

# Education Benefits

Pub 4012 Tab J

Pub 4491 Lesson 22

Video: [Education - AOC](#)

## ■ Interview – Screen for Possible Education Benefits

- Taxpayer (or spouse if MFJ) is a student, even part-time
- Taxpayer has a dependent that is a student in post-secondary study
- If not trained or not comfortable, discuss with your Local Coordinator and decline the return

# ■ Lesson Topics

[Pub 970](#)

- Education benefits general information
- Grants and scholarships
- Education credits
  - American opportunity credit
  - Lifetime learning credit
- Form 1098-T
- Emergency financial aid
- Reducing IRA penalty
- Employer provided education assistance
- Veteran’s education benefits
- Education Savings Bonds
- Recovery of prior year expenses

# ■ Education Benefits

Pub 4012 Tab J

- Different benefits ... different rules for qualifying expenses
- Expense used only once
  - Exception: also use to reduce additional tax on IRA early distribution
- Comprehensive topics
  - Determining the most advantageous education benefit available with unrestricted grants or scholarships using Bogart's calculator
  - Kiddie Tax
  - ESA/QTP/529 plans

## ■ Qualified Education Institution

- Any accredited public, nonprofit, or private post-secondary institution
  - Eligible to participate in Department of Education student aid program
    - College or university
    - Technical, trade or vocational school
    - Exception: for tax-free scholarship, must be accredited, but not necessarily eligible for student aid program

Search for accreditation: <https://ope.ed.gov/accreditation/>

# ■ Qualifying Education Expenses

[Pub 970](#)

- Tuition and fees must be paid to the school as a condition of enrollment
- May include other expenses based on benefit claimed
  - Books, supplies and equipment
  - See Pub 4012, Tab J or Pub 970

# ■ Education Tax Benefits

Pub 4012 Tab J

- Scholarships, grants, education savings account distributions, or employer payments not taxable
- Two possible credits:
  - American Opportunity Credit
  - Lifetime Learning Credit
- Deduction on Schedule C if related to business
  - See *Income – Business* lesson
- Reduce additional tax on IRA early distributions
  - See *Other Taxes* lesson

# ■ Non-Taxable Grants and Scholarships

- Restricted grants and scholarship must be used for tuition and fees (sometimes books) – most common situation
- But... “Pell Grants” are unrestricted
- Not taxable if applied toward qualified education expenses
  - Tuition and fees required for enrollment
  - Required course-related books, supplies and equipment
- and –
- Student is candidate for degree, certificate or other credential

## ■ Taxable Grants and Scholarships

- Grants and scholarships are taxable when
  - Not offset by qualified education expenses
- **or** –
  - When student not degree candidate
- See comprehensive topic on unrestricted grants and scholarships

# ■ Education Credits

[Pub 970](#)

- American Opportunity Credit (AOC) – designed to cover first four years of college or vocational school
- Lifetime Learning Credit – designed to cover lifetime
- Claim only one education credit per year per student
  - Either AOC **or** Lifetime Learning Credit

## ■ Rules for Both Credits

- Student must be taxpayer, spouse, or dependent
  - Student who could be claimed as a dependent but is not claimed as a dependent can claim the credit
- Form 1098-T generally required to claim either AOC or Lifetime Learning Credit
  - Unless school is not required to issue Form 1098-T
    - Taxpayer provides school's FEIN and expense information

## ■ Rules for Both Credits

- Student must be enrolled in eligible post-secondary school
- Taxpayer cannot file Married Filing Separately (MFS)
- Taxpayer cannot treat spouse as nonresident alien
- Taxpayer's AGI must be below phase-out limit for their filing status

## ■ Qualified Expenses for Both Credits

- Tuition and certain related expenses required for enrollment or attendance
- Student activity fees paid to institution as condition of enrollment or attendance
- Insurance and parking are **not** qualifying expenses

## ■ Qualified Expenses for Both Credits

- Expenses **paid in 2021** for academic period beginning 2021 or first 3 months of 2022
- Expenses paid by student considered paid by taxpayer
- Expenses paid by 3rd party treated as paid by student

# ■ American Opportunity Credit Calculation

- AOC up to \$2,500 per **student**
  - 100% of first \$2,000 of expenses
  - 25% of second \$2,000 of expenses
- 40% AOC refundable credit for most taxpayers
  - Up to \$1,000 per student

## ■ AOC Calculation

- Refundable portion of AOC **not** available to taxpayers
  - Under 18 end of tax year – **or** –
  - 18 and earned income less than half their own support\* – **or** –
  - Full-time students over 18 and under 24 with earned income less than half their own support\*
- **and** –
  - One parent alive at the end of tax year – **and** –
  - Not filing MFJ

\* It is not required that the earned income be used for the student's support – just that the student earns that amount or more

## ■ AOC Requirements

- Must not have completed four years of academic credits (as determined by the school) by the beginning of the tax year
- Limited to four tax years
- Student must be candidate for degree, credential or certificate
- Income phase outs starting at \$80,000 (\$160,000 MFJ)
- Enrolled at least half-time for at least one term during tax year set by institution
- Student has no felony drug convictions

# ■ AOC Qualified Expenses

- Course-related books, supplies and equipment
  - Purchased from any source
  - Computers are AOC expense when needed to
    - Receive assignments
    - Post assignments
    - Collaborate with other students on group assignments
    - Receive grades
- Taxpayers should keep
  - Receipts
  - Documentation of computer or internet requirements
    - Example: course syllabus

## ■ Lifetime Learning Credit

- Up to \$2,000 per student per year
  - 20% of first \$10,000 of expenses
- Nonrefundable credit
- Felony drug conviction not a disqualifier

# ■ Lifetime Learning Credit

New

- No limit to number of years available
- No minimum amount of course workload
- No degree requirement
  - If not toward a degree, must be to acquire or improve job skills
- Starting in 2021, phaseout begins with MAGI greater than \$80,000 (\$160,000 MFJ)

# ■ Lifetime Learning Credit Qualified Expenses

- Tuition and fees
- Books and equipment if must be purchased from school as a condition of enrollment
  - Common with trade, apprentice, and other vocational schools

# Quiz

Education Credits

## ■ Education Credits Quiz – Part 1

Jim and May Brown's AGI for 2021 is \$48,000. They claim their two children as dependents; Rose, 21, a full-time college sophomore and John, 23, a 4th year full-time college senior.

The Browns made tuition payments of \$6,000 in August for 2021 classes and \$6,000 in December for term starting in January 2022.

For which education credits do they qualify?

**American Opportunity for both children**

## ■ Education Credits Quiz – Part 2

Can the Browns include the payments they made in December for the 2022 term on their 2021 tax return?

**Yes, payments for terms starting in the first 3 months of the following year are allowed**

## ■ Education Credits Quiz – Part 3

If Rose had paid for her own tuition, how would the answer differ?

**No difference, unless Rose not claimed as dependent**

## ■ Education Credits Quiz – Part 4

If Jim and May had not claimed Rose as a dependent, even though entitled, who is entitled to the credit?

**Rose is entitled to the nonrefundable credit, but not the refundable portion of the credit (student between the ages of 18-24 with no earned income, at least one living parent, and not filing MFJ)**

## ■ Education Credits Quiz – Part 5

If Rose attended only  $\frac{3}{4}$  time and earned \$5,000 at a part-time job, who is entitled to the credit?

**Rose is no longer a dependent (must be full-time student or have income under \$4,300). She is entitled to the nonrefundable credit, but not the refundable portion of the credit (student between the ages of 18-24 with earned income less than  $\frac{1}{2}$  her total support, at least one living parent, and not filing MFJ)**

## ■ Form 1098-T

- Form 1098-T issued by education institution provides
  - Amount paid (should no longer be amount billed)
  - Student status
  - Scholarship or grant amount
- Must have 1098-T to claim AOC or Lifetime Learning Credit, unless school is not required to issue one
- If adjustment needed (box 4 or 6) – return is **out of scope**

## ■ Form 1098-T

- Form 1098-T amounts **must** be verified with taxpayer
  - Best source student's statement of account with school
  - Usually available online

# Form 1098-T

<input type="checkbox"/> CORRECTED (if checked)		<b>Grants and Scholarships: Box 5</b>		<b>Tuition Statement</b>
FILER'S name Street address City or town, state or province, country, ZIP or Foreign Postal Code Telephone number <div style="text-align: center; font-size: 1.2em; font-weight: bold;">Total Paid: Box 1</div>		1 Payments received for qualified tuition and related expenses  2	OMB No. 1545-1574  <div style="font-size: 2em; font-weight: bold;">20XX</div>  Form 1098-T	
FILER'S employer identification no.	STUDENT'S TIN	3		<b>Copy B For Student</b>  This is important tax information and is being furnished to the IRS. This form must be used to complete Form 8863 to claim education credits. Give it to the tax preparer or use it to prepare the tax return.
STUDENT'S name Street address (including apt. no.) City or town, state or province, country, ZIP or Foreign Postal Code <div style="text-align: center; font-weight: bold; color: red;">Boxes 4 and 6 Out of Scope →</div>		4 Adjustments made for a prior year  6 Adjustments to scholarships or grants for a prior year	5 Scholarships or grants  7 Checked if the amount in box 1 or 2 includes amounts for an academic period beginning January-March 20XX+1. <input type="checkbox"/>	
Service Provider/Acct No. (see instr.)	8. Checked if at least half-time student <input type="checkbox"/>	9 Checked if a graduate student <input type="checkbox"/>	10 Ins. contract reimb./refund	
Form 1098-T		<b>Status Indicators: Boxes 8 and 9</b>		

# Higher Education Emergency Financial Aid Grants

New

- School grant under the CARES Act for unexpected expenses, unmet financial need, or expenses related to the disruption of campus operations on account of the COVID-19 pandemic
  - Food, housing, course materials, technology, health care, or childcare
- Not includible in gross income
- Does **not** reduce expenses for either education credit
- Need to analyze student's financial account
- <https://www.irs.gov/newsroom/higher-education-emergency-grants-frequently-asked-questions>

## ■ Reduce Additional Tax on IRA Early Distribution

- Higher education costs qualify for exception to 10% additional tax
  - Including **room and board** if enrolled at least half-time
- Education expenses still available for credit or deduction
- See *Other Taxes* lesson

# ■ Employer-Provided Educational Assistance

- Employers can provide up to \$5,250 of tax-free educational assistance to employees
  - Should not be included on W-2
  - Should not be reported on tax return
  - Qualified education expenses applied toward employer-provided assistance cannot be used for any other educational benefit
- Tax-free employer benefit can apply toward student loan instead!
  - Through tax year 2025

## ■ Veterans' Educational Assistance

- Should not be included on W-2
- Should not be reported on tax return
- Expenses paid with VA education assistance cannot be used for any other educational benefit

# ■ Education Savings Bond Program

[Pub 970](#)

- Exempts interest income on savings bonds used for qualified education expenses
- **Out of scope**

# ■ Recovery of Prior Year's Expenses

- Refund of education expense claimed in a **prior year**
  - Claimed as credit
    - May need to recapture – **out of scope**
  - Claimed as an adjustment or deduction
    - May need to include recovery in income
    - See Bogart recovery calculator

## ■ Review of Education Benefits

- Complete federal and state returns prior to considering education expenses
- Education credits and adjustment
  - American Opportunity Credit – usually first 4 years
  - Lifetime Learning Credit – for rest of your life
- Student can choose to pay tax on unrestricted grants
  - Frees up expenses for education credit
  - See comprehensive topic

## ■ Review of Education Benefits

- Schedule C expense reduces self-employment tax and may be better (not able to optimize in Bogart calculator)
- Let the taxpayer and student decide
  - Where to claim expenses
  - Whether to declare grant or scholarship as taxable
- Taxable scholarship entered on student return
- Credit entered on parent return when parent claiming student

## ■ Education Benefits





Comp

# Education Benefits

Comprehensive topics

- Student can choose to pay tax on unrestricted grants
  - Excess over qualified expenses is always taxable
  - Rest can be allocated to living expenses
  - Qualified expenses are then paid from other funds
    - Making them eligible for the education credits
  - It does not matter how scholarship/grant funds were actually used
    - Student can reallocate them after the fact

# Bogart Education Calculator

- Use Bogart education calculator:
  - [https://cotaxaide.org/tools/Education Calculator.html](https://cotaxaide.org/tools/Education%20Calculator.html)
  - [Video tour \(22 min\)](#) – upper left-hand of front page
  - Use Optimizer tab to calculate most advantageous benefit
- Highly Recommended:
  - NTTC Video: [Education Vincent 1](#)
  - NTTC Workbook Comprehensive Exercise:
    - Van Vincent

# Kiddie Tax (Form 8615) – Out Of Scope

- Kiddie tax applies and the return is Out of Scope if both situations apply:
  1. The dependent has over \$2,200 in unearned income that includes taxable scholarship income
  2. The dependent has a filing requirement when earned income includes taxable scholarship income

# Coverdell Education Savings Account (ESA)

- Contribute up to \$2,000 per year per individual
  - AGI phase-out limitation (\$110,000 or \$220,000 if MFJ)
- Contributions not deductible – **and** –
- Distributions not taxable when used for qualified educational expenses
  - Distribution reported on 1099-Q
  - If distribution greater than education expenses – **out of scope**

# ESA Qualifying Expenses

- Tuition and fees required for enrollment
- Books, supplies and equipment required for enrollment
- Expenses for special needs services
- **Room and board** if enrolled at least half-time

## Qualifying Tuition Program (QTP)

- Also called Section 529 plans
- Contribution amount limited to the amount necessary for qualified education
- No AGI phase-out limitations
- Can contribute to QTP and ESA in the same year

# QTP/529 Qualifying Expenses

- Tuition and fees required for enrollment
- Books, supplies and equipment used by beneficiary
- Expenses for special needs services
- **Room and board** if student at least half-time
- Up to \$10,000 per year can be distributed for elementary or secondary school tuition

## Expansion of QTP/529 Plan Qualified Distributions

- Distributions allowed to pay beneficiary or sibling student loan principal or interest
  - Lifetime limit \$10,000
  - Interest repaid is not eligible for student loan interest deduction
- Distributions allowed to pay for apprenticeship programs registered and certified by U.S Department of Labor
  - Qualified expenses include books, fees, supplies and equipment
- Applies to distributions after December 31, 2018

# Forms 1099-Q and 1099-QA

- ESA/QTP distributions are reported on Form 1099-Q
  - Not taxable when used for qualified educational expenses
  - If distribution greater than education expenses – **out of scope**
  
- Similar form 1099-QA used for distributions from ABLE accounts (for persons with disabilities)
  - Same rules apply – not taxable if used for qualified expense
  - **Out of scope** otherwise

[Pub 907](#)

## ■ Education Benefits



**Questions?**

**Comments?**