data on the use of Hope and Lifetime tax credits and the tuition deduction in our 2005 report, some tax filers appear to make less-than-optimal choices among them.[13] The apparent suboptimal use of postsecondary tax preferences may arise, in part, from the complexity of these provisions.

Some Tax Filers Appear to Make Suboptimal Choices

Making poor choices among tax preferences for postsecondary education may be costly to tax filers. For example, families may strand assets in a tax-exempt savings vehicle and incur tax penalties on their distribution if their child chooses not to go to college. They may also fail to minimize their federal income tax liability by claiming a tax credit or deduction that yields less of a reduction in taxes than a different tax preference or by failing to claim any of their available tax preferences. For example, if a married couple filing jointly with one dependent in his/her first 2 years of college had an adjusted gross income of $50,000, qualified expenses of $10,000 in 2006, and tax liability greater than $2,000, their tax liability would be reduced by $2,000 if they claimed the Lifetime Learning credit but only $1,650 if they claimed the Hope credit.

[13] Due to time constraints, we were unable to update these analyses for this testimony.

In our 2005 report, we found that some people who appear to be eligible for tax credits and/or the tuition deduction did not claim them. The files of about 77 percent of the tax year 2002 tax returns that we were able to review were apparently eligible to claim one or more of the three tax preferences. However, about 27 percent of those returns, representing about 374,000 tax filers, failed to use the any of them. The amount by which these tax filers failed to reduce their tax averaged $169; 10 percent of this group could have reduced their tax liabilities by over $500.[14]

Suboptimal choices were not limited to tax filers who prepared their own tax returns. A possible indicator of the difficulty people face in understanding education-related tax preferences is how often the suboptimal choices we identified were found on tax returns prepared by paid tax preparers. We estimate that about 50 percent of the returns we found that appear to have failed to optimally reduce the tax filer's tax liability were prepared by paid tax preparers. Generalized to the population of tax returns we were able to review, returns prepared by paid tax preparers represent about 223,000 of the approximately 447,000 suboptimal choices we found. Our April 2006 study of paid tax preparers corroborated the problem of confusion over which of the tax preferences to claim.[15] Of the 9 undercover investigation visits we made to paid preparers with a taxpayer with a dependent college student, 3 preparers did not claim the credit most advantageous to the taxpayer and thereby cost these taxpayers hundreds of dollars in refunds. In our investigative scenario, the expenses and the year in school made the Hope education credit far more advantageous to the taxpayer than either the tuition and fees deduction or the Lifetime Learning credit.

The Suboptimal Use of Postsecondary Tax Preferences May Result from Their Complexity

The apparently suboptimal use of postsecondary tax preferences may arise, in part, because of the complexity of using these provisions. Tax policy analysts have frequently identified postsecondary tax preferences as a set of tax provisions that demand a particularly large investment of knowledge and skill on the part of students and families or expert assistance purchased by those with the means to do so. They suggest that this complexity arises from multiple postsecondary tax preferences with similar purposes, from key definitions that vary across these provisions,

[14] Confidence intervals for all estimates in this section are included in appendix IV.

[15] GAO, *Paid Tax Return Preparers: In a Limited Study, Chain Preparers Made Serious Errors*, GAO-06-563T (Washington, D.C.: Apr. 4, 2006).

and from rules that coordinate the use of multiple tax provisions. Twelve tax preferences are outlined in the IRS publication, Tax Benefits for Education, for use in preparing 2005 returns (the most recent publication available). The publication includes 4 different tax preferences for educational saving. Three of these preferences—Coverdell Education Savings Accounts, Qualified Tuition Programs, and U.S. education savings bonds—differ across more than a dozen dimensions, including the tax penalty that occurs when account balances are not used for qualified higher education expenses, who may be an eligible beneficiary, annual contribution limits, and other features.

In addition to learning about, comparing, and selecting tax preferences, filers who wish to make optimal use of multiple tax preferences must understand how the use of one tax preference affects the use of others. The use of multiple education-related tax preferences is coordinated through rules that prohibit the application of the same qualified higher education expenses for the same student to more than one education-related tax preference, sometimes referred to as "anti-double-dipping rules." These rules are important because they prevent tax filers from underreporting their tax liability. Nonetheless, anti-double-dipping rules are potentially difficult for tax filers to understand and apply, and misunderstanding them may have consequences for a filer's tax liability.[16]

Research on Effectiveness of Federal Postsecondary Assistance Is Incomplete

Little is known about the effectiveness of federal grant and loan programs and education-related tax preferences in promoting attendance, choice, and the likelihood that students either earn a degree or continue their education (referred to as persistence). Many federal aid programs and tax preferences have not been studied, and for those that have been studied, important aspects of their effectiveness remain unexamined. In our 2005 report, we found no research on any aspect of effectiveness for several major title IV federal postsecondary programs and tax preferences. For example, no research had examined the effects of federal postsecondary education tax credits on students' persistence in their studies or on the type of postsecondary institution they choose to attend. Gaps in the research-based evidence of federal postsecondary program effectiveness may be due, in part, to data and methodological challenges that have proven difficult to overcome. The relative newness of most of the tax

[16] For an example of this phenomenon, please see app. III.

preferences also presents challenges because relevant data are just now becoming available.

In 2002, we recommended that Education sponsor research into key aspects of effectiveness of title IV programs, that Education and the Department of the Treasury collaborate on such research into the relative effectiveness of title IV programs and tax preferences, and that the Secretaries of Education and Treasury collaborate in studying the combined effects of tax preferences and title IV aid.[17] In April 2006, Education's Institute for Education Sciences (IES) issued a Request for Applications to conduct research on, among other things, "evaluating the efficacy of programs, practices, or policies that are intended to improve access to, persistence in, or completion of postsecondary education." Multiyear projects funded under this subtopic are expected to begin in July 2007.

As we noted in our 2002 report, research into the effectiveness of different forms of postsecondary education assistance is important.[18] Without such information federal policymakers cannot make fact-based decisions about how to build on successful programs and make necessary changes to improve less effective programs. The budget deficit and other major fiscal challenges facing the nation necessitate rethinking the base of existing federal spending and tax programs, policies, and activities by reviewing their results and testing their continued relevance and relative priority for a changing society.[19]

Concluding Observations

In light of the long-term fiscal challenge this nation faces and the need to make hard decisions about how the federal government allocates resources, this hearing provides an opportunity to continue a discussion about how the federal government can best help students and their families pay for postsecondary education. Some questions that Congress should consider during this dialog include:

[17]GAO, *Student Aid and Tax Benefits: Better Research and Guidance Will Facilitate Comparison of Effectiveness and Student Use*, GAO-02-751 (Washington, D.C.: Sept. 13, 2002).

[18] GAO-02-751.

[19] GAO-05-325SP.

- Should the federal government consolidate postsecondary education tax provisions to make them easier for the public to use and understand?
- Given its limited resources, should the government further target title IV programs and tax provisions based on need or other factors?
- How can Congress best evaluate the effectiveness and efficiency of postsecondary education aid provided through the tax code?
- Can tax preferences and title IV programs be better coordinated to maximize their effectiveness?

Mr. Chairman and Members of the Committee, this concludes our statement. We welcome any questions you have at this time.

Staff Contacts and Acknowledgments

For further information regarding this testimony, please contact Michael Brostek at (202) 512-9039 or brostekm@gao.gov or George Scott at (202) 512-7215 or scottg@gao.gov. Individuals making contributions to this testimony include David Lewis, Assistant Director; Jeff Appel, Assistant Director; Shirley Jones, Sheila McCoy, John Mingus, Jeff Procak, Carlo Salerno, Andrew Stephens, and Michael Volpe.

Appendix I: Postsecondary Aid Programs

The federal government helps students and families save, pay for, and repay the costs of postsecondary education through grant and loan programs authorized under title IV of the Higher Education Act of 1965, and through tax preferences—reductions in federal tax liabilities that result from preferential provisions in the tax code, such as exemptions and exclusions from taxation, deductions, credits, deferrals, and preferential tax rates.

Federal Grant and Loan Assistance to Postsecondary Students

Assistance provided under title IV programs include Pell Grants for low-income students, the newly established Academic Competitiveness and National Science and Mathematics Access to Retain Talent Grants, PLUS loans, which parents as well as graduate and professional students may apply for, and Stafford loans.[1] While each of the three grant types reduces the price paid by the student, student loans help to finance the remaining costs and are to be repaid according to varying terms. Stafford loans may be either subsidized or unsubsidized. The federal government pays the interest cost on subsidized loans while the student is in school, and during a 6-month period known as the grace period, after the student leaves school. For unsubsidized loans, students are responsible for all interest costs.[2] Stafford and PLUS loans are provided to students through both the FFEL program and the William D. Ford Direct Loan Program (FDLP). The federal government's role in financing and administering these two loan programs differs significantly. Under the FFEL program, private lenders, such as banks, provide loan capital and make loans, and the federal government guarantees FFEL lenders a minimum yield on the loans they make and repayment if borrowers default. Under FDLP, federal funds are used as loan capital and loans are provided through participating schools.

[1] Consolidation loans are also authorized under title IV. These loans allow borrowers to combine multiple student loans, possibly from different lenders and from different loan programs, into a single new loan with extended repayment periods. Because consolidation loans do not generally result in an increase in loan principal, consolidation loans are not addressed in this review. However, the federal government can incur significant costs in providing borrowers with these loans. See GAO, *Student Loan Programs: As Federal Costs of Loan Consolidation Rise, Other Options Should Be Examined*, GAO-04-101 (Washington, D.C.: Oct. 31, 2003) and *Student Loan Programs: Lower Interest Rates and Higher Loan Volume Have Increased Federal Consolidation Loan Costs*, GAO-04-568T (Washington, D.C.: Mar. 17, 2004).

[2] While called "unsubsidized," the federal government can still incur costs on such loans, including the costs associated with borrowers who default on their loans and, under the Federal Family Education Loan Program, the costs of making payments to lenders to ensure them a minimum federally guaranteed yield.

The Department of Education and its private-sector contractors jointly administer the program. Title IV also authorizes programs funded by the federal government and administered by participating higher education institutions, including the Supplemental Educational Opportunity Grant (SEOG), Perkins loans, and federal work-study aid, collectively known as campus-based aid.

To receive title IV aid, students (along with parents, in the case of dependent students) must complete a Free Application for Federal Student Aid form. Information from the FAFSA, particularly income and asset information, is used to determine the amount of money—called the expected family contribution—that the student and/or family is expected to contribute to the student's education. Statutory definitions establish the criteria that students must meet to be considered independent of their parents for the purpose of financial aid, and statutory formulas establish the share of income and assets that are expected to be available for the student's education. Once the EFC is established, it is compared with the cost of attendance at the institution chosen by the student. The cost of attendance comprises tuition and fees; room and board; books and supplies; transportation; miscellaneous personal expenses; and, for some students, additional expenses.[3] If the EFC is greater than the cost of attendance, the student is not considered to have financial need, according to the federal aid methodology. If the cost of attendance is greater than the EFC, then the student is considered to have financial need. Title IV assistance that is made on the basis of the calculated need of aid applicants is called need-based aid. Key characteristics of title IV programs are summarized in table 5 below.

[3]These may include child care expenses for parents of young dependent children or supportive services for disabled students.

Table 5: Description of Federal Student Aid Programs Authorized under Title IV of the Higher Education Act

Title IV student aid program	Program details	Annual award amounts	Number and characteristics of beneficiaries
Pell Grant	Grants are awarded on the basis of the difference between the EFC and the maximum Pell award or the student's cost of attendance, whichever is less. Grants are not available for postgraduate study.	$400 to $4,050 for school year 2006-2007.	Dependent students: About 2.1 million grants were awarded in school year 2003-2004, totaling $5.3 billion. The average grant award was $2,573; the median income of recipients was $24,576. Independent students: About 3 million grants were awarded in school year 2003-2004, totaling $7.4 billion. The average grant award was $2,436; the median income of recipients was $12,925.
Supplemental Educational Opportunity Grant	Schools administer grant funds, which are awarded to undergraduates with exceptional financial need; priority is given to Pell Grant recipients. Institutions must match a portion (at least 25 percent) of the federal funds allocated.	$100 to $4,000.	Dependent students: About 554,000 grants were awarded in school year 2003-2004, totaling $494.2 million. The average grant award was $892; the median income of recipients was $22,827. Independent students: About 715,000 grants were awarded in school year 2003-2004, totaling $391.9 million. The average grant award was $548; the median income of recipients was $11,040.
Academic Competitiveness Grant	Available to first- and second-year students who have completed a rigorous course of study in high school. To be eligible, students must also be eligible to receive a Pell Grant. Second-year students must also maintain at least a 3.0 grade-point average.	$750 for first-year students and $1,300 for second year students.	Students: About 310,000 first-year grants and 110,000 second-year grants are expected to be awarded in school year 2006-2007, totaling an estimated $340.0 million. The average grant award is estimated to be $657 and $1,245 respectively.
National Science and Mathematics Access to Retain Talent (SMART) Grant	Available to third- and fourth-year students pursuing a major in mathematics, science, or a foreign language deemed critical to national security. To be eligible, students must also be eligible to receive a Pell Grant and maintain at least a 3.0 grade-point average in their major.	$4,000.	Students: About 40,000 third-year grants and 40,000 fourth-year grants are expected to be awarded in school year 2006-2007, totaling an estimated $310.0 million. The average grant award is estimated to be $3,718 and $3,875 respectively.

Title IV student aid program	Program details	Annual award amounts	Number and characteristics of beneficiaries
Federal Work-Study	Schools administer funds, which are used to provide part-time jobs for undergraduate and graduate students with financial need. Participating schools or nonprofit employers generally contribute at least 25 percent of student's earnings (50 percent in the case of for-profit employers).	Up to $300 more than the student's determined financial need; if employment continues past this point, federal funds may not be used to subsidize the employment.	Dependent students: About 1.1 million awards were awarded in school year 2003-2004, totaling $2 billion. The average award was $1,901; the median income of recipients was $46,441. Independent students: About 438,000 awards were awarded in school year 2003-2004, totaling $1 billion. The average award was $2,303; the median income of recipients was $10,561.
Federal Perkins Loan	Schools administer funds, comprised of federal capital contributions and school matching funds (at least 1/3 of federal contributions), to make low-interest (5 percent) loans for both undergraduate and graduate students with exceptional financial need. Borrower repayments are owed to the school.	$4,000 maximum for undergraduate students and $6,000 for graduate students; no minimum award amount. (Aggregate limits: $8,000 for undergraduates who have not completed 2 academic years; $20,000 for undergraduates who have completed 2 years; and, $40,000 for graduate students, including loans borrowed as an undergraduate.)	Dependent students: About 495,000 loans were made in school year 2003-2004, totaling $956 million. The average loan amount was $1,932; the median income of recipients was $39,175. Independent students: About 329,000 loans were made in school year 2003-2004, totaling $905.3 million. The average loan amount was $2,752; the median income of recipients was $10,277.
Subsidized FFEL or Direct Stafford Loan[a]	Loans made on the basis of financial need to undergraduate and graduate students who are enrolled at least half-time. The federal government pays the interest costs on subsidized loans while the student is in school, for the first 6 months after the student leaves school, and during a period of deferment.	$2,625 to $8,500 depending upon year of schooling. Aggregate limits are $23,000 for undergraduates and $65,500 for graduate students.	Dependent students: About 2.6 million loans were made in school year 2003-2004, totaling $8.1 billion. The average loan amount was $3,188; the median income of recipients was $44,678. Independent students: About 3.8 million loans were made in school year 2003-2004, totaling $16.3 billion. The average loan amount was $4,340; the median income of recipients was $19,430.

Title IV student aid program	Program details	Annual award amounts	Number and characteristics of beneficiaries
Unsubsidized FFEL or Direct Stafford Loan[a]	Loans made to undergraduate and graduate students who are enrolled at least half-time. Unlike subsidized loans, the federal government does not pay the interest costs on unsubsidized loans while the student is in school, for the first 6 months after the student leaves school, and during a period of deferment. Otherwise, the terms and conditions of unsubsidized loans are the same as those for subsidized loans.	$2,625 to $18,500 depending on year of schooling (including any subsidized loan amounts received for the same period). Aggregate limits are $23,000 for dependent undergraduates, $46,000 for independent undergraduates, and $138,500 for graduate students.	Dependent students: About 1.6 million loans were made in school year 2003-2004, totaling $5.3 billion. The average loan amount was $3,293; the median income of recipients was $75,835. Independent students: About 3.3 million loans were made in school year 2003-2004, totaling $18.5 billion. The average loan amount was $5,671; the median income of recipients was $22,108.
FFEL or Direct PLUS Loan	Loans made to parents on behalf of dependent undergraduate students enrolled at least half-time. The Higher Education Reconciliation Act of 2005 makes both graduate and professional students eligible for these loans as well. Borrowers are subject to a credit check for adverse credit history and may be denied a loan.	Maximum loan amounts are limited to cost of attendance less other federal, state, private, and institutional aid received for the period of enrollment.	About 634,000 loans were made in school year 2003-2004, totaling $5.7 billion. The average loan amount was $9,019; the median income of recipients was $71,397.

Source: GAO analysis of applicable laws and regulations and school year 2003-2004 NPSAS data.

[a]New slightly higher limits for these loans will take effect on July 1, 2007.

Tax Preferences

Prior to the 1990s, virtually all major federal initiatives to assist students with the costs of postsecondary education were provided through grant and loan programs authorized under title IV of the Higher Education Act. Since the 1990s, however, federal initiatives to assist families and students in paying for postsecondary education have largely been implemented through the federal tax code. The federal tax code now contains a range of tax preferences that may be used to assist students and families in saving for, paying, or repaying the costs of postsecondary education. These tax preferences include credits and deductions, both of which allow tax filers to use qualified higher education expenses to reduce their federal income tax liability. The tax credits reduce the tax filers' income tax liability on a dollar-for-dollar basis but are not refundable. Tax deductions permit qualified higher education expenses to be subtracted from income that would otherwise be taxable. To benefit from a higher education tax credit or tuition deduction, a tax filer must use tax form 1040 or 1040A, have an adjusted gross income below the provisions' statutorily specified income limits, and have a positive tax liability after other deductions and credits are calculated, among other requirements.

Tax preferences also include tax-exempt savings vehicles. Section 529 of the tax code makes tax free the investment income from qualified tuition programs. There are two types of qualified tuition programs: savings programs established by states and prepaid tuition programs established either by states or by one or more eligible educational institutions. Another tax-exempt savings vehicle is the Coverdell Education Savings Account. Tax penalties apply to both 529 programs and Coverdell savings accounts if the funds are not used for allowable education expenses. Key features of these and other education-related tax preferences are described below, in table 6.

Table 6: Selected Postsecondary Education Tax Preferences

	Preference details				
Tax preference	**Eligibility**	**Income ranges for phasing out benefits (2006)a**	**Eligible expenses**	**Tax benefit (2006)**	**Number and characteristics of beneficiaries**
Hope Credit	Tax filer on behalf of self, spouse, or dependent who is working toward a degree or certificate at least half-time in the first 2 years of postsecondary enrollment.	Single filer: $45,000-$55,000 Joint return: $90,000-$110,000.b	Tuition and fees at institutions eligible to participate in title IV programs.	Maximum credit: $1,650 per student. Credit rate is 100 percent on first $1,100 of qualified higher education expenses, 50 percent on next $1,100.d Nonrefundable: if filer has no tax liability due to offsetting deductions, exemptions, or competing tax credits, filer cannot receive credit.	In tax year 2002, 3.3 million tax filers claimed $3.2 billion in Hope credits; the average credit claimed was $991, and the median income of filers claiming the credit was $39,203.

Tax preference	Preference details: Eligibility	Preference details: Income ranges for phasing out benefits (2006)a	Eligible expenses	Tax benefit (2006)	Number and characteristics of beneficiaries
Lifetime Learning Credit	Tax filer on behalf of self, spouse, or dependent who is enrolled in undergraduate or graduate courses, or any course that aids in learning new or improving existing job skills, for as many years as the student is enrolled.	Single filer: $45,000-$55,000 Joint return: $90,000-$110,000.b	Tuition and fees at institutions eligible to participate in title IV programs.	Maximum credit: $2,000 per tax filer. (20 percent of qualified higher education expenses up to $10,000).d Nonrefundable: if filer has no tax liability due to offsetting deductions, exemptions, or competing tax credits, filer cannot receive credit.	In tax year 2002, 3.5 million tax filers claimed $1.7 billion in Lifetime Learning credits; the average credit claimed was $477, and the median income of filers claiming the credit was $39,706.
Student Loan Interest Deduction	Tax filer, on behalf of self, spouse, or dependent, available even to those who do not itemize interest paid. Student must have been enrolled at least half-time in a degree program.	Single filer: $50,000-$65,000 Joint return: $105,000-$135,000.c	Eligible loans are those used to pay for tuition, fees, room and board, and related expenses and include, for example, student loans provided under title IV.	Maximum deduction: $2,500 interest paid on eligible education loans is deductible.	In tax year 2002, 6.6 million tax filers deducted $892.6 million of student loan interest; the average deduction was $134, and the median income of filers deducting student loan interest was $43,544.
Section 529 qualified tuition programs—prepaid tuition programs and state-sponsored college savings programs	Specifics depend on particular program. Normally a prepaid program is open for contributions only on behalf of young children and accounts must be closed within some number of years after the beneficiary reaches college age. Generally, savings programs do not have age restrictions.	No phase-out.	Tuition, fees, books, supplies, and equipment required for attendance. Room and board if enrolled half-time or more.	No tax is due on a distribution from an account unless the amount distributed is greater than the beneficiary's adjusted qualified education expenses.	Section 529 qualified tuition programs—prepaid tuition programs and state-sponsored college savings programs

	Preference details				
Tax preference	Eligibility	Income ranges for phasing out benefits (2006)a	Eligible expenses	Tax benefit (2006)	Number and characteristics of beneficiaries
Coverdell Education Savings Accounts	Distributions can be used for students enrolled on full-time, half- time, or less than half-time basis. Account must be closed within 30 days after beneficiary reaches age 30.	For contributions, $95,000-$110,000 for single filers and $190,000-$220,000 for joint returns.	Tuition, fees, books, supplies, and equipment required for attendance. Room and board if enrolled half-time or more.	No tax is due on a distribution from an account unless the amount distributed is greater than the beneficiary's adjusted qualified education expenses. Annual contribution limit is $2,000 per year per student (through age 17).	Coverdell Education Savings Accounts
Tuition Deduction (expired Dec. 31, 2005)e	Same as Lifetime Learning credit.	Single filer: $65,000-80,000 Joint Return: $130,000-160,000.	Tuition and fees at institutions eligible to participate in title IV programs.	Maximum deduction: $4,000 per return for individual filers whose modified adjusted gross income is less than $65,000 ($130,000 for joint filers); $2,000 per return for individuals whose modified adjusted gross income is more than $65,000 ($130,000) but less than $80,000 ($160,000).	Tuition Deduction (expired Dec. 31, 2005)e

Sources: IRS, Investment Company Institute, and College Savings Plan Network documents; GAO analysis of IRS Statistics of Income data for tax year 2002.

[a] Modified adjusted gross income amounts are provided.

[b] Under the Taxpayer Relief Act of 1997, the income phase-out amounts are indexed to inflation according to a formula specified in law for this purpose, which may or may not result in a yearly increase.

[c] Under the 26 U.S.C. § 221(f), the income phase-out amounts are indexed to inflation according to a formula specified in law for this purpose, which may or may not result in a yearly increase.

[d] For students attending otherwise eligible educational institutions located within the Gulf Opportunity Zone, the maximum Hope tax credit and maximum Lifetime Learning tax credit are doubled for taxable years 2005 and 2006. Gulf Opportunity Zone Act, Pub. L. No. 109-135, § 102, 119 Stat. 2577, 2594 (2005).

[e] Although the tuition deduction has expired, H.R. 5970, 109th Cong. § 201 (2006), among other bills, would renew the deduction for tuition expenses through December 31, 2007. H.R. 5970 passed in the House on July 29, 2006, but had not yet passed the Senate.

Our review of tax preferences did not include exclusions from income, which permit certain types of education-related income to be excluded from the calculation of adjusted gross income on which taxes are based. For example, qualified scholarships covering tuition and fees and qualified tuition reductions from eligible educational institutions are not included in gross income for income tax purposes. Similarly, student loans forgiven when a graduate goes into certain professions for a certain period of time are also not subject to federal income taxes. We also did not include special provisions in the tax code that also extend existing tax preferences when tax filers support a postsecondary education student. For example, tax filers may claim postsecondary education students as dependents after age 18, even if the student has his or her own income over the limit that would otherwise apply. Also, gift taxes do not apply to funds used for certain postsecondary educational expenses, even for amounts in excess of the usual $11,000 limit on gifts. In addition, funds withdrawn early from an Individual Retirement Account are not subject to the usual 10 percent penalty when used for either a tax filer's or his or her dependent's postsecondary educational expenses.

Appendix II: Comparison of Assistance by Timing of Benefit for Selected Programs and Tax Preferences

Table 7: Comparison of Assistance by Timing of Benefit for Selected Programs and Tax Preferences

Type of assistance	Save for future expenses	Pay current expenses	Repay expenses
Grant programs		Pell Grants Supplemental Educational Opportunity Grants Academic Competitiveness Grants SMART Grants	
Loan programs		Subsidized and Unsubsidized Stafford Loans Federal Perkins Loans Federal PLUS Loans	
Tax preferences	Coverdell Educational Savings Accounts and Section 529 Qualified Tuition Programs	Hope Credit Lifetime Learning Credit Tuition Deduction	Student Loan Interest Deduction
Work-Study program		Federal Work Study	

Source: GAO.

Appendix III: Effects of Tax Rules on Tax Preference Use

For an example of how the use of college savings programs and the tuition deduction is affected by “anti-double-dipping” rules, consider the following: To calculate whether a distribution from a college savings program is taxable, tax filers must determine if the total distributions for the tax year are more or less than the total qualified educational expenses reduced by any tax-free educational assistance, i.e., their adjusted qualified education expenses (AQEE). After subtracting tax-free assistance from qualified educational expenses to arrive at the AQEE, tax filers multiply total distributed earnings by the fraction (AQEE / total amount distributed during the year). If parents of a dependent student paid $6,500 in qualified education expenses from a $3,000 tax-free scholarship and a $3,600 distribution from a tuition savings program, they would have $3,500 in AQEE. If $1,200 of the distribution consisted of earnings, then $1,200 x ($3,500 AQEE / $3,600 distribution) would result in $1,167 of the earnings being tax free, while $33 would be taxable. However, if the same tax filer had also claimed a tuition deduction, anti-double-dipping rules would require the tax filer to subtract the expenses taken into account in figuring the tuition deduction from AQEE. If $2,000 in expenses had been used toward the tuition deduction, then the taxable distribution from the section 529 savings program would rise to $700.[1] For families such as these, anti-double-dipping rules increase the computational complexity they face and may result in unanticipated tax liabilities associated with the use of section 529 savings programs.

[1]The new nontaxable distribution figure is calculated $1,200 x ($1,500/$3,600) = $500. The taxable portion then becomes $1,200 - $500 = $700.

Appendix IV: Confidence Intervals

We used two data sets for this testimony: Education's 2003-2004 National Postsecondary Student Aid Study and the Internal Revenue Service's 2002 and 2004 Statistics of Income. Estimates from both data sets are subject to sampling errors and the estimates we report are surrounded by a 95 percent confidence interval. The following tables provide the lower and upper bounds of the 95 percent confidence interval for all estimate figures in the tables in this testimony. For figures drawn from these data, we provide both point estimates and confidence intervals.

Table 8: Federal Student Aid Programs Authorized under Title IV of the Higher Education Act, Academic Year 2003-2004

	Number of recipients		Total award		Average award		Median income	
Type of assistance	Lower bound	Upper bound	Lower bound	Upper bound	Lower bound	Upper bound	Lower bound	Upper bound
Dependent students								
Pell Grant	2,026,011	2,115,312	5,201,091,600	5,452,845,564	2,543	2,573	24,165	24,999
Supplemental Educational Opportunity Grant	530,408	577,316	466,079,305	522,325,472	857	892	22,022	23,484
Federal Work- Study	1,023,755	1,089,687	1,927,247,135	2,090,819,033	1,856	1,901	45,000	48,231
Federal Perkins Loan	472,640	517,207	907,800,538	1,004,290,295	1,887	1,932	37,623	40,814
Subsidized FFEL or Direct Stafford Loan	2,505,118	2,604,668	7,962,531,788	8,329,729,995	3,155	3,188	43,834	45,446
Unsubsidized FFEL or Direct Stafford Loan	1,578,160	1,664,757	5,173,481,648	5,505,576,910	3,244	3,293	74,263	77,439
FFEL or Direct PLUS Loan	609,125	659,071	5,458,550,634	5,979,275,038	8,787	9,019	69,547	73,439
Independent students								
Pell Grant	2,967,340	3,087,638	7,212,123,299	7,540,282,035	2,409	2,436	12,614	13,262
Supplemental Educational Opportunity Grant	684,528	745,839	368,492,546	415,343,758	526	548	10,425	11,626
Federal Work- Study	676,216	766,317	933,916,755	1,084,530,206	2,192	2,303	9,808	11,525
Federal Perkins Loan	522,918	595,499	839,749,704	970,851,318	2,648	2,752	9,181	11,628
Subsidized FFEL or Direct Stafford Loan	3,658,692	3,869,237	15,604,880,694	17,068,144,196	4,244	4,340	18,754	20,148
Unsubsidized FFEL or Direct Stafford Loan	3,154,948	3,359,231	17,728,962,613	19,212,909,259	5,531	5,671	21,190	23,095
FFEL or Direct PLUS Loan	0	0	0	0	0	0	0	0

Source: GAO analysis of 2003-2004 National Postsecondary Student Aid Study data.

Table 9: Selected Postsecondary Education Tax Preferences, Tax Year 2002

	Number of returns		Total benefits		Average benefit		Median income	
Type of assistance	Lower bound	Upper bound	Lower bound	Upper bound	Lower bound	Upper bound	Lower bound	Upper bound
Hope Credit	3,115,595	3,414,023	3,064,601,005	3,399,426,275	965	1,016	37,506	41,004
Lifetime Learning Credit	3,307,354	3,612,179	1,560,825,683	1,740,857,453	462	493	38,060	41,001
Student Loan Interest Deduction	6,432,399	6,849,170	848,115,632	937,085,664	129	140	42,378	44,657
Tuition Deduction	3,295,741	3,599,012	1,226,452,349	1,370,953,823	364	391	51,808	56,842

Source: GAO analysis of Statistics of Income data for 2002.

Table 10: Tax Filers Claiming an Education Tax Credit or Tuition Deduction

		1998	1999	2000	2001	2002	2003	2004
Hope Credit, Lifetime Learning Credit, and Tuition Deduction	Lower bound	4,482,106	6,233,732	6,606,583	6,997,019	9,319,692	10,370,110	11,360,283
	Upper bound	4,827,719	6,639,576	7,024,049	7,428,088	9,809,833	10,882,359	11,892,067

Source: GAO analysis of Statistics of Income data.

Table 11: Percentage of Aid Recipients and Dollars of Aid by Income Category for Dependent Students Served by Selected Title IV Programs, School Year 2003-2004

Program	Dependent students		$0-20,000	$20,001-40,000	$40,001-60,000	$60,001-80,000	$80,001-100,000	More than $100,000
Pell Grant	Recipients	Lower bound	36.66	45.41	13.17	1.41	0	0
		Upper bound	38.89	47.72	14.76	2.02	0	0
	Dollars	Lower bound	46.29	42.41	7.38	0.65	0	0
		Upper bound	48.82	44.89	8.5	1.04	0	0
Stafford Subsidized Loan	Recipients	Lower bound	15.41	26.79	22.45	16.1	8.38	6.23
		Upper bound	16.94	28.73	24.3	17.72	9.61	7.33
	Dollars	Lower bound	15.32	27.14	22.83	15.68	7.92	5.87
		Upper bound	17.07	29.35	24.94	17.51	9.3	7.08
Stafford Unsubsidized Loan	Recipients	Lower bound	6.51	12.83	13.15	17.69	16.68	27
		Upper bound	7.88	14.76	15.21	19.94	18.84	29.5
	Dollars	Lower bound	6.22	11.05	11.31	16.69	17.55	30.3
		Upper bound	7.75	12.99	13.41	19.2	20.15	33.37

Source: GAO analysis of 2003-2004 National Postsecondary Student Aid Study data.

Table 12: Percentage of Aid Recipients and Dollars of Aid by Income Category for Independent Students Served by Selected Title IV Programs, Academic Year 2003-2004

Program			$0- 20,000	$20,001-40,000	$40,001-60,000	$60,001-80,000	$80,001-100,000	More than $100,000
Pell Grant	Recipients	Lower bound	66.28	26.59	4.59	0	0	0
		Upper bound	68.35	28.57	5.62	0	0	0
	Dollars	Lower bound	71.68	23.62	2.32	0	0	0
		Upper bound	73.77	25.65	2.96	0	0	0
Stafford Subsidized Loan	Recipients	Lower bound	49.67	27.54	10.78	4.04	1.3	0.86
		Upper bound	52.62	30.38	13.48	5.36	1.98	2.38
	Dollars	Lower bound	49.93	25.26	10.05	3.87	1.2	0.46
		Upper bound	54.61	29.79	14.73	5.4	2.05	2.65
Stafford Unsubsidized Loan	Recipients	Lower bound	44.65	26.59	12.09	5.48	2.31	2.26
		Upper bound	47.82	29.75	15.18	6.87	3.18	4.08
	Dollars	Lower bound	44.28	22.51	11.96	6.22	2.86	3.42
		Upper bound	48.37	26	14.78	8.49	4.12	6.99

Source: GAO analysis of 2003-2004 National Postsecondary Student Aid Study data.

Table 13 Percentage of Tax Filers Claiming Hope and Lifetime Learning Credits and Tuition Deduction and Tax Preference Dollars by Income Category, Tax Year 2004

Type of aid			$0-20,000	$20,001-40,000	$40,001-60,000	$60,001-80,000	$80,001-100,000	More than $100,000
Hope Credit	Tax filers	Lower bound	16.5	31.4	17	14.3	10.4	1.2
		Upper bound	20.1	35.7	20.4	17.6	13.3	2
	Dollars	Lower bound	14.7	30.6	18.1	14.6	10.7	1.4
		Upper bound	18.2	35.2	22.1	18.2	13.9	2.3
Lifetime Learning Credit	Tax filers	Lower bound	15.5	30.3	18.7	17.5	8.3	1.4
		Upper bound	18.6	34.1	21.9	20.7	10.7	2.2
	Dollars	Lower bound	13.2	28	17.5	17.4	11.1	1.7
		Upper bound	16.9	32.9	21.7	21.7	14.8	3
Tuition Deduction	Tax filers	Lower bound	21.9	11.4	13.6	9.3	11.9	23.6
		Upper bound	25.1	13.9	16.3	11.7	14.5	26.7
	Dollars	Lower bound	10	5.8	16.2	9.9	13.5	34.5
		Upper bound	12.1	7.6	20.4	13.4	17.2	39.5

Source: GAO analysis of Statistics of Income data for 2004.

Table 14: Percentage of Form 1098-Ts with Postsecondary Expense Information in 2002: Point Estimates

	Number of returns	Percent of returns
1098Ts with expense information	1,795,180	13
1098Ts without expense information	12,356,444	87

Source: GAO analysis of Statistics of Income data for 2002.

Table 15: Percentage of Form 1098-Ts with Postsecondary Expense Information in 2002: Confidence Intervals

	Number of returns: Lower bound	Number of returns: Upper bound	Percent of returns: Lower bound	Percent of returns: Upper bound
1098Ts with expense information	1,687,744.88	1,902,614.62	11.97	13.4
1098Ts without expense information	12,087,410.46	12,625,476.86	86.6	88.03

Source: GAO analysis of Statistics of Income data for 2002.

Table 16: Percentage of Taxpayers Apparently Eligible to Claim an Education Tax Credit or Tuition Deduction in 2002: Point Estimates

	Number of returns	Percent of returns
Total	1,795,180	100
Potentially eligible	1,386,659	77
All other	408,521	23

Source: GAO analysis of Statistics of Income data for 2002.

Table 17: Percentage of Taxpayers Apparently Eligible to Claim an Education Tax Credit or Tuition Deduction in 2002: Confidence Intervals

	Number of returns: Lower bound	Number of returns: Upper bound	Percent of returns: Lower bound	Percent of returns: Upper bound
Total	1,795,176.75	1,795,179.75	100	100
Potentially eligible	1,290,394.34	1,482,923.26	74.83	79.66
All other	360,292.26	456,749.64	20.34	25.17

Source: GAO analysis of Statistics of Income data for 2002.

Table 18: Percentage of Apparently Eligible Taxpayers to Claim an Education Tax Credit or Tuition Deduction That Failed to Do So in 2002: Point Estimates

	Number of returns	Percent of returns
Failed to claim	373,595	27

Source: GAO analysis of Statistics of Income data for 2002.

Table 19: Percentage of Apparently Eligible Taxpayers to Claim an Education Tax Credit or Tuition Deduction That Failed to Do So in 2002: Confidence Intervals

	Number of returns: Lower bound	Number of returns: Upper bound	Percent of returns: Lower bound	Percent of returns: Upper bound
Failed to claim	323,504.26	423,686.08	23.85	30.04

Source: GAO analysis of Statistics of Income data for 2002.

Table 20: Amounts by Which Apparently Eligible Taxpayers Failed to Reduce Their Tax Liability in 2002: Point Estimates

	Inaction led to increased tax liability
Median	52.45
Mean	168.66
10th percentile	4.34
25th percentile	10.94
75th percentile	207.2
90th percentile	532.96
Maximum value	1,116

Source: GAO analysis of Statistics of Income data for 2002.

Table 21: Amounts by Which Apparently Eligible Taxpayers Failed to Reduce Their Tax Liability in 2002: Confidence Intervals

	Inaction led to increased tax liability
Median: Lower bound	34.69
Median: Upper bound	73.57
Mean: Lower bound	136.57
Mean: Upper bound	200.76
10th percentile: Lower bound	3.01
10th percentile: Upper bound	6.57
25th percentile: Lower bound	8.66
25th percentile: Upper bound	16.72
75th percentile: Lower bound	137.73
75th percentile: Upper bound	312.14
90th percentile: Lower bound	429.22
90th percentile: Upper bound	729.58

Source: GAO analysis of Statistics of Income data for 2002.

Table 22: Percentage of Apparently Eligible Taxpayers That Claimed the Tuition Deduction but Would Have Been Better off Claiming the Lifetime Learning Credit in 2002: Point Estimates

	Number of returns	Percent of returns
Would have been better off claiming Lifetime Learning Credit	50,908	21

Source: GAO analysis of Statistics of Income data for 2002.

Table 23: Percentage of Apparently Eligible Taxpayers That Claimed the Tuition Deduction but Would Have Been Better off Claiming the Lifetime Learning Credit in 2002: Confidence Intervals

	Number of returns: Lower bound	Number of returns: Upper bound	Percent of returns: Lower bound	Percent of returns: Upper bound
Would have been better off claiming Lifetime Learning Credit	34,819.89	70,274.77	14.53	29.33

Source: GAO analysis of Statistics of Income data for 2002.

Table 24: Amounts by Which Apparently Eligible Taxpayers Could Have Reduced Their Tax Liability in 2002: Point Estimates

	Lifetime Learning Credit produced larger reduction
Median	50.67
Mean	83.22
10th percentile	7.35
25th percentile	26.23
75th percentile	119.6
90th percentile	157.91
Maximum value	556

Source: GAO analysis of Statistics of Income data for 2002.

Table 25: Amounts by Which Apparently Eligible Taxpayers Could Have Reduced Their Tax Liability in 2002: Confidence Intervals

	Lifetime Learning Credit produced larger reduction
Median: Lower bound	32.89
Median: Upper bound	84.27
Mean: Lower bound	49.76
Mean: Upper bound	116.68
10th percentile: Lower bound	.
10th percentile: Upper bound	27.14
25th percentile: Lower bound	10.7
25th percentile: Upper bound	47.56
75th percentile: Lower bound	62.07
75th percentile: Upper bound	148.53
90th percentile: Lower bound	106.35
90th percentile: Upper bound	.

Source: GAO analysis of Statistics of Income data for 2002.

Table 26: Percentage of Apparently Eligible Taxpayers That Claimed the Lifetime Learning Credit but Would Have Been Better off Claiming the Tuition Deduction in 2002: Point Estimates

	Number of returns	Percent of returns
Would have been better off claiming the Tuition Deduction	22,469	8

Source: GAO analysis of Statistics of Income data for 2002.

Table 27: Percentage of Apparently Eligible Taxpayers That Claimed the Lifetime Learning Credit but Would Have Been Better off Claiming the Tuition Deduction in 2002: Confidence Intervals

	Number of returns: Lower bound	Number of returns: Upper bound	Percent of returns: Lower bound	Percent of returns: Upper bound
Would have been better off claiming the Tuition Deduction	12,228.08	37,165.3	4.48	13.61

Source: GAO analysis of Statistics of Income data for 2002.

Table 28: Amounts by Which Apparently Eligible Taxpayers Could Have Reduced Their Tax Liability in 2002: Point Estimates

	Tuition deduction produced larger reduction
Median	108.05
Mean	137.68
10th percentile	17.3
25th percentile	36.42
75th percentile	191.55
90th percentile	237.42
Maximum value	456

Source: GAO analysis of Statistics of Income data for 2002.

Table 29: Amounts by Which Apparently Eligible Taxpayers Could Have Reduced Their Tax Liability in 2002: Confidence Intervals

	Deduction produced larger reduction
Median: Lower bound	37.39
Median: Upper bound	190.77
Mean: Lower bound	77.08
Mean: Upper bound	198.28
10th percentile: Lower bound	4.36
10th percentile: Upper bound	41.46
25th percentile: Lower bound	20.16
25th percentile: Upper bound	108.84
75th percentile: Lower bound	107.3
75th percentile: Upper bound	244.85
90th percentile: Lower bound	154.73
90th percentile: Upper bound	350.13

Source: GAO analysis of Statistics of Income data for 2002.

Table 30: Percentage of Apparently Eligible Taxpayers That Claimed a Hope Credit but Would Have Been Better off Claiming a Lifetime Learning Credit in 2002: Point Estimates

	Number of returns	Percent of returns
Total	271,494	100
Would have been better off claiming Lifetime Learning Credit	0	0
All other	271,494	100

Source: GAO analysis of Statistics of Income data for 2002.

Table 31: Percentage of Apparently Eligible Taxpayers That Claimed a Hope Credit but Would Have Been Better off Claiming a Lifetime Learning Credit in 2002: Confidence Intervals

	Number of returns: Lower bound	Number of returns: Upper bound	Percent of returns: Lower bound	Percent of returns: Upper bound
Total	271,491.04	271,494.04	100	100
Would have been better off claiming Lifetime Learning Credit	0	0	0	0
All other	271,491.04	271,494.04	100	100

Source: GAO analysis of Statistics of Income data for 2002.

Table 32: Percentage of Suboptimal Choices Made by Paid Tax Preparers in 2002: Point Estimates

	Taxpayers making suboptimal choice	
	Number of returns	Percent
Total	446,972	100
No preparer	219,139	49.03
Paid preparer	223,011	49.89
IRS prepared/reviewed	0	0
VITA/self help/outreach/elderly assistance	4,822	1.08

Source: GAO analysis of Statistics of Income data for 2002.

Table 33: Percentage of Suboptimal Choices Made by Paid Tax Preparers in 2002: Confidence Intervals

	Taxpayers making suboptimal choice			
	Number of returns: Lower bound	Number of returns: Upper bound	Percent: Lower bound	Percent: Lower bound
Total	392,039	501,905	99.72	100
No preparer	179,777	258,500	42.87	55.19
Paid preparer	184,952	261,070	43.74	56.05
IRS prepared/reviewed	0	0	0	0.28
VITA/self help/outreach/elderly assistance	1,131	9,328	0.26	2.91

Source: GAO analysis of Statistics of Income data for 2002.

GAO's Mission

The Government Accountability Office, the audit, evaluation and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site (www.gao.gov). Each weekday, GAO posts newly released reports, testimony, and correspondence on its Web site. To have GAO e-mail you a list of newly posted products every afternoon, go to www.gao.gov and select "Subscribe to Updates."

Order by Mail or Phone

The first copy of each printed report is free. Additional copies are $2 each. A check or money order should be made out to the Superintendent of Documents. GAO also accepts VISA and Mastercard. Orders for 100 or more copies mailed to a single address are discounted 25 percent. Orders should be sent to:

U.S. Government Accountability Office
441 G Street NW, Room LM
Washington, D.C. 20548

To order by Phone:	Voice:	(202) 512-6000
	TDD:	(202) 512-2537
	Fax:	(202) 512-6061

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Gloria Jarmon, Managing Director, JarmonG@gao.gov (202) 512-4400
U.S. Government Accountability Office, 441 G Street NW, Room 7125
Washington, D.C. 20548

Public Affairs

Paul Anderson, Managing Director, AndersonP1@gao.gov (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, D.C. 20548