

**TESTIMONY OF LINDSAY CLARK, POLICY ANALYST
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**At the Public Hearing on
Bill 17-0235: College Savings Program Increased Tax Benefit Act of 2007
District of Columbia Committee of the Whole
October 9, 2007**

Chairperson Gray and members of the Committee, thank you for the opportunity to speak today. My name is Lindsay Clark, and I am a policy analyst with the DC Fiscal Policy Institute. DCFPI engages in research and public education on the fiscal and economic health of the District of Columbia, with a particular emphasis on policies that affect low- and moderate-income residents.

DCFPI supports the Council's intent to encourage families to save for college; with rapidly escalating college tuition fees, families cannot begin saving too early. However rather than merely expanding the existing deduction, we see this bill as an opportunity to reshape the current tax incentive structure to encourage more low- and moderate-income residents to participate. Specifically, we are asking the Council to consider shifting from a tax deduction model to a tax credit model. Our interest in making this request stems largely from data that show much of the current tax benefit goes to relatively higher-income households, with very limited participation among low- and moderate- income families and those East of the river.

As you can see from the attached tables, in 2005, more than half of the tax benefits went to households with incomes over \$150,000. In contrast, only three percent of residents participating in the program lived in Wards 7 & 8 – a total of 290 households – and they represented less than two percent of all funds invested in DC's college savings plan. Yet, Wards 7 & 8 stand out as the wards with the largest child populations in the District. Some 28 percent of the population of Ward 7 are children, and 36 percent of residents in Ward 8 are children, more than in any other ward in the District.

These data suggest that more needs to be done to encourage low- and moderate- income families across the District to save – or save more – for college. As a first step, we recommend the Council convert the current tax deduction into a refundable tax credit equal to the benefit of the proposed deduction for the highest tax bracket.

This is needed because the current tax deduction actually gives more benefit to higher-income residents than lower-income. Because the tax savings from a deduction is the size of the deduction times your marginal tax rate, a higher-income resident receives a larger savings than a lower-income resident, despite the same positive behavior. Currently, if two residents – one with an income of \$10,000 and the other with an income of \$150,000 – each set aside \$3,000 in savings, the higher

income resident receives a tax savings more than twice as much as the lower-income resident, \$255 vs. \$120. The tables below show the difference in tax savings by income bracket.

Table 4.

Tax Savings from DC's Current Deduction for Contributions to College Savings Plan by Tax Bracket					
Tax Rates and Brackets		Contribution/Deduction		Tax Benefit	
Income Bracket	Tax Rate	Single	Joint	Single	Joint
Under \$10,000	4.0%	\$ 3,000.00	\$ 6,000.00	\$ 120.00	\$ 240.00
\$10,000 to \$40,000	6.0%	\$ 3,000.00	\$ 6,000.00	\$ 180.00	\$ 360.00
Above \$40,000	8.5%	\$ 3,000.00	\$ 6,000.00	\$ 255.00	\$ 510.00

Table 5.

Tax Savings from DC's Proposed Deduction for Contributions to College Savings Plan by Tax Bracket					
Tax Rates and Brackets		Contribution/Deduction		Tax Benefit	
Income Bracket	Tax Rate	Single	Joint	Single	Joint
Under \$10,000	4.0%	\$ 4,000.00	\$ 8,000.00	\$ 160.00	\$ 320.00
\$10,000 to \$40,000	6.0%	\$ 4,000.00	\$ 8,000.00	\$ 240.00	\$ 480.00
Above \$40,000	8.5%	\$ 4,000.00	\$ 8,000.00	\$ 340.00	\$ 680.00

We recommend a tax credit equal to 8.5 percent of contributions up to \$4,000, a maximum credit of \$340. Converting the tax deduction to a tax credit is a more equitable means of distributing the tax benefit because each resident, regardless of income, will see the same dollar value of savings. This also provides a greater incentive for lower-income residents to save. Using the tax credit, both the high-income and low-income resident would receive a tax savings amount of \$340 for a \$4,000 contribution. The Council also could consider making the tax credit as a higher percentage of contributions for lower earners than higher earners, to increase their incentive to save. Additionally, making the tax credit refundable would also ensure residents with no taxable income, after other deductions, could still claim the full benefit through a refundable credit.

As I mentioned, converting the current deduction into a refundable tax credit is one step towards encouraging greater participation of low- and moderate- income families in college savings plans. However, there are several other options that have been or are being implemented in other states to help increase lower-income residents' participation. One such option is to establish and "seed" accounts for low-income families (or all families) when a child is born, with some modest amount of

funds. Maine, for example, began such a program in 2006, offering a one-time \$50 voucher to all newborns in the state. Other states, including Maine, have also started matching programs where the state will match individuals' deposits into 529 college savings plans.

In summary, DCFPI strongly supports the District's objective to encourage residents to save for college, and we'd like to see more low – and moderate- income families across the District taking advantage of the 529 college savings plan. However, we do not believe expanding the current deduction from \$3,000 to \$4,000 is the best way to accomplish this goal. Instead we recommend restructuring the incentives to encourage those who are more disadvantaged to begin saving or saving more.

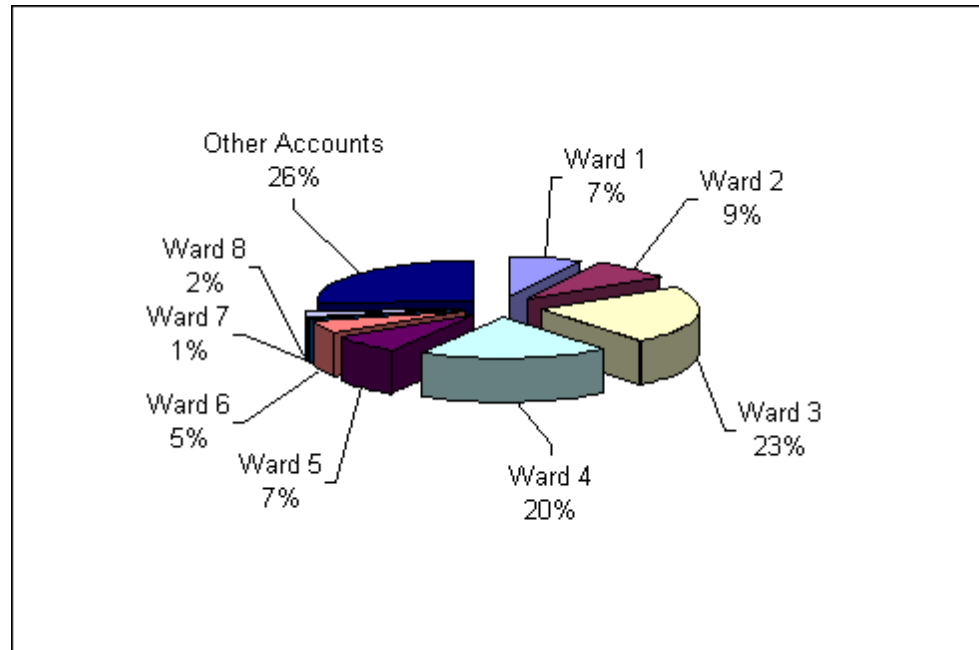
Thank you for the opportunity to speak and I am happy to answer any questions you may have.

Table 1. Number of tax recipients and dollar amounts of DC College Savings Plan Deduction by Adjusted Gross Income Category

Tax Year 2005		
Category of Statistic	DC College Savings Plan Returns	DC College Savings Plan Deduction
Total Returns	1,966	\$7,402,961
Breakeven and Loss	31	\$85,486
\$0.01 Under \$10,000	36	\$84,082
\$10,000 Under \$20,000	42	\$109,465
\$20,000 Under \$30,000	63	\$139,808
\$30,000 Under \$50,000	168	\$371,977
\$50,000 Under \$75,000	177	\$401,691
\$75,000 Under \$100,000	188	\$594,682
\$100,000 Under \$150,000	382	\$1,380,827
\$150,000 Under \$200,000	271	\$1,184,176
\$200,000 Under \$500,000	473	\$2,325,663
\$500,000 Under \$1,000,000	96	\$513,454
\$1,000,000 and Over	39	\$211,650
Source: DC Statistics of Income.		

Table 2.
DC College Savings Plan, July
2007 Management Report, DC vs.
Non DC Accounts by Ward

DC College Savings Accounts:	6,666
Ward 1	664
Ward 2	771
Ward 3	2,082
Ward 4	1,765
Ward 5	625
Ward 6	469
Ward 7	93
Ward 8	197
Other Accounts	2,286
Total	8,952



**Table 3. DC College Savings Plan, July 2007
Management Report, DC vs Non DC Assets By Ward**

DC vs Non DC & Ward	Total Assets	Percent of Total
DC Assets	\$ 68,634,219	72%
Ward 1	\$ 5,579,699	6%
Ward 2	\$ 9,020,970	9%
Ward 3	\$ 26,564,561	28%
Ward 4	\$ 19,523,467	21%
Ward 5	\$ 3,554,223	4%
Ward 6	\$ 3,725,065	4%
Ward 7	\$ 168,520	0%
Ward 8	\$ 497,714	1%
Other Assets	\$ 26,518,311	28%
Total	\$ 95,152,530	100%

