



MODERNIZING FEDERAL TAX CREDITS FOR EMPLOYER EDUCATIONAL ASSISTANCE BENEFITS

Updating tax credits for worker education and talent development under Section 127 can help to address talent-related challenges employers face nationwide

Introduction

Business Champions Supporting Credential Completion is a unique, national partnership made up of senior-level human resources and corporate learning leaders from highly influential companies within diverse industry sectors. We are committed to getting more employers nationwide to invest in ongoing education, training and career advancement support for their employees. As part of our work towards increasing career mobility and education opportunities for America's workforce, Business Champions is advocating for the modernization of tax credits around employer-provided educational assistance. Without more employer investment in their employees' education, America will continue to lag behind other countries in attaining postsecondary credentials and employers will have trouble filling jobs crucial to industry growth.

Issues

There are a range of issues facing the U.S. that impact our competitive edge including our low postsecondary credential attainment levels, employers' complaints about the skill level of our workforce, and the increased cost for pursuing the education and training needed to meet labor market demands.

Low rate of postsecondary credential attainment

The United States' economy is experiencing a widening gap between employer needs and the skills and credentials of the current and emerging workforce. By 2020, 65% of jobs will require a college degree or postsecondary credential.ⁱ The current rate of postsecondary credential attainment for adults ages 25-84 in the U.S. is only at 40%.ⁱⁱ

A 2014 Gallup-Lumina Foundation study of the American public's opinion on higher education reports "a majority (94%) say it is somewhat or very important to increase the proportion of Americans with a degree or professional certificate beyond high school."ⁱⁱⁱ The poll also reports "eight in 10 (80%) U.S. adults agree or strongly agree that colleges and universities need to change to better meet the needs of today's students."^{iv}



The inability to find a talented pool of workers with the right skills to fill these jobs constrains industry growth and hurts our competitive edge. The Organization for Economic Cooperation and Development (OECD) reports that the U.S. continues to lose ground in global postsecondary attainment and is currently ranked in 11th place behind countries including Korea (1st place), Slovenia, Poland, Russian Federation, Slovak Republic, Czech Republic, Canada, Finland, Sweden and Israel.”^v Ranking 12th in the world in the percentage of young adults who attain a college education, the U.S. falls behind other countries such as Korea, Japan and Canada.^{vi}

Difficulty filling job openings

Four out of ten U.S. employers report difficulty filling jobs, reporting the following top five reasons that make it difficult for them to fill open positions in their companies:

- 47% - Lack of technical competencies (hard skills)
- 39% - Lack of workplace competencies (soft skills)
- 36% - Lack of available applicants/no applicants
- 30% - Looking for more pay
- 25% - Lack of experience.^{vii}

Increase in cost of education

As state support for adult education has declined, the cost for students has gone up. According to the U.S. Department of Education, “over the past three decades, average tuition at a public 4-year college has increased by more than 250 percent.”^{viii} The cost of education has influenced the number of adults in the U.S. who pursue a postsecondary education, affecting the United States’ ranking in college education completion. The 2014 Gallup-Lumina Foundation study found that “more than three-quarters (79%) of adults in the U.S. do not think that education beyond high school is affordable for everyone in this country who needs it.”^{ix}

To increase the number of companies that invest in education and training, there need to be more incentives for employers through changes in policy. A 2013 Gallup-Lumina Foundation report on business leaders’ opinions on higher education found that “most leaders (88%) favor an increased level of collaboration with higher education institutions.”^x We need policies that encourage and support increased employer investment, in addition to public and private support.

Obstacles

Business Champions is a group made up of U.S. business leaders who are invested in addressing the shortage of skilled workers on a national level. These national business leaders face similar obstacles when expanding the pipeline of skilled workers within their companies.

Employers want to be able to offer assistance to their employees to promote learning, including both traditional and nontraditional success strategies. Employers have stressed the need to expand awareness of federal policies including, particularly, those that will yield tax credits, currently in place to help employees attain credentials and degrees. For example, employers have asked for clarification of the different types of employer-provided education



assistance that are not taxable to the employee under Section 127 of the Internal Revenue Code. However, even if employers make tuition assistance programs widely available to their workforce, the per employee cap under Section 127 is badly outdated given today's cost of education. It does not offer adequate assistance to employees enrolling in college courses using employer-provided education assistance.

Current policies in place

There are two provisions in the Internal Revenue Code that provide tax incentives and assistance to employees wishing to further their education and training, Sections 127 and 132.

Section 127

Section 127 of the Internal Revenue Code provides that qualified employer-provided educational assistance up to \$5,250 may be exempt from an employee's gross income for purposes of federal taxation. The Internal Revenue Code currently defines "educational assistance" as:

"(A) the payment, by an employer, of expenses incurred by or on behalf of an employee for education of the employee (including, but not limited to, tuition, fees, and similar payments, books, supplies, and equipment), and

(B) the provision, by an employer, of courses of instruction for such employee (including books, supplies, and equipment)." ^{xi}

But Section 127 educational assistance "does not include payment for, or the provision of, tools or supplies which may be retained by the employee after completion of a course of instruction, or meals, lodging, or transportation." ^{xii}

The exemption for employer-provided educational assistance originated in the Internal Revenue Act of 1978 and was continually extended by Congress until 2013 when the provision was made permanent as part of the American Taxpayer Relief Act of 2012. However, the language in Section 127 has not been updated since 1986, when the cap was raised from \$5,000 to \$5,250. In 2015 the cap remains at \$5,250 and does not reflect the higher cost of education today, which has gone up significantly since 1986.

Section 132

To increase the number of working adults with meaningful credentials, there may also be benefit in looking at Section 132, which excludes certain fringe benefits from an employee's gross income including "working condition fringe." Under Section 132, "working condition fringe" is defined as "any property or services provided to an employee of the employer to the extent that, if the employee paid for such property or services, such payment would be allowable as a deduction under section 162 or 167." ^{xiii}

"To be excludable as a working condition fringe benefit, all of the following must apply:

- The benefit must relate to employer’s business
- The employee would have been entitled to an income tax deduction if expense had been paid personally
- The business use must be substantiated with records.”^{xiv}

Unlike Section 127, there is no cap on Section 132.

Changes we need

SECTION 127

Raise the cap of \$5,250 to reflect the current cost of education

The first and only time the cap on Section 127 has been raised was in 1986, and only by \$250. For in-state students enrolled at public four-year colleges and universities during 1986-87, the average annual tuition and required fees was \$1,414.^{xv} For in-state students enrolled full time at public four-year colleges and universities from 2014-15, the average annual tuition and fees is \$9,139.^{xvi} The percent increase in the average annual cost of education for in-state students at a public four-year college/university from 1986 to 2015 is 546.32%. The current cap does not reflect this large increase in education costs.

Include coverage of other learning services

The language of Section 127 does not explain or make clear whether educational assistance includes coverage of strategies that promote success for the working learner, such as Prior Learning Assessment, advising and tutoring.

Prior Learning Assessment (PLA) is the process of earning college credit for college-level learning acquired from other sources, such as work experience, professional training, military training, or open source learning from the web. For the modern-day employee this learning strategy is both cost- and time-efficient, allowing them to further their education and gain the skills necessary to advance in their specific industry. Research by the Council on Adult and Experiential Learning (CAEL) shows that adult students with credit earned through PLA are two-and-a-half times more likely to complete a degree compared to adult students without such credit. These students also had higher persistence rates and a faster time to degree completion. This was true for students regardless of race, ethnicity, age, financial aid status, or gender.^{xvii}

Working with tuition-paying employers since 1984, CAEL has found that many find advising to be a valuable component of their employee learning strategies.^{xviii} CAEL conducted a national survey of 287 employers across multiple industries and found that learning and development advising improves employee performance, creates a pipeline of future talent and improves retention. Specifically, “82% of organizations that offer advising or coaching services [said] it improves employee productivity. 78% of those who track results report[ed] that participants are promoted more often. 88% of those who track results report[ed] that program participants stay with the company longer.”^{xix} Tutoring is another success strategy that offers adult learners individualized attention and support to continue with their learning.

By including these innovative and modern academic programs and services under Section 127, employers would be able to improve the affordability of and access to postsecondary education for their employees.

Include in Section 127 education expenses covered under Section 132

There are permissible education expenses covered under Section 132 that are not clearly permissible under Section 127, including ordinary and necessary travel, meals or lodging. Under Section 132, these expenses are covered only if the benefit relates to an employer's business. Section 127, which is not specifically tied to the employee's current job requirements, needs to also include these expenses as permissible.

Recommendations

Business Champions are interested in modernizing federal tax credits for worker education and talent development under Sections 127 of the Internal Revenue Code. We suggest the following changes in order to update these tax credits and make learning opportunities readily available to adult workers, thereby increasing the number of adult workers with meaningful credentials and helping to address talent-related challenges employers face nationwide.

1) Appoint a taskforce to study the modernization of tax credits

Business Champions recommend appointment of a federal working group or taskforce that would study the modernization of tax credits in order to advise the Treasury Department regarding education and training success strategies that could be included under Sections 127 and 132 of the Internal Revenue Code.

2) Raise the cap of \$5,250 under Section 127

Business Champions recommends that this same task review and recommend an appropriate adjustment of the cap to better reflect the increased cost of education today.

3) Explicitly cover modern learning services under Section 127

Business Champions recommend a clarification of Section 127 allowing for modern learning practices, including the following success strategies that are not currently explicitly covered: advising, tutoring and Prior Learning Assessment.

4) Including coverage of expenses not currently specified under Section 127

Business Champions recommend allowing specific expenses covered under Section 132 to also be covered under Section 127, including permitting education-related expenditures for transportation, lodging or other modern success strategies that are not currently covered under Section 127.



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For more information, or to collaborate with CAEL to advance these ideas, please contact our policy team at cael@cael.org.

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- ^{vi} “College Affordability and Completion: Ensuring a Pathway to Opportunity,” U.S. Department of Education, accessed May 22, 2015, <http://www.ed.gov/college>.
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