John Dickinson: Good afternoon, everyone. Thank you so much for choosing this seminar, *Don’t Flunk Out on Education Credits*. No, you are not going to flunk out on education credits. Today, you are going to graduate with honors as I share with you some basic, yet key, information on these education credits.

I am John Dickinson, and I work for the Internal Revenue Service. I have worked for the IRS for nearly 30 years. Specifically, I work for a group called the Refundable Credits Administration, and our group has oversight for the IRS refundable credits. I am sure you have heard of the Earned Income Tax Credit, the Additional Child Tax Credit. Our office now has the premium tax credit. And of course, my favorite is the American Opportunity Tax Credit. We are going to refer to it from here on out as AOTC.

Part of our group's mission is to help taxpayers and preparers understand these credits and maximize the benefits. But for AOTC, we not only want you to be aware of this credit (maximize this credit), but we want you to avoid some potential hazards so you can keep your tax preparation businesses “on the honor roll” and out of “the dean's office,” meaning the IRS.

Don't be shocked, but today you are going to have to pay special attention because you are going to be tested on these education credits during the seminar. You are going to be tested on two education credits. We have mentioned AOTC. AOTC is partially refundable; up to 40 percent (or $1,000) per each eligible student may be refunded. There is also the nonrefundable credit, called the Lifetime Learning Credit.

Let me briefly explain refundable and nonrefundable. Refundable tax credits not only can be applied to a person's tax liability, but they can also generate a refund, even if that person owes no tax. For a nonrefundable credit, like the Lifetime Learning Credit, it can only be applied to a person's tax liability. Because AOTC is partially refundable, it is the more popular of these two credits.

I am going to give you a warning: I am going to give you some shocking facts on AOTC. Hold on to your seats. For tax year 2013, there were over 10 million claims for AOTC. Do you realize that you, our paid tax professionals, filed over 53 percent of those claims? That is very good. That just shows how important you are to the Internal Revenue Service and to the taxpayers in filing these claims for them and filing them accurately.

Another fact: of those 10 million claims filed, the IRS could not match a Form 1098-T to 2.5 million of those claims. So, what is so important about that Form 1098-T? As of today, it is not a requirement to claim an education
credit, but it is a high indicator of their eligibility. Another fact: there were over 23,000 students claimed for AOTC that were under the age of 14.

[Laughter]

Wow, we have a lot of smart children in the United States is what I am thinking. But also, there were more than 3,000 students that were over the age of 80.

[Laughter]

Do you think there is some confusion here? You think probably there could be some fraud involved as well? Probably a little bit of both, but we know, sadly, that our refundable credits are open and exposed to fraud. While most of the errors that we see with AOTC are unintended, probably due to the complexity of the law, we do realize and know that there are some out there that will file fraudulent claims to take advantage of those refunds. Make sure the returns/the claims that you file are accurate before you send them to the IRS. And we are going to help you with that today by providing you with information and resources needed for you to stay on the honor roll with the IRS and avoid the dreaded audits. That's right; audits on education credits are going to increase again this year, particularly those where the IRS cannot match the Form 1098-T.

This is your honors curriculum for today. We will discuss what's new. We will discuss the Form 1098-T in great detail. We will discuss each education credit and the basics. We will provide you some interview best practices. We will provide you some resources and information on how to contact us.

Last year, the instructions for Form 8863 and this year's Form 1098-T instructions for students included a tip about coordination with Pell Grants and other scholarships. The importance with this is that it provides information on how to maximize an education credit for those that did have Pell Grants or other scholarships. We are going to discuss this in much more detail as we move along.

Also, the Form 1098-T, the student's copy (Copy C) includes a note to help students realize how important this form is. It basically states, “This is information provided to the Internal Revenue Service. This form may be used to complete Form 8863. Give it to your tax preparer or use it to prepare your tax return.”

Last year, the limit on modified adjusted gross income for the Lifetime Learning Credit increased to $64,000 for single, head of household, and qualifying widower, and up to $128,000 if filing married filing joint. The AOTC income limits remained unchanged.
Legislative reminders: AOTC is currently extended through tax year 2017. We have three more years to file claims for this credit, but note that legislation can change very quickly. Example: it could include additional requirements to claim an education credit/benefit, or extend a benefit or expired benefit, or one that is set to expire. The IRS reviews new legislation and provides information on IRS.gov, so stay tuned on IRS.gov.

I am just curious. How many of you out there filed claims for AOTC last year? Raise your hand. Good, good. Now, how many of you that raised your hand are familiar with Publication 970? About half of you. The Publication 970 has some valuable information and examples on education credits and other education benefits. I recommend that you go to IRS.gov and download it and use it as you prepare claims for next year.

One of the main points when discussing education credits is this Form 1098-T. It is very important; and as mentioned before, it is not a requirement as of today. The information contained on the Form 1098-T will assist you in completing the Form 8863, which is a requirement. The problem with the Form 1098-T is it is not all-inclusive. It does not contain all the information that you might need to maximize an education credit; therefore, you are going to have to interview your client to properly determine the amount of qualified education expenses paid during that tax year, the amount of scholarships received, and even the student's status.

Let’s take a look at a short video that explains the importance of this form from the school's point of view.

[Video begins]

**Female 1:** John, thanks so much for helping me prepare the Form 1098-T for our students. Form 1098-T is easy to complete once you understand what goes where and why. We are required to complete it, and it sure helps many of our students stay in school.

**John:** I am happy to help. I know it helped me when I was in school.

**Female 1:** Let's go over the form step by step to make sure you understand. First, you need to know when to complete the form. I have one right here. We complete Form 1098-T for each student who enrolls, attends, was billed, or paid to attend our school. But there's some exceptions when a 1098-T is not needed. Why don't you tell me what they are?

**John:** Well, let's see if I can get them all. Courses for which no academic credit is offered. Oh, nonresident alien students, students whose tuition is waived or paid by scholarship, and what is that last one? There is one more.
Female 1: There is one more. Students under a formal billing arrangement, such as Department of Veterans Affairs or Department of Defense.

John: Oh, yeah, that's right. I'm pretty clear on that. What about filling out the form itself? I want to make sure I go over all of the entries on the form that need to be completed.

Female 1: Our school's name and address go in the entity section, unless there is a third party who collects the funds and does the billing. The telephone number should be the number of our office, since we complete the form and can answer questions. And for goodness' sake, don't use the general switchboard number.

John: I know the student's name and SSN must match Social Security records, and the school-verified SSN and name when a student enrolled is required. I hear it is important because the IRS does penalize for inaccurate reporting. I also know we can shorten the SSN on the student's copy, but not the version filed with the IRS.

Female 1: Did you know there is a $100 penalty per incorrect form? That's up to $1.5 million in penalties per year.

John: Whoa.

Female 1: So, it is very important to collect the right information when the student registers. Now, let's start going through the boxes on the form. We can choose to use either Box 1 or Box 2. Box 1 is for payments received for qualified tuition and related expenses. This is the total amount received from all sources during the calendar year. The amount in Box 1 is not reduced by the scholarships and grants reported in Box 5. Box 2 is the amounts billed for the exact same things as Box 1.

John: And just to make sure I am right, Box 5 is for reporting scholarships or grants administered and processed during the calendar year?

Female 1: Yes, that's correct. We only report the ones we administer or process. Now, the student may have other scholarships or grants, but they are responsible for having that information.

John: Makes sense. What's next?

Female 1: It is very important to check Box 8 if the student attended school at least half-time for any academic period during the year. We can set the period as long as it follows the standards set by the Department of Education. What about Box 9?
John: If the student finished their undergraduate degree early and is a graduate student any part of the year, we will check Box 9.

Female 1: You are right. For 1098-T, we must provide the form or an acceptable substitute to each student. We can give the student the form electronically or on paper. There are a lot of students who access the information on their cell phones.

John: Modern technology. You have really made this easy to understand, and I am ready to get started.

Female 1: Don't forget, if I am not around, there is plenty of information on the IRS website.

John: I wouldn't want to be the person who costs our school to have a $1 million penalty. I want to keep my job.

Female 1: Boy, do I have something for you.

John: Oh, boy.

Female 1: I have a lot of papers here. And guess what… [Fades out]

[Video ends]

John Dickinson: Remember, most students should receive a Form 1098-T from their college or university. However, as mentioned in the video, there are some exceptions when schools are not required to send the Form 1098-T, but most schools will. If the client does not have a Form 1098-T, ask them why, and inform them to contact the school to go get a copy.

Also, the school can confirm if they are an eligible institution. As this video pointed out, most everyone has electronic access at their fingertips. Most of these students can access their student information from their smartphone, a tablet, or their computer. The video also reminds us of the school's requirements and the options that they have in completing this Form 1098-T, like the amounts of qualified tuition and fees. Remember, the schools have the option to report this in either Box 1, “received” (meaning paid), or Box 2, “billed.” Guess what most schools prefer to report at? Billed.

They also have an option for the scholarships and grants. They only put a figure in that Box 5 if they administered or processed that grant. Also, the student status; Box 8 will be checked if that student was at least a half-time student for at least one academic period during the year. And there is a Box 9, “graduate student.” If that box is checked, that means that student was a
graduate student or became a graduate student at some point during that tax year.

There are general qualifications that must be met in order to claim either education credit. All three must be true to claim an education credit: your client must have paid “qualified education expenses” of “higher education;” the client must have paid education expenses for an eligible student; and the eligible student is the client, the client's spouse, or their dependent that they claim as an exemption.

I mentioned some terms in quotation that I would like to expand on: higher education, postsecondary education. What does that actually mean? We know, but your clients probably don't. This means college or vocational schools. It is not your elementary schools. It is not your middle schools. It is not your high schools, even if these schools were private and even if there was some sort of tuition paid. Remember the stat that I gave you about the 14-year-olds being claimed? That's right; I think there may be some confusion with our taxpayers on these terms that we're using.

Also, qualified education expenses: these are amounts paid for tuition, fees, and other expenses that are required for attendance. To be a qualified education expense, it must be paid during the tax year for an academic period that started during that tax year or for the first three months of the following year. Question: what about books, supplies, and equipment? Are those qualified education expenses? There’s some confusion there. These are qualified education expenses for AOTC, even if they were not paid to the school. But for the Lifetime Learning Credit, they must have been paid directly to the school to qualify.

There are a few more differences in the qualifications for AOTC and the Lifetime Learning Credit that I would like you to see side by side. For AOTC, a student can only be claimed for four tax years, and the student must be within their first four years of postsecondary education. This means the student must be within their freshman through senior years of college. And we will talk more about graduate students as we move on.

Another requirement is the student must be enrolled at least half-time for at least one academic period during that tax year, and they must be in a degree program or other accepted education credential. The student could not have been convicted of a drug felony before the end of the tax year.

For the Lifetime Learning Credit, a student is not limited by the number of years that they can claim the credit. It is available for one or more courses, which means they are not required to be at least a half-time student. And you are not required to be in a degree program. Eligible courses can include those to get or improve a job skill. And there are no felony drug restrictions with the
Lifetime Learning Credit.

Let's compare the value of each credit. AOTC is worth up to $2,500 per each eligible student, and as we mentioned, 40 percent (or $1,000) may be refunded. Let me give you a tip for AOTC. Once your client reaches this magical number of $4,000 in qualified education expenses paid, that's it. You don't have to look for any other qualified education expenses. They will receive the maximum amount of AOTC allowed. Plus, the Form 8863 restricts you from putting in a number greater than $4,000.

AOTC also has some income limits that I want to mention. It cannot be claimed if the modified adjusted gross income is more than $90,000 for single, head of household, or qualifying widower, or more than $180,000 if they file a joint return.

The Lifetime Learning Credit is worth $2,000 per tax return, not per student like AOTC. And, of course, it is not refundable. Let me give you a tip for the Lifetime Learning Credit. Once your client reaches this magical number of $10,000 in qualified education expenses paid, there's no more reason to search for any other expenses. They will receive the maximum credit allowed for the Lifetime Learning Credit. And, again, as a refresher, for the Lifetime Learning Credit, the modified adjusted gross income was raised to $64,000 for single, head of household, and qualifying widower, and $128,000 for joint filers.

Knowing the qualifications and the value of each credit – is it important to you or not? It is important to know that. I know your software catches that for you, but it still is good for you to know that. But what is equally as important is knowing what the students know about this Form 1098-T and their thoughts. Let's listen to this video conversation with two students talking about the Form 1098-T.

[Video begins]

**Female 2:** Hey, Charles.

**Charles:** Hey, what's up?

**Female 2:** Do you know much about that American Opportunity Tax Credit?

**Charles:** Yeah, my parents got it last year, and they got a pretty big refund, too.

**Female 2:** Really? I sure could use $2,500. I know my school puts on this account information, a Form 1098-T. Does this mean I can qualify for the American Opportunity Tax Credit?
Charles: Possibly, but what the form does let you know is that you may be eligible. Last year my parents claimed me, and they got the AOTC. I know they got back a large part of the tuition they paid for me. Which reminds me: I didn't get a 1098-T this year, so I'll have to make note of it right now.

Female 2: Okay, so here's the thing. I don't know a thing about taxes, and my parents probably don't either. They go to a preparer every year.

Charles: Yeah, well, for starters, your parents will need to take Form 1098-T to their preparer. And my parents did mention, just because you get the form does not mean you qualify. So, just as an FYI, if all your expenses are not reported on 1098-T, it does not mean you can't take a tax benefit. It just means you need more documentation. That is why my parents asked for more information on expenses that we paid last year.

Female 2: Really? Like what?

Charles: Well, I had to give them a copy of my receipts for books and for my lab supplies.

Female 2: Okay, you have given me a lot of information that I did not know about. I am actually pulling the form up now. Wow, look at Box 1. I paid a lot more than what they have on here. It is not just tuition. It is the cost of books and supplies and things of that nature, right?

Charles: Yeah, that is why it is important to keep all your receipts for tuition, fees, and books and supplies that you had to buy.

Female 2: Yeah, I see. Oh, my gosh.

Charles: What?

Female 2: You have yogurt everywhere. Nothing's changed since kindergarten.

Charles: Looks that way, right?

Female 2: Geez. Okay, now, how about Box 5? Scholarships? What's that all about?

Charles: Okay, so scholarship is another important form of money. I had scholarship money, too. I learned that if it's just used to pay for your tuition, books, and fees, that you can't use those funds for expenses. However, there wasn't a problem for me last year, because it only covered half of my expenses. The rest my parents paid for. So, if you go to a preparer, I'm certain they're going to ask you about any other types of scholarships on your 1098-T and other expenses.
Female 2: Okay, so what did you have to do?

Charles: Well, they just asked me about the amounts of scholarships I received and how I used those amounts. Did I use the scholarship just for tuition, books, and fees, or some just for tuition and room? And I had to give them a list of other scholarships I got that weren't listed in Box 5 there.

Female 2: Okay, so I guess I just need to make sure my parents have the Form 1098-T handy when they go to their preparer this year.

Charles: Yep. And I have to remember to bring it all to my parents when I go home next weekend, too.

Female 2: How about this? You know how you keep hassling me about this new phone you got for Christmas that can do everything? Why don't you see how well it works with taking pictures? Take a picture and send it to them on your phone.

Charles: Not a bad idea. Well, you know, when my parents were looking for additional information, they checked out IRS.gov and searched for education credits. There was a ton of information on the site.

Female 2: Okay. Well, IRS.gov, I'll have my parents go there as well. You know, I will say one thing. You're not too good with first dates. After all, this is a coffee shop. But you do know your stuff, I'll give you that, about the American Opportunity Tax Credit. I'm so glad we had this discussion.

Charles: Okay, well, perhaps happy hour next time?

Female 2: Sure, you drive.

[Video ends]

John Dickinson: These two students were aware of the importance of the Form 1098-T. They knew it helped them and their parents offset the cost of college expenses. But as this young man stated, just because you receive a Form 1098-T, it does not mean you automatically qualify for an education credit. If these situations on the screen apply to your client, they cannot claim an education credit:

- if your client files married filing separately;
- if the student is listed as a dependent on someone else's return;
- if your client or client's spouse were a nonresident alien for any part of that tax year.

To determine the tax consequences for nonresident and resident aliens, please check out Publication 519, *U.S. Tax Guide for Aliens*.

That reminds me of a situation that we see each year (almost each year), and it involves our international students. International students generally have F-1
visas, and the F-1 visas are for full-time students that allow them to pursue their academic studies in the United States, and students with F-1 visas are generally nonresident aliens. As we just learned, nonresident aliens do not qualify for the education credits.

The story is these students often get scammed by dishonest promoters of AOTC. They advertise that the IRS is giving away free money or some type of stimulus payment or some other type of gimmick. And these promoters have charged as much as $500 to these students to file these claims. And, of course, these claims are only for the refundable part of the credit ($1,000). Be careful; and remember, if your clients do not have a Social Security number, ask questions and refer to Publication 519 on IRS.gov.

I’ve got a question for you: can high school students qualify for AOTC? Great, I hear two answers. The general answer is no. Remember, these credits are for postsecondary education, meaning college and college students. To be eligible for AOTC, a student must meet the degree requirement, which is to be in a program that leads to a degree or other some sort of education credential. They must also meet other requirements, like being enrolled at least half-time for at least one academic period that began in that tax year.

Having said all that, a high school student that took college courses before graduating from high school could be eligible for AOTC only if, during that same tax year, they became an eligible student that meets the criteria that we just explained. In that situation, the student can claim AOTC for any qualified education expenses that were paid to the college, including those paid to the college for courses that were taken in high school.

Use the Form 1098-T as a guide when completing Form 8863. Review this entire form closely, including the section that lists the student's name and Social Security number. Make sure this information matches the student's Social Security card, if possible. Incorrect information could cause a mismatch with the IRS, and if we can't match the Form 1098-T to the claim, remember, your client runs a higher risk of being audited.

I am sure you are asking yourself, “Well, why can't this Form 1098-T be like a W-2? Why is it just used as a guide?” Well, I am going to remind you of some of the things that we have already seen in the video. Remember, because schools have the option on how to report the tuition and fees, they can be in Box 1, “received” (meaning paid), or Box 2. You have to use it as a guide. You have to verify that the student has actually paid those qualified education expenses.

And remember, the schools are not required to report other qualified education expenses, such as books and equipment. Remember, schools, again, only report the amounts of scholarships that they processed or administered.
Whether there is an amount in Box 5 or not, you still need to ask the student if they received any scholarships or grants.

Also, Box 8… look at Box 8. If Box 8 is checked, it means that this student was at least a half-time student. But if it is not checked, it is possible that student was still considered at least a half-time student. I live in the Atlanta area. We have a lot of schools around the Atlanta area, and a lot of the students go to multiple schools, so they would receive multiple 1098-Ts. The sum of the 1098-Ts, the sum of the courses that they are taking, it could make them eligible for AOTC being more than a half-time student.

Box 9 is checked if the student is a graduate student or they became a graduate student at some point during that tax year. Is it possible for a graduate student to qualify for AOTC? It is possible for a graduate student to qualify for AOTC as long as they were an undergraduate at some part during that tax year; meaning they were probably a senior and, at some point during that tax year, they became a graduate student. And then if that is the case, then that student can use any expenses for their senior year, and they can use the expenses as a graduate student for that one year.

For all those reasons that I just mentioned, you can only use the Form 1098-T as a guide. You cannot simply take the data off of it and then put the figures on it. You must use it as a guide.

This is my favorite video. This is a tax preparer, and he has a client in his office. He is asking some very good interview questions regarding the Form 1098-T and other issues. Let's watch this video.

[Video begins]

Male 3: Now that we have finished the other parts of your return, let's move on to education credits. I would like to begin by looking at your daughter Sandy's Form 1098-T.

Female 3: Here it is.

Male 3: Great. This form is a good indicator that she may be eligible for an education credit, but I have to verify a few things first. If she is eligible, you could take her education credit since you are able to claim her as a dependent this year.

Female 3: Yes, she's grown up now and goes by “Sandra.”

Male 3: It just seems like yesterday she was running around the office, playing hide and seek. Let me take a quick look at the form. Okay. I see her name and Social Security number match the information I verified earlier. First, I'd like to make sure she is an eligible student before we talk about what expenses you
can take. I see Box 8 is marked showing that she is at least half-time and that she isn't a graduate student. Remind me again, is Sandy – I mean, Sandra – is she still in high school, or is she going to college now?

Female 3: Time goes by quickly, and it is hard to believe, but she isn't in high school anymore. She is not getting a college degree; she is going to school to be an EMT.

Male 3: Great field choice. Is this her first year of school?

Female 3: Yes, she started in September.

Male 3: Okay. I just need to verify that Box 8 is marked correctly. Was she going to school full-time?

Female 3: Yes. This is the type of program you have to attend all the time or not at all. She goes continuously, with just short spring, summer, and winter breaks.

Male 3: Great. She may qualify so you can take the American Opportunity Tax Credit, which I usually just call the AOTC. That is the more valuable of the education credits. You can get up to $2,500, and $1,000 of that is refundable.

Female 3: A thousand. Wow.

Male 3: But I still have to ask some more questions before I can determine what amount you are eligible for.

Female 3: I hope I can get it. This is an expensive certificate. I could sure use some help paying for it.

Male 3: Tell me about it. Both of mine are in college. Now, I really hate to ask this, but I am required to. Has Sandra ever been convicted of a felony drug charge?

Female 3: What kind of question is that? But no; she's caused me some trouble, but thankfully not that.

Male 3: Yeah, I know, I know. It is just part of the law. In order to be eligible for AOTC, you can't have a felony drug conviction before the end of the tax year. Next, I need to confirm Sandra's qualified education expenses. Did she receive any help to pay for school, such as Veterans Educational Assistance, the Department of Defense, or from her employer?

Female 3: Nope. That would have been nice.

Male 3: The amount in Box 2 shows the amount the school billed you for. What did you actually pay last year?
Female 3: I paid $2,000. My mom and dad gave her $3,000. And Sandra got a few scholarships, but she took out a loan for the rest.

Male 3: Okay. I see Box 5 lists some scholarships of $4,000. What type of scholarships did she get? For instance, did she get a tax-free Pell Grant? Also, the school only reports the amounts they handled, so I need to know if she got any grants or scholarships that aren't listed on the form.

Female 3: She did get a Pell Grant of $4,000, but the local fire department also gave her a $500 scholarship, but that is all she got.

Male 3: So far, I have the $15,400 the school billed you for. Did she pay that full amount during the year?

Female 3: Yes. Let me look at the billing statements to make sure. Yes, the last payment was sent in December.

Male 3: Okay. Of the $15,400, $4,000 was paid from a Pell Grant, so I will need to deduct that. Now we are at $11,400. For the education credits, you can also consider amounts paid by your daughter, or by third parties like your mom or dad, or the fire department, as having been paid by you.

Usually, my next question is if you or your daughter paid any additional expenses that are not reported on her Form 1098-T. These would include expenses for items such as books or any other materials required for the course. But you are already at the maximum amount of expenses you can claim for the AOTC, so I don't need to go over that.

Female 3: Wow, that is excellent.

Male 3: Not so fast. I still have to do the rest of your return to make sure you are within the maximum income limits. But so far, it is looking good.

[Video ends]

John Dickinson: He did ask some great questions. As a preparer, you do need to fulfill your necessary due diligence. If your client's answers leave you doubting, continue to ask them more and more questions until you feel reasonably comfortable before you file that claim. In this video, this preparer did verify that the expenses were paid because the Form 1098-T reported the tuition and fees as billed. He also asked if her daughter received any education assistance, and he asked about the scholarships in Box 5 and if she received any other scholarships that were not listed.

Ask the right questions to verify the school name and school federal
identification number. Verify the expenses paid, including books and equipment, if necessary. Verify the student's eligibility, especially for AOTC. Remember, you can only claim the credit for four years.

How are you going to know that your client has not claimed it for more than four years? You have to simply ask. And you can apply some common sense as well. If the student has been in college for 10 years, chances are they may have exceeded the four-year limit. So, just verify their eligibility for AOTC. Keep documentation and notes for your records.

I am going to give you an important tip. I know this may be hard to do, but if possible, coordinate the returns of the student and the parent together. Remember to check to see who is eligible to claim the student as a dependent. These education credits go with whoever can and does claim the dependency exemption.

A question to you: can someone claim both AOTC and the Lifetime Learning Credit for the same student for the same year? Of course not. That would be a double benefit. There are no double benefits, which means a person can only claim one education benefit – I am saying “benefit” not “credit” – one benefit per year per student, based on those same expenses for that student.

As a preparer, when you are working these returns, your client is often going to qualify for both of the education credits and even some other of the education benefits; but you must decide which is the most advantageous because you can only choose one benefit. Another instance of double-dipping is trying to claim a qualified education expense that was paid with tax-free education assistance. If you remember in the video, the preparer asked the client if her daughter's tuition was paid with any tax-free assistance, such as a scholarship, a grant, or employer assistance. Again, that would be double-dipping. There is no double-dipping.

I need you to maximize these education credits for your clients. There are times when it is better to claim traditional, non-taxable income into income to maximize an education credit, such as a Pell Grant. Claiming AOTC often requires some complicated decisions. Students, parents, and preparers don't always realize that there is a choice in how they can allocate that Pell Grant expense.

For tax purposes, there is a choice regardless of how that school applied that Pell Grant. Example: if your client received a Pell Grant and you apply that Pell Grant toward qualified tuition and related expenses, which is how the school will apply it, that Pell Grant is going to remain tax-free. However, you cannot claim those qualified tuition and related expenses that were paid with that Pell Grant to calculate AOTC. Remember, that is double-dipping. But on the other hand, you may be able to increase the value of that education credit.
if you applied the Pell Grant in whole or in part to non-qualified education expenses, such as living expenses (room and board), and then you include that Pell Grant – whatever part of the Pell Grant that you used, you include that part of the Pell Grant – into income in the year it was received.

There are clear examples in the Publication 970, *Tax Benefits for Education*. Chapter 2 is on the American Opportunity Tax Credit, and Chapter 3 is on the Lifetime Learning Credit. Each of these chapters has sections and tips about coordination with Pell Grants and other scholarships.

Okay, are you guys ready? I told you you're going to be tested. I have got five total questions for you, and let's get on with the questions. The questions are going to be simple at first, and they are going to graduate.

Question number one: What amount of qualified education expenses is needed to claim the maximum amount of AOTC? A, $2,500; B, $4,000; or C, $10,000? Let me hear your answers.

*Audience:* B.

*John Dickinson:* Great, the answer is B. But why is it B? The answer is $4,000. Why? The calculation to figure AOTC is 100 percent of the first $2,000 in qualified education expenses, plus 25 percent of the next $2,000 in qualified education expenses. Very good, that was an easy question.

Question two: Dexter is filing single. He earned $80,000, and during your interview process, you found out that he did pay $4,000 in qualified education expenses. And in your interview process, you get a copy of his Form 1098-T, and it shows that he is a graduate student. Now, based just on this information, does Dexter qualify for AOTC? A, yes; B, no; or C, you need some more information?

*Audience:* [Inaudible responses]

*John Dickinson:* Not so confident. The answer is C, you need more information. Why do you need more information? Remember, it is possible for a graduate student to qualify for AOTC. But you need to find out if Dexter was within his first four years of postsecondary education during that tax year, meaning was he still a senior at some point during that tax year? Who got that question right? Let me see your hands. Good. He is within the income limits.

Question number three: Yolanda paid her tuition with a $5,000 gift from her grandparents, $5,000 from her student loan, and $5,000 from a Pell Grant. What amount of qualified education expenses can Yolanda use to calculate an education credit? Can she use A, $5,000; can she use B, $10,000; can she use the entire $15,000; or D, zero? Let me hear your answers.
Audience: B.

John Dickinson: The answer is B. Very good, but why is it B? The loan and the gift are allowable funds to calculate qualified education expenses. The Pell Grant, if treated as tax-free, is not. Would anybody consider including the Pell Grant in income in this situation? No, you wouldn't, because she is already over the maximum amount of qualified expenses to maximize either AOTC or the Lifetime Learning Credit.

Question four: Sarah is in an undergraduate program and received a Form 1098-T. The form shows that she was billed $5,000. And, as you see on the screen, Box 8 is not checked, so it doesn't indicate she is at least a half-time student. What two questions would you need to ask Sarah right away? Let me just hear it.

Audience: [Inaudible responses]

John Dickinson: Right, was it paid and was she at least a half-time student? During your great interview with Sarah, you found out that Sarah did pay the amount billed, but Sarah also indicated that she only took six credit hours. The school considers 15 credit hours to be full time. Based on this information, choose the eligible credit for Sarah: A, AOTC; B, Lifetime Learning Credit; or she can claim either A or B; or D, none of the above. What is the answer?

Audience: B.

John Dickinson: Good, the answer is B, the Lifetime Learning Credit. Why? Remember, you don't have to be at least a half-time student to claim the Lifetime Learning Credit. For AOTC, you must be at least a half-time student.

All right, class, this is the extra credit. Before I read this question, I want to remind you of the tip that I talked about: if possible, coordinate your tax returns with your student and your parent.

Jay is single. He is 20 years old. He files single. He is a full-time student, received multiple Forms 1098-T. He earned $12,000. Jay's parents provided more than half of his support and paid his tuition of $14,000, but his parents chose not to claim him as a dependent. Which education credit can Jay claim? Can he claim AOTC; Lifetime Learning Credit; either A or B; or D, none of the above? Let me hear your answers.

Audience: [Inaudible responses]

John Dickinson: The answer is he can claim either the Lifetime Learning Credit or AOTC, but he cannot claim the refundable part of the American Opportunity Tax Credit.
And why is that? Remember, 40 percent of the American Opportunity Tax Credit is refundable for most taxpayers. However, if the student was under 24 at the end of the year and the conditions that you see on the screen apply to your client, they can only use the non-refundable part of AOTC. Publication 970 provides more information in Chapter 2 under AOTC for this particular part of the law. How many got that question right? Let me see your hands. Very good. We do have some honor students today.

The resources that I mentioned today can be found at eitc.irs.gov/Other-Refundable-Credits/main. Again, that is eitc.irs.gov/Other-Refundable-Credits/main. And if you need to contact our office, please contact us at eitc.program@irs.gov.

Thank you very much. Enjoy the rest of your day.

[End of Audio]
Glossary

American Opportunity Tax Credit – American Opportunity Tax Credit (AOTC) is a credit for qualified education expenses paid for an eligible student for the first four years of higher education. You can get a maximum annual credit of $2,500 per eligible student. If the credit brings the amount of tax you owe to zero, you can have 40 percent of any remaining amount of the credit (up to $1,000) refunded to you.

Form 1098-T, Tuition Statement – An eligible educational institution, such as a college or university in which you are enrolled, and an insurer who makes reimbursements or refunds of qualified tuition and related expenses to you must furnish the Form 1098-T to you. You, or the person who can claim you as a dependent, may be able to claim an education credit on Form 1040 or 1040A, only for the qualified tuition and related expenses that were actually paid.

Lifetime Learning Credit – The Lifetime Learning Credit is for qualified tuition and related expenses paid for eligible students enrolled in an eligible educational institution. This credit can help pay for undergraduate, graduate and professional degree courses--including courses to acquire or improve job skills. There is no limit on the number of years you can claim the credit. It is worth up to $2,000 per tax return.
Index

A
American Opportunity Tax Credit (AOTC)
   Definition, 18
   Overview, 1-3
   Qualifications for claiming, 6-9
   Value of credit, 7

D
Double benefits, 14

F
Form 1098-T
   Completing the form, 5-6
   Definition, 18
   Overview, 2-5, 7-9
   Using the form as a guide, 10-14
Form 8863, 2-3, 7

H
High school students, 10

I
International students, 9-10

L
Lifetime Learning Credit
   Definition, 18
   Overview, 1-3
   Qualifications for claiming, 6-9
   Value of credit, 7

P
Pell Grants, 2, 13, 14-15
Pop quiz, 15-17

Q
Qualified education expenses, 3, 6-8, 10, 12-13

R
Resources, 17

S
Scholarships, 2, 3-5, 8-9, 13, 15