Education Benefits

Introduction

This lesson covers tax benefits available to help a taxpayer offset the costs of higher education by reducing the amount of income tax. This lesson suggests probing questions you can ask based on the intake and interview sheet, the Volunteer Resource Guide, Education Benefits Tab J and on the rules for claiming education benefits.

During the interview, ask taxpayers if they are aware of the education benefits and give a brief description. Next, gather information to determine which benefits can be claimed

After the return is otherwise completed (both federal and state), compare the effects of using the different benefits so the taxpayer can decide which ones he or she will chose to use.

Objectives

At the end of this lesson, using your resource materials, you will be able to:

• Determine which education benefits the taxpayer can claim

• Compare the effects of different benefits for the taxpayer

What are education benefits?

Education benefits are amounts that will increase the refund or reduce the amount of tax due. The amount is based on qualified education expenses that the taxpayer paid during the tax year. Most benefits apply only to post-secondary education.

There are several education benefits—see the *Highlights of Education Tax Benefits* in Tab J of the Resource Guide. Some of the benefits reduce AGI; some reduce the tax; and one is a refundable credit. The most common benefits seen at VITA/TCE sites are tax-free scholarship or grants, an adjustment for tuition and fees, and two education credits (American opportunity and lifetime learning). You may wish to highlight these four benefits in your Resource Guide.

Do all the different benefits use the same rules and definitions?

No, each benefit was established by a different Congress, which may have used identical terms to refer to different things. It is important to refer to the chart in the Resource Guide when you are working with education benefits and use the definitions that apply to the benefit you are considering. In particular, the definition of "qualifying education expenses" varies considerably from benefit to benefit.

Whose expenses qualify?

- For the most common benefits the student must be the taxpayer, the spouse or a dependent whose exemption is being claimed on the return.
- For both education credits (American opportunity and lifetime learning):
  - if the student is not claimed on someone else's return as a dependent (even though he or she could be), then the student may be able to claim the credit on his or her own return
  - expenses paid by others, e.g. grandparents, are deemed paid by the student; and if the student is a dependent, the expenses are deemed paid by the taxpayer claiming the student as a dependent.
- For the other benefits, the definition of a qualifying student is included in the descriptions below.

What are the rules that are the same?

> **CAUTION**
>
> The taxpayer and the student must have valid social security numbers or ITINs by the due date of the return to claim either credit or the tuition and fees deduction.

Some of the definitions are the same for most or all of the benefits. Two that are the same are the definition of candidate for a degree and eligible educational institution.

Who is a candidate for a degree?

Several of the education benefits require that the student be a "candidate for a degree" or be "pursuing a degree." The student meets this requirement if he or she attends a primary or secondary school, is pursuing a degree at a college or university, or is pursuing a credential for gainful employment in a recognized occupation. The school must be eligible to participate in the federal student aid program. This generally includes any accredited public, nonprofit or proprietary (privately owned profit-making) college, university, vocational school or other postsecondary educational institution.

What is an eligible institution?

For most education benefits, an eligible institution is any college, university, vocational school or other postsecondary educational institution eligible to participate in a student aid program administered by the U.S. Department of Education. The school should be able to tell the student if it is an eligible education institution. To search all accredited schools, go to https://fafsa.ed.gov/FAFSA/app/schoolsearch. If the student receives a Form 1098-T, you can assume that the school is an eligible institution. Beginning with tax year 2017, if the school did not send a Form 1098-T, the student is not eligible to claim the American opportunity credit, the lifetime learning credit, or the tuition and fees adjustment.

What are the education benefits and how do they differ?

Tax-free scholarship or grant

Scholarships or grants that are not based on work can be tax-free if all the following are true. If they are tax-free, they are not entered on the tax return.

- Student must be a candidate for a degree.
- School may be primary, secondary or post-secondary college, university or vocational school.
- They must be spent on tuition and fees required to enroll at, or attend, an eligible education institution; or on course-related expenses, such as fees, books or supplies and equipment that are required for the courses. These items must be required of all students in the course of instruction.
- If the scholarship or grant exceeds the qualifying expenses, a portion of the grant will be taxable. Use the following worksheet to calculate the minimum taxable amount. If the student is not a candidate for a degree, the entire scholarship or grant is taxable.

Grants and scholarships			____________	A
Tuition and fees	____________	B		
Books and supplies	+ ____________	C		
Total qualifying expenses			- ____________	B+C
Minimum taxable grant or scholarship			____________	A-(B+C)

American opportunity credit (AOC)

This credit is designed to help students in the first four years of post-secondary school.

- Taxpayer cannot file married filing separately.
- AOC or Hope credit cannot be claimed for a particular student in more than four tax years.
- Student cannot have completed four years' of post-secondary education before the beginning of the tax year as determined by the school.
- Student must be enrolled at least half-time for one term during the year.
- Student must be a candidate for a degree.
- Student cannot have a felony drug conviction before the end of the tax year.
- Qualifying expenses include tuition, fees, required books, supplies and equipment. Sports or hobby-type expenses are allowed only if such course or other education is part of the student's degree program. Non-academic fees are not included.
- Qualifying expenses paid by others are deemed paid by the taxpayer claiming the credit.
- Credit is calculated for each student. It is 100% of first $2,000 of expenses + 25% of second $2,000 of expenses. It is calculated on Form 8863.
- 40% of credit is refundable.
- Refundable part of the credit is disallowed if taxpayer/student is over age 18 and under age 24 unless he or she:
  - a) had earned income in excess of 50% of his or her total support,
  - b) was **not** a full-time student for parts of at least 5 months of the year,
  - c) is an orphan as of the end of the year (no surviving parent) or
  - d) is married filing a joint return.
  - – Refundable part of the credit is disallowed to the student/taxpayer if he or she is under age 18 unless c) **or** d) applies
  - – Refundable part of the credit is disallowed to student/taxpayer age 18 unless a), c) **or** d) applies.
- Credit is phased out for income between $80,000 - $90,000 ($160,000 - $180,000 for joint returns).

TIP
It is not required that the student spend their income on their support – just that he or she has enough earned income.

Lifetime learning credit (LLC)

- Taxpayer cannot file married filing separately.
- Qualifying expenses include tuition and fees. If required books or materials must be purchased from the school as a condition of enrollment, they may also be included. This occurs most often with vocational schools. Sports or hobby-type expenses are allowed only if such course or other education is part of the student's degree program. Non-academic fees are not included.
- Qualifying expenses paid by others are deemed paid by the taxpayer claiming the credit.
- Student does not need to be a candidate for a degree
- Available for all years of postsecondary education and for courses to acquire or improve job skills.
- Credit is 20% of first $10,000 of expenses per return and is calculated on Form 8863.
- Credit is phased out for income between $55,000 - $65,000 ($111,000 - $130,000 for joint returns).

Tuition and fees adjustment (T&F)

- Taxpayer cannot file married filing separately.
- If taxpayer could be claimed as a dependent on someone else's return (whether or not he or she is claimed), he or she cannot claim the adjustment.
- Qualifying expenses include tuition and fees. Books or other materials that must be purchased from the school as a condition of enrollment may also be included. This occurs most often with vocational schools.

TIP
Since the tuition and fees adjustment reduces AGI, you may want to consider applying expenses here when there is EIC, premium tax credit, shared responsibility payment or retirement savers credit that will be affected.

- Qualifying expenses must be paid by the taxpayer claiming the tuition and fees adjustment.
- Qualifying expenses of a dependent paid by others **directly to the school** are deemed paid by the student.
- Qualifying expenses paid by the student or deemed paid by the student can be claimed by the student only if he or she is not a dependent of another taxpayer.
- Student does not need to be a candidate for a degree.
- Available for all years of postsecondary education.
- Adjustment is first $4,000 of expenses per return and is entered on Form 8917. Credit is phased out for income between $60,000 - $80,000 ($120,000 - $160,000 for joint returns).

Education exception to additional tax on early IRA distribution

- If education expenses are not paid with tax-free income, they can reduce the amount upon which the additional tax is calculated.
- The student must be the taxpayer, the spouse or a child (natural, foster or adopted) or a descendent of any of them—it is not required that he or she be claimed as a dependent.
- Qualifying expenses are extensive and are listed in the chart in the Resource Guide. Room and board (or living off campus—even at home) is included if the student attends at least half-time.

- **Unlike the other benefits, expenses may be used toward this exception and also used toward another education benefit.**

Coverdell Education Savings Accounts (ESA) and Qualified Tuition Programs (QTP)

- These are special accounts that have been set up to pay education expenses. The earnings are tax-free if the distributions are spent for qualifying expenses. Distributions are reported on Form 1099-Q.
- If the distributions exceed qualifying education expenses, the return is out of scope.
- Qualifying expenses are extensive and are listed in the chart in the Resource Guide. They include room and board if the student attends at least half-time. This includes expenses of living off campus—even at home. Coverdell distributions can be used for K-12 expenses as well as post-secondary education.
- Benefit for Coverdell ESA distribution is phased out if income exceeds $95,000 - $110,000 ($190,000 - $220,000 for joint returns). There is no phase out for QTP distributions.
- If distributions are used to pay qualifying expenses, neither the distributions nor the expenses show on the tax return.

Education Savings Bond Program—out of scope

Interest on some U.S. savings bonds is not taxable if used for education expenses. This is out of scope.

Employer-provided educational assistance

Employers may provide up to $5,250 of tax-free payments or reimbursements for an employee's education expenses. None of these payments or the expenses will be shown on the tax return. Expenses that exceed the employer payments can be used toward other benefits. See Pub 970 Chapter 11 for more information.

Veterans' education benefit

If the student qualifies for one or more VA education benefits, the payments are not included on his or her tax return, but he or she must reduce the amount of education expenses qualifying for an education tax benefit by his or her VA payments. This applies only to the part of his or her VA payments that is required to be used for education expenses.

Business or work-related deduction

The taxpayer can deduct the costs of qualifying work-related education as a business expense. This is education that meets at least one of the following two tests.

- The education is required by his or her employer or the law to keep his or her present salary, status or job. The required education must serve a bona fide business purpose of his or her or the employer's business.
- The education maintains or improves skills needed in his or her present work.

However, even if the education meets one or both of the above tests, it isn't qualifying work-related education if it:

- Is needed to meet the minimum educational requirements of his or her present trade or business or

- Is part of a program of study that will qualify him or her for a new trade or business.

The taxpayer can deduct the costs of qualifying work-related education as a business expense even if the education could lead to a degree.

For business or work-related deductions the student must be the taxpayer or spouse. If he or she is self-employed, deduct the expenses on Schedule C or C-EZ. If he or she is an employee, deduct the expenses on Schedule A.

Educator Expenses

Professional development expenses can now be claimed as part of the educator expense adjustment to gross income. The maximum educator expense amount is small, up to $250 per educator; but, may be helpful in situations where AGI affects other items.

Can more than one benefit be used for the same student?

- The AOC, LLC and T&F are mutually exclusive. If a student uses any one of them then he or she cannot claim or be claimed for either of the others. However, the other education benefits can be used if there are unused expenses.

Example

Miron and Carey claim their two children as dependents on their joint return. Both children are full-time college students, and Miron also took a college class to further his career. Their joint return can claim the American opportunity credit for each child and also claim the lifetime learning credit for Miron's course.

Generally, any expense can be used only once. The exception to that rule is the education exception to additional tax on early IRA distributions. Expenses can be used to reduce the additional tax and also be used toward another benefit unless the expenses were paid with tax-free educational assistance (tax-free grants or scholarships, veterans' benefits, etc.)

Example

Pete spent $8,500 on college tuition to improve his job skills in his current job. He received $4,500 in VA benefits toward the tuition. His unused $4,000 of qualified education expenses can be used toward an education credit or other benefit, if he meets the requirements.

If a student qualifies for more than one benefit, how do I decide which is better?

- Complete the rest of the federal and the state tax returns.
- Use the trial and comparison method. Enter the expenses toward the first benefit and record the resulting tax due or refund for both the federal and state returns. Remove the expenses from that benefit and try the next. Record the resulting refund amounts. Repeat for each benefit that applies.
- Here is one way to display the results. You would complete only the columns that apply.

	A Use Tax-free Scholarship, Excess Expense to AOTC	B Use Tax-free Scholarship, Excess Expense to LLC	C Use Tax-free Scholarship, Excess Expense to T&F	D Up to $2,000 of Expense for AOTC	E Up to $4,000 of Expenses for AOTC	F Up to $10,000 of Expenses for LLC	G Up to $4,000 of Expenses for T&F	H Eliminate Filing Requirement
Student's Return								
Taxable Scholarship								
AGI								
Federal refund								
State refund								
Total refund								
Parents' Return								
AGI								
Federal refund								
State refund								
Total refund								
TOTAL refund for both returns								

Why would a student want to pay tax on the grants or scholarships?

The grant or scholarship is taxable to the student—who may not be the taxpayer—so the tax on the scholarship or grant would generally be no more than 10% or 15%. The American opportunity credit is 100% of the first $2,000 and 25% of the second $2,000. Even the lifetime learning credit is 20% of the first $10, 000. So, the credit is often larger than the additional tax.

Example

Juan, a student, receives a grant exactly equal to his qualifying education expenses. He otherwise has no filing requirement. He has $5,000 from a summer job, $100 federal withholding, $3,000 education expenses and a $3,000 Pell grant. Juan's parents file a return claiming Juan as a dependent and showing income that is within the allowable range for the American opportunity credit (AOC).

In Scenario A, Juan uses the grant to pay the education expenses. Neither shows up on his tax return or his parents' return. Juan has no filing requirement and files only to get his withholding (from his summer job) back. His parents claim no education benefits for Juan.

Gross income = $5,000, no filing requirement, tax = 0, refund = $100.

In Scenario B, Juan chooses to declare $2,000 of the grant as taxable and his parents use the education expenses toward the AOC.

Juan's gross income is $5,000 + $2,000 = $7,000. As a dependent, Juan has a filing requirement. His taxable income is $7,000 - $6,300 = $700. At 10%, his tax is $70 reducing his refund to $30.

His parents claim Juan and the AOC is 100% of $2,000. Parents take a $2,000 tax credit and the family is net ahead by $1,930 (parents $2,000 less Juan's $70).

Note that for the kiddie tax, Juan's unearned income is $2,000, which is below the $2,100 kiddie tax threshold.

Example (Cont.)

In Scenario C, Juan chooses to show the whole grant as taxable and his parents use all the education expenses toward the AOC.

Juan's gross income is $5,000 + $3,000 = $8,000. As a dependent, Juan has a filing requirement and unearned income (the taxable scholarship) over $2,100. The kiddie tax applies and his return is out of scope. His taxable income is $8,000 - $6,300 = $1,700. Juan's tax will depend on his parents' tax bracket. If his parents' tax bracket is the same or less than Juan's rate, Juan's tax will be based on his own income. Assuming that is the situation here, at 10%, Juan's tax is $170 and he owes $70.

His parents claim AOC of $2,250 (100% of $2,000 plus 25% of $1,000). Parents take a $2,250 tax credit and might be willing to pay Juan's $70 tax bill. The family is net ahead by $2,080 (parents' $2,250 less Juan's $170), but Juan's return **cannot** be prepared at the volunteer site.

In Scenario D, Juan chooses to show $2,100 of the grant as taxable and his parents use that amount toward the AOC.

Juan's gross income is $5,000 +$2,100 = $7,100. He still has a filing requirement, but the kiddie tax does **not** apply. His tax is 10% on $800 of taxable income = $80. His refund is now $20.

His parents claim AOC of $2,025 (100% of $2,000 plus 25% of $100). The family is net ahead by $1,945 (parents' $2,025 less Juan's $80). Not as good as scenario C by $55, but both returns remain in scope.

Why would a student <u>not</u> want to pay tax on the grants or scholarships?

- Sometimes adding taxable scholarships or grants can create a filing requirement for a dependent student who wouldn't otherwise have one. If the parents have a premium tax credit (PTC) or shared responsibility payment (SRP) that depends on the family's total income (including the income of dependents with filing requirements), it might be better if the student has no filing requirement.
- If the student has a filing requirement and unearned income (including the taxable scholarship) over $2,100, the kiddie tax may apply and the student's return will be out-of-scope. There are exceptions, so if the student is not subject to the kiddie tax, the return remains in scope. The parents' return will still be in scope generally.
- If the student is not a dependent and has PTC or SRP, the negative effect on the PTC or SRP may be greater than the positive effect on the education credit.
- Sometimes, the student has a child and qualifies for earned income credit. In that case, additional scholarship income may reduce his EIC more than it increases the education credit. The only way to know is to try it each way.

What are the unusual but important questions I need to ask?

- Was the education related to self-employment business? Expenses not used in any of the three stand-alone benefits can be used on Schedule C if it's a normal expense of the business.
- Was the education needed to improve skills for current employment? Expenses not used in any of the three stand-alone benefits can be used on Schedule A Line 23.
- Were the expenses paid by Veterans' Education Benefits? Neither the income nor the expenses will be shown on the tax return.
- Were the expenses paid by an employer's education program? Up to $5,250 can be paid or reimbursed by an employer. None of these expenses will be shown on the tax return. If expenses exceed employer payments, the excess can be shown.
- Were the expenses paid by distributions from a Coverdell or QTP (Form 1099-Q)? If the total distribution is used to pay qualifying expenses (including room and board for a student who is attending more than half-time) then those expenses and the distribution do not show on the return. If taxpayer chooses to pay tax on some of the distribution so the expenses can be used elsewhere, then the return is out of scope.
- Were the expenses paid by a third party? The expenses are allowed for the American opportunity or lifetime learning credit so long as the student is the taxpayer, spouse or dependent. These expenses are allowable for all other benefits only if the student is the taxpayer or spouse.

What's Form 1098-T?

Form 1098-T is sent to the student from the eligible educational institution. Beginning tax year 2017 (delayed by IRS), if the institution does not submit Form 1098-T to the IRS, the student or taxpayer cannot claim the American opportunity credit, the lifetime learning credit or the tuition and fees deduction.

Form 1098-T usually shows the amounts billed by the school, amount of scholarships or grants received, whether the student was enrolled at least half-time, whether he or she was a graduate student. The amount billed is not very useful as the benefits are based on the amount actually paid during the tax year.

☐ CORRECTED

FILER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone number	1 Payments received for qualified tuition and related expenses $ 2	OMB No. 1545-1574 2016 Form 1098-T	Tuition Statement
FILER'S federal identification no. / STUDENT'S taxpayer identification no.	3 If this box is checked, your educational institution has changed its reporting method for 2016 ☐		Copy B For Student
STUDENT'S name	4 Adjustments made for a prior year $	5 Scholarships or grants $	This is important tax information and is being furnished to the Internal Revenue Service. 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.
Street address (including apt. no.) City or town, state or province, country, and ZIP or foreign postal code	6 Adjustments to scholarships or grants for a prior year $	7 Checked if the amount in box 1 or 2 includes amounts for an academic period beginning January – March 2017 ▶ ☐	
Service Provider/Acct. No. (see instr.) / 8 Check if at least half-time student ☐	9 Checked if a graduate student . . . . ☐	10 Ins. contract reimb./refund $	

Form **1098-T** (keep for your records) www.irs.gov/form1098t Department of the Treasury - Internal Revenue Service

Where can I find better information?

Most schools provide student account statements on-line. If the student is at the site, he or she can generally log onto the school's website and print out the student account for each term of the tax year. Use only the expenses paid during the tax year. Student loans should be treated as paid by the student or the taxpayer—depending on who is liable for the loan—on the date the funds are posted to the account.

Sometimes, the student is not with the parents at the tax site. The student may be able to e-mail them the statement or give them the log-in information.

> **TIP**
> In addition to the amounts that show on the student statement, include amounts paid to third parties for qualifying expenses, such as books purchased online.

How do I start?

1. Complete the rest of the tax return, both federal and state.
2. Verify that the student is the taxpayer, spouse or a dependent. Among other tests, to be a qualifying child the student must be a full-time student for at least five months if over age 18 and under age 24, or, to be a qualifying relative, his or her income must be under the exemption amount.
3. Look at the student's Form 1098-T. This will show the amounts billed by the school, whether the student was at least half-time, whether he or she was a graduate student and the amount of any grants or scholarships he or she received. Use the student's financial account statement to verify that the amounts billed were actually paid during the tax year.

> **TIP**
> When the student is a qualifying child of (for example) the parents and the student is not eligible for the refundable part of the AOC, the parents will need to file a return to claim the refundable portion of the AOC, even though they may not otherwise need to file a return.

4. Determine if the student received any unrestricted scholarships or grants (such as a Pell Grant). If there were no scholarships or grants or if they were all restricted to tuition and books, then the return is fairly straight-forward and you can proceed.

Example

LaToya is a student who meets the qualifications for the American opportunity credit and receives a 1098-T. The student statement shows paid tuition and fees for $5,240, health fee for $11 and a parking fee for $150. The statement shows a Stafford loan for $6,000 and a $500 music scholarship. LaToya paid $189 cash for books at a local bookstore. This summarizes a possible result:

Tuition	$5,240	
Books	189	
Qualifying expenses	$5,429	
Less restricted scholarship	-500	
Adjusted qualifying expenses		$4,929
Apply toward American opportunity credit (or toward tuition and fees deduction)		4,000
Remaining expenses		$ 929

Enter $4,000 on Form 8863. If LaToya is her parents' dependent, enter it on the parents' return.

What do I do if there are unrestricted scholarships or grants?

Determine the amount of the allowable expenses for the benefit being considered. Subtract any **restricted** scholarships (which are now tax free and are not included on the tax return) and enter the remainder of the expenses toward the selected benefit (usually the American opportunity credit). If these expenses are more than $4,000, use the excess to reduce the taxable scholarship.

Example (cont.)

Same as above plus LaToya also received an unrestricted grant of $5,400.

Tuition	$5,240	
Books	189	
Qualifying expenses	$5,429	
Less restricted scholarship	-500	
Adjusted qualifying expenses		$4,929
Apply toward American opportunity credit (or tuition and fees deduction)		4,000
Remaining expenses		$ 929
Unrestricted grant	$5,400	
Less remaining expenses	929	
Taxable grant	$4,471	

Enter $4,000 on Form 8863. If LaToya is a dependent, enter it on the parents' return. Enter $4,471 as a taxable scholarship or grant on LaToya's return.

Should I always apply all the expenses toward the credit?

There are many situations where the additional credit is not worth the effects of the increased AGI from showing the scholarship as taxable. The amount you apply toward the credit is flexible, but the optimum usually occurs (for the AOC) with zero credit, $2,000 of expenses toward the credit or $4,000 of expenses toward the credit. The following example shows how the taxable scholarship amount is calculated in each case.

Example (cont.)

Same as above plus LaToya also received an unrestricted grant of $5,400.

Alternative:		A	B	C
Tuition	$5,240			
Books	189			
Qualifying expenses	$5,429			
Less restricted scholarship	-500			
Adjusted qualifying expenses		$4,929	$4,929	$4,929
Apply toward American opportunity credit		0	2,000	4,000
Remaining expenses to reduce taxable grant		$4,929	$2,929	$ 929
Unrestricted grant		$5,400	$5,400	$5,400
Less remaining expenses		4,929	2,929	929
Taxable grant		$ 471	$2,471	$4,471

What expenses should I include for the current tax year?

Do include qualified education expenses (as defined for the benefit you are testing) that were paid during the current tax year for academic periods beginning in the current year or beginning in the first three months of the next year.

Do **not** include qualified education expenses that are reimbursed with tax-free scholarships or grants, which may be posted to the student's account after the end of the tax year.

> Example
>
> Veejay is a full-time college student. His student account shows that the winter semester tuition of $5,500 was charged in December and paid with a student loan. He is awarded a scholarship which must be used for tuition for the winter semester in the following January of $5,000. Veejay can use the remaining $500 toward an education benefit in the current year.

When should I check the tuition and fees adjustment?

Whenever a student does not qualify for the American opportunity credit, the lifetime learning credit should be compared to the tuition and fees adjustment.

Even if the student qualifies for the American opportunity credit, if there are premium tax credits, shared responsibility payments, retirement savings credit or earned income credits that will be affected if AGI changes, you will want to try the expenses both as a credit (on Form 8863) and as an adjustment (on Form 8917). First, enter the allowable expenses as a credit and record the refund (or tax due) on both federal and state returns. Then change the entry on Form 8863 to zero and enter expenses allowable for the adjustment on form 8917. Confirm the calculation of premium tax credit, shared responsibility payment, retirement savings credit and/or earned income credit are correct with the new AGI. Then record the resulting refund or tax due on both federal and state returns. Show the different results to the taxpayer, who can choose which benefit to claim.

How do I display the different results?

Here is one way to display the results. Complete only the columns that apply. If the student is not a dependent, only the top section needs to be completed.

	A Use Tax-free Scholarship, Excess Expense to AOTC	B Use Tax-free Scholarship, Excess Expense to LLC	C Use Tax-free Scholarship, Excess Expense to T&F	D Up to $2,000 of Expense for AOTC	E Up to $4,000 of Expenses for AOTC	F Up to $10,000 of Expenses for LLC	G Up to $4,000 of Expenses for T&F	H Eliminate Filing Requirement
Student's Return								
Taxable Scholarship								
AGI								
Federal refund								
State refund								
Total refund								
Parents' Return								
AGI								
Federal refund								
State refund								
Total refund								
TOTAL refund for both returns								

How can I avoid common errors?

If you complete Form 8863, make sure that you have entered the names, SSNs and education expense amounts correctly. Check that you have not claimed more than one (AOC, LLC or T&F) tax benefit for the same student, the same expenses more than once, or taken a credit or deduction for expenses paid with a tax-free benefit like a scholarship.

On the intake and interview sheet, make sure that the appropriate box is checked to indicate that the taxpayer had education expenses. Note anything unusual that the quality reviewer may need to know when reviewing this part of the tax return. For example, you could note if some expenses were paid with a nontaxable scholarship.

Summary

You are now ready to help a taxpayer determine which education tax benefits are best for him or her. When you get to this section of the return, always check the intake and interview sheet and ask probing questions based on the taxpayer's information and on the rules for claiming education benefits. Rely on Tab J for the various rules and definitions for each education benefit.

There are two education credits that may reduce a taxpayer's tax:

- American opportunity credit
- Lifetime learning credit

Education expenses can be applied to those credits, deducted as an adjustment to gross income, deducted on Schedules C, itemized on Schedule A or used to reduce taxable portion of scholarships, grants, fellowships and distributions from education savings accounts. Choose the method that will give the taxpayer the lowest tax. The American opportunity credit can be claimed for a student if as of the beginning of the tax year, the student had not completed the first 4 years of postsecondary education and neither the American opportunity credit nor the Hope scholarship credit has been claimed for the student for any 4 tax years before this tax year and may be more beneficial than the lifetime learning credit. Remember, 40% of the American opportunity credit may be a refundable credit, which means taxpayers can receive up to $1,000 even if they have no tax liability.

One of your roles as a volunteer is to help taxpayers maximize the benefits that they are entitled to under the tax law. Stay alert to ways they can use their education expenses to lower their tax.

What situations are out of scope for the VITA/TCE programs?

The following are out of scope for this lesson. While this list may not be all inclusive, it is provided for your awareness only.

- Taxpayers who must repay (recapture) part or all of an education credit claimed in a prior year
- Distributions from Coverdell ESAs or QTPs if the taxpayer wishes to pay tax on the distribution and use other education benefits
- Education expenses paid with interest from qualified US Savings bonds