



1098-T: Credits and Deductions for Educational Expenses

Institutions of higher education provide students with Form 1098-T, which documents educational expenses and scholarship.

The 1098-T is for informational purposes only and is not sent to the IRS. It may not accurately portray the student's actual expenses and scholarship income. Rely on the taxpayer's information.

<input type="checkbox"/> VOID <input type="checkbox"/> CORRECTED		OMB No. 1545-1574 <div style="font-size: 2em; font-weight: bold;">2007</div> Form 1098-T		Tuition Statement
FILER'S name, street address, city, state, ZIP code, and telephone number		1 Payments received for qualified tuition and related expenses \$	Copy C For Filer For Privacy Act and Paperwork Reduction Act Notice, see the 2007 General Instructions for Forms 1099, 1098, 5498, and W-2G.	
FILER'S federal identification no. STUDENT'S social security number		2 Amounts billed for qualified tuition and related expenses \$		
STUDENT'S name		3 Check if you have changed your reporting method for 2007 <input type="checkbox"/>	Copy C For Filer For Privacy Act and Paperwork Reduction Act Notice, see the 2007 General Instructions for Forms 1099, 1098, 5498, and W-2G.	
Street address (including apt. no.)		4 Adjustments made for a prior year \$		
City, state, and ZIP code		6 Adjustments to scholarships or grants for a prior year \$	Copy C For Filer For Privacy Act and Paperwork Reduction Act Notice, see the 2007 General Instructions for Forms 1099, 1098, 5498, and W-2G.	
Service Provider/Acct. No. (see instr.)	8 Check if at least half-time student <input type="checkbox"/>	9 Check if a graduate student <input type="checkbox"/>		
Form 1098-T		Department of the Treasury - Internal Revenue Service		

There are three types of educational benefits:

1. Non-refundable and refundable credit: **American Opportunity Credit**
2. Non-refundable credit: **Lifetime Learning Credit**
3. Reduction of taxable income: **Tuition and Fees adjustment to income**

Wait until the end of return preparation to determine which educational benefit applies.

Scholarship & Grants less than Tuition & Fees.

If the scholarship amount (box 5) is zero or less than the tuition and fees (boxes 1 or 2), the difference may be used in the calculation of a credit or as adjustment to income. Next step is determine which credit applies. Then, determine if the customer will get the bigger refund by taking the appropriate credit or the adjustment to income.

Scholarship & Grants equal to Tuition & Fees.

If you are eligible for the American Opportunity Credit, you may take the credit for the amount you paid out-of-pocket or with a loan for books and supplies required for courses. You are not eligible for the Tuition and Fees adjustment to income or the Lifetime Learning Credit because those benefits only apply to amounts paid for tuition and fees, which in this case were fully covered by scholarships and grants.

Scholarship & Grants greater than Tuition & Fees.

If the student received a scholarship to help pay for room, board and living costs in addition to tuition, the student is not eligible for the credits or the tuition and fees adjustment to income. Some amount of the scholarship may have to be reported as income on Form 1040, line 7 and subject to income taxes.

Qualifying Educational Expenses

Expenses	American Oppor. Credit	Lifetime Learning Credit	Deduction from income	When Part of Scholarship is Taxable	
				Degree Candidate	Not a Degree Candidate
Tuition required to enroll at or attend a qualified educational institution	YES	YES	YES	YES	NO
Activity fees and expenses for course-related books, supplies, and equipment that must be paid to a qualified educational institution as a <u>condition of enrollment</u> or attendance. <i>(Buying text books at the university book store does not qualify- it is not a condition of enrollment. Only the amounts paid directly to the school qualify.)</i>	YES	YES	YES	YES	NO
Course-related expenses, such as fees, books, supplies, and equipment that are <u>required for the courses</u> at an eligible educational institution (must be required of all students in the same course of instruction).	YES	NO	NO	YES	NO
Room and board; Travel; Research expenses; Parking permit; student health insurance	NO	NO	NO	NO	NO
OTHER REQUIREMENTS					
For first 4 years of post-secondary education.	YES	NO	NO	NO	NO
Must be at least half-time student for at least one academic period	YES	NO	NO: Must be enrolled in one course and have high school diploma or GED	YES	NO
Not convicted of a felony	YES	NO	NO	NO	NO
Program leads to a degree, certificate or credential	YES	NO	NO	YES	NO
Maximum credit per student	\$2,500	N/A	N/A	N/A	N/A
Maximum credit per family	N/A	\$2,000	N/A	N/A	N/A
Maximum reduction of taxable income (for clients in our income range)	N/A	N/A	\$4,000	N/A	N/A
The person who claims the student's exemption gets the tax credit	YES	YES	Only if you paid the tuition. If your dependent paid all the tuition and you are eligible to claim dependent, no one is allowed to take deduction.	N/A	N/A
Taxable scholarships: The person whose SSN is on the 1098-T must report it as income	N/A	N/A	N/A	YES	YES

**When tuition and fees are more than scholarships and grants
aka
when you have to pay out-of-pocket or get a loan to pay for tuition, books and supplies**

When the qualifying tuition and expenses are greater than the scholarship amount, the difference may be used as an adjustment to taxable income or as a credit against income tax.

Only the tuition amount over the scholarship amount can be applied to an educational credit or tuition deduction! Also, only qualified expenses that were actually **PAID** can be claimed. Remember, you cannot claim a double benefit for expenses – you must choose between American Opportunity, Lifetime Learning, or reduction of taxable income.

The easiest way to determine which benefit is better for the client is to follow these steps.

1. Complete the return, including the Child Tax Credit and Earned Income Credit.
2. Subtract scholarship amount (box 4) from the qualified expenses (box 1 or 2).
3. In TaxWise, go to File and select What If Mode.
4. For the tuition and fees deduction, the amount computed in step 2 is capped at \$4,000. Only amounts paid for tuition and fees are considered qualified expenses for the adjustment to income.
5. Link from line 34 to the worksheet and enter the amount. Write down the client's refund that shows on the refund monitor.
6. Zero out the amount you just entered on the worksheet.
7. Go to line 49, Education Credits, and link to Form 8863.
8. Determine which credit they are eligible to receive: American Opportunity or Lifetime Learning.
9. If the student is eligible for the American Opportunity Credit, link to a scratch pad to include tuition, fees, required books and supplies as the qualified expenses.
10. If the student is only eligible for the Lifetime Learning Credit, the only qualified expenses are tuition and fees.
11. Note the refund amount using the credit.
12. If the credit is better, go to File and What If mode and answer YES to the question that will add the education credit on the What If return to the original return.
13. If the deduction is better, exit the What If mode and answer no to the question about replacing the original return with the What If version. On the original return, enter the tuition and fees deduction amount by linking to the worksheet from line 34.

**When the scholarship and grants are more than the tuition and fees
aka**

**When your scholarship covers all your tuition and
gives you additional money for living expenses**

Determining the taxability of a scholarship or grant:

If the amount of scholarships/grants is **MORE** than the tuition and qualified expenses, client does **NOT** qualify for an education credit or a tuition deduction on their tax return. Instead, the preparer must determine how much of the scholarship or grant is taxable and should be included as income on line 7 of Form 1040.

- 1) Start with the 1040, line 7, by "Taxable Scholarship not on Form W-2"
- 2) Link to Wkt1, Social Security and Other Income Worksheet.
- 3) From "Additional Earned Income" section, link from the scholarship line to a scratchpad.
- 4) Title the Scratch Pad "Calculation of Scholarship Income" so it will be clear to the quality reviewer and the transmitter.
- 5) First line on the scratch pad: type "Scholarship/Grants" and enter the amount from box 5 of 1098-T.
- 6) Second line: "Expenses from box 1 or 2 of 1098-T" and enter the amount as a negative so that it will subtract from the scholarship/grant amount.
- 7) On the following lines: title them and enter the amounts paid (as negatives) for books, supplies and equipment required for the courses.
 - a. Be careful to include only books, supplies and equipment that were required for a course. A laptop may be very helpful but if it is possible to take the specific course(s) without a laptop then you cannot subtract the cost of the laptop.
 - b. If the client does not have receipts for the required books, supplies and equipment, we can still prepare the return but the client must have a reasonable idea of the amounts paid. If the client has no idea of the amounts paid, leave the amount as is (scholarship minus tuition) and let the client know that they can amend the return at a later date when they find receipts or can reconstruct those expenses.
- 8) The result of your entries at the bottom of the scratchpad is **taxable income**. Do a sanity check: Were all the numbers you entered subtracted from the scholarship amount?
- 9) If you have linked properly, the amount on the bottom of the scratch pad will be on line 7 of the 1040 as "Scholarship income not reported on W-2."

Again, if the scholarships and grants are more than the tuition and qualified expenses costs, then the taxpayer (or the person claiming the student's exemption) does not qualify for a tuition deduction or education credit. Those lines should be blank on the tax return.

American Opportunity Credit: Questions and Answers

- Q. The Hope credit originally applied only to the first two years of college. Has that changed?
A. Yes. The American opportunity tax credit can be claimed for expenses for the first four years of post-secondary education.
- Q. How much is the American opportunity tax credit worth?
A. It is a credit of up to \$2,500 of the cost of qualified tuition and related expenses paid during 2009.
- Q. What education expenses qualify for the American opportunity tax credit?
A. The term "qualified tuition and related expenses" has been expanded to include expenditures for "course materials." For this purpose, the term "course materials" means books, supplies and equipment needed for a course of study whether or not the materials are purchased from the educational institution as a condition of enrollment or attendance.
- Q. Does an expenditure for a computer qualify for the American opportunity tax credit?
A. Whether an expenditure for a computer qualifies for the credit depends on the facts. An expenditure for a computer would qualify for the credit if the computer is needed for enrollment or attendance at the educational institution.
- Q. How is the American opportunity tax credit calculated?
A. Taxpayers will receive a tax credit based on 100 percent of the first \$2,000 of tuition, fees and course materials paid during the taxable year, plus 25 percent of the next \$2,000 of tuition, fees and course materials paid during the taxable year.
- Q. How will the American opportunity tax credit affect my income tax return?
A. You will be able to reduce your tax liability one dollar for each dollar of credit for which you're eligible. If the amount of the American opportunity tax credit for which you're eligible is more than your tax liability, the amount of the credit that is more than your tax liability is refundable to you, up to a maximum refund of 40 percent of the amount of the credit for which you're eligible.
- Q. Can I also claim the tuition and fees tax deduction in addition to claiming the American opportunity tax credit?
A. No. You cannot claim the tuition and fees tax deduction in the same year that you claim the American opportunity tax credit or the lifetime learning credit. You must choose among them. You also cannot claim the tuition and fees tax deduction if anyone else claims the American opportunity tax credit or the lifetime learning credit for you in the same year.