



State System of Higher Education

**Taxation of Scholarships,
Waivers, and Educational
Benefits**
Users' Guide



*Intended for State System of Higher Education Reference
Not Intended for Distribution to External Parties*

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Document Sources:

American Payroll Association Publications
Board of Governors Policies—State System of Higher Education
Bureau of National Affairs—Payroll Administration Guide
General Legal Opinion #2-98, supplemented by 5/11/98 advice
Internal Revenue Service Publication 520
Management Directive 535.3 Amended—Out Service Training
National Association of College and Business Officers—Tax Forum III;
Bertand M. Harding, Esq., 12/8/97
Pennsylvania Department of Revenue—Guide on Taxable Items

Section I.

Terms and Definitions

The terms used in this manual are provided to aid the user in interpreting *this* manual. These definitions represent State System terminology and could differ from federal, state, and local tax regulations.

Assistantship—A paid appointment awarded on a semester/annual basis to a qualified graduate student that requires part-time teaching, research, or other duties.

Compensation for Services Provided—Cash or non-cash remuneration that represents a payment for past, present, or future teaching, research, or the performance of other services.

Condition of Employment—This test is met if lodging is required in order for the recipient to properly perform the duties of his or her employment. It is recommended that this requirement be identified in the recipient's job description.

Degree Candidate—A full or part-time student pursuing a degree at any college or university accredited to provide a program that is acceptable for full credit toward a baccalaureate or higher degree.

Educational Assistance Program—A plan of an employer for the exclusive benefit of its employees to provide such employees with educational assistance.

Employee—One who performs services for the State System and is subject to the System's direction and control. The following individuals are treated as an employee:

1. current salary or wage employee,
2. former employee who retired or left on disability,
3. widow or widower of an individual who died while an employee,
4. widow or widower of a former employee who retired or left on disability, or
5. dependent children/step children or spouse of any person listed in 1. through 4. above.

Note: This does not include a student worker.

Employer—The State System of Higher Education

Fee—A fixed charge established by a council of trustees or university president, according to Act 188, to recover costs of certain services, materials, or activities.

Graduate Assistant—An individual enrolled in post-baccalaureate studies who has been selected by the graduate department to perform certain services for the university in exchange for cash compensation and/or tuition remission.

Grant—Gift aid programs that require neither repayment nor work obligation from students (e.g., PHEAA, Pell Grants, SEOG, etc.).

Nonqualified Tuition and Related Expenses—Expenses/fees for room, board, books, supplies, equipment, travel, teaching, research, and other services provided to students not required for courses of instruction at an educational institution.

Nonresident Alien—Admitted to the U.S. for a temporary stay that will end when the purpose of that stay has been met. Employment authorization depends upon visa category grants by the Immigration and Naturalization Service (INS). This individual **is not** a U.S. citizen.

Qualified Tuition and Related Expenses—Expenses/fees for tuition, books, supplies and equipment required for the enrollment or attendance of a student at an educational institution.

Qualified Tuition Reduction—The reduction of tuition provided to an employee of a System university for education at another System institution. The tuition must be for education below the graduate level.

Resident Alien—(classified as an immigrant) A non-U.S. citizen who has been authorized to live and work in the U.S. indefinitely. This individual meets either the green card test or the substantial presence test.

Section 117 of the Internal Revenue Code (Scholarships)—This section of the code applies to the exclusion of gross income for any amounts received as a qualified scholarship/waiver (excluding employees). No services are performed for the qualified scholarship/waiver. A special rule applies to graduate assistants. For the purpose of this section, if the student is compensated reasonably for the value of any service performed, the scholarship/waiver received would be excludable from gross income.

Section 127 of the Internal Revenue Code (Educational Assistance Programs)— Assistance can be in the form of a payment, reimbursement, or waiver. This specific section of the code only applies to qualified educational expenses for undergraduate education up to the amount of \$5,250 per calendar year. For the purpose of this section, a spouse and/or dependent(s) is not considered an employee.

Section 132 of the Internal Revenue Code (Certain Fringe Benefits)—For the purpose of this section, any educational assistance reimbursement made by the employer to the employee is excludable from gross income if it is a working condition fringe benefit for the purpose of:

1. maintaining/improving skills required by the individual in his/her employment;
2. meeting the express requirement of the individual's employer; or
3. complying with applicable law or regulation imposed as a condition for the retention of the employee for an established employment relationship, status, or rate of compensation.

Scholarship—An amount paid for the benefit of a student at a State System institution to aid in the pursuit of studies. The student may be enrolled in either undergraduate or graduate course work.

Tuition—The basic charge established by the Board of Governors to supplement state appropriations in support of instruction and instructional services at a State System university.

Waiver—The full or partial reduction of tuition and/or fees assessed by a university for enrollment at a State System university.

Section II.

Applicable Regulatory Excerpts

Internal Revenue Code

Section 117—Qualified Scholarships

(a) General Rule

Gross income does not include any amount received as a qualified scholarship by an individual who is a candidate for a degree at an educational organization.

(b) Qualified Scholarship

For purposes of this section:

(1) In General

The term “qualified scholarship” means any amount received by an individual as a scholarship or fellowship grant to the extent the individual establishes that, in accordance with the conditions of the grant, such amount was used for qualified tuition and related expenses.

(2) Qualified Tuition and Related Expenses

For purposes of paragraph (1), the term “qualified tuition and related expense” means:

- (A) tuition and fees required for the enrollment or attendance of a student at an educational organization, and
- (B) fees, books, supplies, and equipment required for courses of instruction at such an educational organization.

(c) Limitation

Subsections (a) and (d) shall apply to that portion of any amount received which represents payment for teaching, research, or other services by the student required as a condition for receiving the qualified scholarship or qualified tuition reduction.

(d) Qualified Tuition Reduction

(1) In General

Gross income shall not include any qualified tuition reduction.

(2) Qualified Tuition Reduction

For purposes of this subsection, the term “qualified tuition reduction” means the amount of any reduction in tuition provided to an employee for education below the graduate level.

- (A) such as employee, or
- (B) any person treated as an employee (or whose use is treated as an employee).

(4) Special rules for teaching and research assistants. In the case of the education of an individual who is a graduate student at an educational organization and who is engaged in teaching or research activities for such organizations, paragraph (2) shall be applied as if it did not contain the phrase “below the graduate level.”

Section 127—Educational Assistance Programs

(a) Exclusion from Gross Income

(1) In General

Gross income of an employee does not include amounts paid or expenses incurred by the employer for educational assistance to the employee if the assistance is furnished pursuant to a program which is described in subsection (b).

(2) \$5,250 Maximum Exclusion

If, but for this paragraph, this section would exclude from gross income more than \$5,250 of educational assistance furnished to an individual during a calendar year, this section shall apply only to the first \$5,250 of such assistance so furnished.

(b) Educational Assistance Program

(1) In General

For purposes of this section, an educational assistance program is a plan of an employer for the exclusive benefit of its employees to provide such employees with educational assistance. The program must meet the requirements of the following paragraphs.

(2) Eligibility

The program shall benefit employees who qualify under a classification set up by the employer and found by the Secretary not to be discriminatory in favor of employees who are highly compensated employees or their dependents. For purposes of this paragraph, there shall be excluded from consideration employees not included in the program who are included in a unit of employees covered by an agreement which the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and one or more employers, if there is evidence that educational assistance benefits were the subject of good faith bargaining between such employee representatives and such employer or employers.

(4) Other Benefits as an Alternative

A program must not provide eligible employees with a choice between educational assistance and other remuneration includible in gross income. For purposes of this section, the business practices of the employer (as well as the written program) will be taken into account.

(6) Notification of Employees

Reasonable notification of the availability and terms of the program must be provided to eligible employees.

(c) Definitions; Special Rules

For purposes of this section:

(1) Educational Assistance

The term “educational assistance” means

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

(B) The provision, by an employer, of courses of instruction for such employee (including books, supplies, and equipment), but does not include payment for, or the provision of, tools or supplies which may be retained by the employee after completion of a course of instruction, or meals, lodging, or transportation. The term “educational assistance” also does not include any payment for, or the provision of any benefits with respect to, any course or other education involving sports, games, or hobbies. The term also does not include any payment for, or the provision of any benefits with respect to, any graduate level course of a kind normally taken by an individual pursuing a program leading to a law, business, medical, or other advanced academic or professional degree.

(2) Employee

An individual paid as an employee.

(3) Employer

An entity employing individuals as employees.

(5) Certain Tests Not Applicable

An educational assistance program shall not be held or considered to fail to meet any requirements merely because:

(A) of utilization rates for the different types of educational assistance made available under the program; or

(B) successful completion, or attaining a particular course grade, is required for or considered in determining reimbursement under the program.

(6) Relationship to Current Law

This section shall not be construed to affect the deduction or inclusion in income of amounts (not within the exclusion under this section) which are paid or incurred, or received as reimbursement, for educational expenses.

(7) Disallowance of Excluded Amounts as Credit or Deduction

No deduction or credit shall be allowed to the employee under any other section of this chapter for any amount excluded from income by reason of this section.

(d) Termination

This section shall not apply to expenses paid with respect to courses beginning after May 31, 2000.

Section 132—Certain Fringe Benefits

(a) Exclusion from Gross Income

Gross income shall not include any fringe benefit, which qualifies as a:

- (1) no-additional-cost service,
- (2) qualified employee discount,
- (3) working condition fringe,
- (4) de minimis fringe,
- (5) qualified transportation fringe, or
- (6) qualified moving expense reimbursement.

(d) Working Condition Fringe Defined

For purposes of this section, the term “working condition fringe” means any property or service provided to an employee of the employer to the extent that, if the employee paid for such property or services, such payment would be allowable as a deduction.

(h) Certain Individuals Treated as Employees for Purposes of Subsections (a)(1) and (2)

For purposes of paragraphs (1) and (2) of subsection (a):

(1) Retired and Disabled Employees and Surviving Spouse of Employee Treated as Employee

With respect to a line of business of an employer, the term “employer” includes:

(A) any individual who was formerly employed by such line of business and who separated from service with such employer in such line of business by reason of retirement or disability, and

(B) any widow or widower of any individual who died while employed by such employer in such line of business or while an employee.

(2) Spouse and Dependent Children

(A) In General

Any use by the spouse or a dependent child of the employee shall be treated as use by the employee.

(B) Dependent Child

For purposes of subparagraph (A), the term “dependent child” means any child of the employee:

- (i) who is a dependent of the employee, or
- (ii) both of whose parents are deceased and who has not attained age 25.

(8) Application of Section to Otherwise Taxable or Educational Training Benefits

Amounts paid or expenses incurred by the employer for education or training provided to the employee which are not excludable from gross income under Section 127 shall be excluded from gross income under this section (and only if) such amounts or expenses are a working condition fringe.

Pennsylvania Department of Revenue

Tax Reform Code of 1971

Article III of the Tax Reform Code of 1971 (Tax Reform Code) provides that every resident individual, estate or trust shall pay (be taxed on each dollar of income) for the privilege of receiving each of the classes of income from all sources, and that every nonresident individual, estate, or trust shall pay (be taxed on each dollar of income) from Pennsylvania sources (i.e., compensation earned for services performed in Pennsylvania). The Tax Reform Code provides the following eight classes of [taxable] income: 1) Compensation; 2) Interest; 3) Dividends; 4) Net income or [loss] from the operation of a business, profession or farm; 5) Net gain or [loss] from the sale, exchange or disposition of property; 6) Net income or [loss] from rents, royalties, patents and copyrights; 7) Estate and trust income; 8) Gambling and lottery winnings. 72 P.S. §§7302, 7303.

Under the Tax Reform Code, the term:

“Compensation” means and shall include [barring a specific exception under the code] salaries, wages, commissions, bonuses and incentive payments whether based on profit or otherwise, fees, tips and similar remuneration received for services rendered . . . whether in cash or in property.

The term “compensation” shall not mean or include:

* * *

(v) payments to reimburse actual [business] expenses;

* * *

(x) personal use of an employer’s owned or leased property or of employer provided services.

72 P.S. §7301 (d) (as amended by Act 45 of 1998), see also 72 P.S. §7303 (a) (1) and 61 Pa. Code §101.6.

“Scholarships, stipends, grants and fellowships shall be taxable as compensation, if services are rendered in connection therewith.” 61 Pa. Code §101.6. Scholarships and fellowship awards made on the basis of need or academic achievement for the purposes of encouraging or allowing the recipient to further his/her educational development and not as compensation for past or present services or in expectation of future employment are not taxable. Id. If a taxpayer believes his/her scholarship or fellowship award meets this requirement, he/she must attach an original detailed description of the program under which the scholarship, fellowship or stipend was granted. This must be an original letter and signed by the taxpayer’s department head or other official. The taxpayer must also attach to their Pennsylvania Personal Income Tax (PIT) return a detailed description of the program under which the award was granted (a form letter is not acceptable).

Fellowship awards and stipends constitute compensation for services if the recipient is required to apply his skill and training to advance research, creative work or some other project or activity, unless the recipient can show that:

1. The benefits resulting from the services of the recipient are so minimal, given the actual services performed or expected to be performed, that they constitute no realistic basis for compensation; or
2. The activities of the recipient are so closely and directly supervised and immediately controlled by regular faculty members so as to constitute a burden on the institution which would offset any benefit it receives from the recipient's activities; or
3. The recipient is a candidate for a degree and the same activities are required of all candidates for that degree as a condition to receiving such degree.

Local Taxing Authorities

Act 511

Compensation subject to the Pennsylvania Personal Income Tax and earned income are similar in many respects. The only three differences are that 1) the state does not tax personal **use** of an employer's property (i.e., cars, planes) while we do at the local level; 2) the state taxes both the employer's contribution **and income** of a **premature** retirement distribution while we tax only the portion representing the employer's contribution; and 3) the state does not tax the fair market value of employer provided dependent care benefits but we do.

If an employer does not withhold the earned income tax where it should have been withheld, and if attempts to collect the tax directly from the taxpayer are unsuccessful, the employer is responsible for the tax as though it had been levied against them.

Section III.

Taxability Decision Trees and Related Narratives

Student Scholarship/Waiver

Summary

Scholarship/waiver benefits provided to students, spouses, and/or dependents fall under Section 117 of the IRC. There are two classes of benefits, qualifying and non-qualifying. For the most part, qualifying benefits are not reportable nor are they taxable. Non-qualifying benefits are taxable but not reportable by the employer. However, the IRS recommends the employer notify the student of the possible taxability of this benefit and any taxable amounts should be claimed on the tax return by the student.

Background

A student may receive an exclusion from income for all or part of an amount received as tuition in the form of a scholarship/waiver. This is a benefit provided to a student at an educational institution to aid in the pursuit of studies. The student must be a candidate for a degree, enrolled in either undergraduate or graduate level course work, and the educational institution must maintain a regular faculty and curriculum and have a regularly enrolled body of students in attendance.

The student scholarship/waiver section will only address undergraduate level course work. The graduate level will be addressed in this manual under Graduate Assistant Tuition Waivers. There are two types of scholarship/waivers, referred to as either qualified or non-qualified. The Internal Revenue Code (IRC) defines the portion of the fee that is considered qualified and non-qualified. The type of benefit received will determine the exclusion and taxability of the benefit. In addition to the type of benefit received, if the student must provide service for this benefit, this will also have tax ramifications.

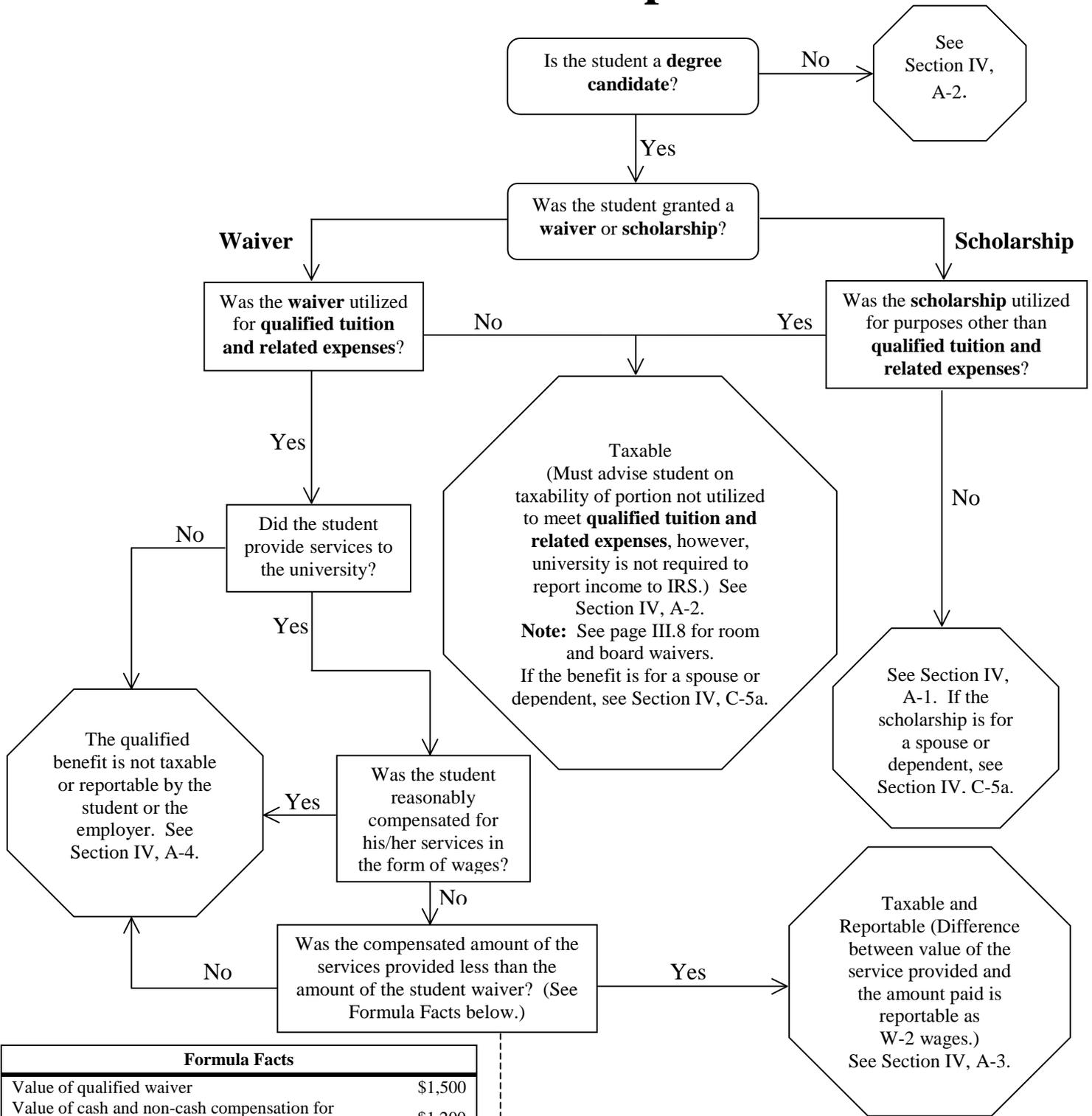
For the most part, qualified benefits are excludable from income. However, non-qualified benefits are subject to federal income tax and should be included in the students' income.

Tax Implications

Scholarship/waivers (e.g., Pell Grants, Supplemental Educational Opportunity Grants and PHEAA Grants) are excludable from income if they are used for tuition and course related expenses during the benefit period. Any non-qualifying benefit used for incidental expenses such as room and board, travel and research are taxable and includible in the students' income. If the student performed service, the value of the service is taxable as W-2 wages. However, if the value of the qualified benefit exceeds the value of the service performed, the excess is not taxable to the student.

The employer is not required to report on or withhold any tax for non-qualified scholarship/waiver benefit where services are not performed. The IRS recommends the employer advise the student that some or all parts of the scholarship/waiver may be taxable and reported on the students' tax return.

Student Scholarship/Waiver



Formula Facts	
Value of qualified waiver	\$1,500
Value of cash and non-cash compensation for services provided for qualified waiver	\$1,200
Value of wages paid via HRS	\$700
Taxable Non-cash Compensation	
Value of cash and non-cash compensation for services	\$1,200
Minus wages paid via HRS	- 700
Taxable non-cash compensation	\$ 500
Non-Taxable Waiver	
Value of waiver	\$1,500
Value of cash and non-cash compensation for services	- 1,200
Non-taxable waiver	\$ 300

Note: See page III.8 for Room and Board Waivers.

Graduate Assistantship Tuition Waiver

Summary

If full compensation is paid to graduate assistants for services rendered, there is no taxability of the educational assistance portion (e.g., waiver) of the assistantship. However, if full compensation is not paid, the university must determine the amount of educational assistance that is considered compensation for services rendered.

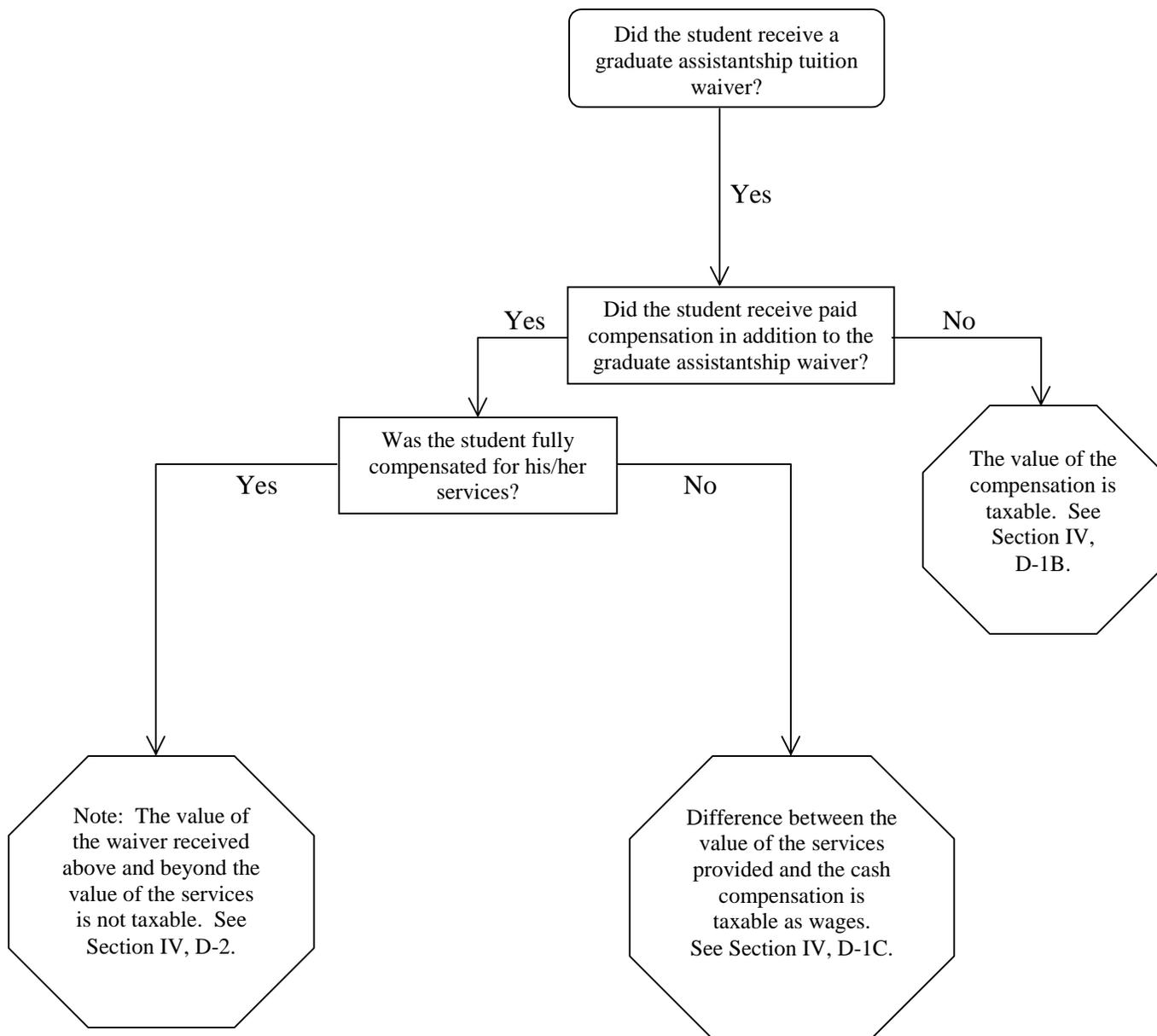
Background

A graduate assistantship is a form of educational benefit provided to graduate-level students. Typically, assistantships are granted by each university's graduate school, with the requirement that certain services be provided by the graduate assistant (GA) in return for the assistantship. Within the System, only Indiana University of Pennsylvania is permitted to offer teaching assistantships. All other System universities operating graduate schools may offer assistantships in return for the performance of research and/or other services. Cash compensation for services is authorized in accordance with Board Policy 1983-09-A, in the form of stipends. Minimum rates of pay cannot be less than the federally established minimum wage. Additionally, GAs receive an educational tuition benefit in the form of a waiver, concurrent with the performance of services. Educational assistance relating to assistantships granted in the form of a waiver is authorized by Board Policy 1983-18-A.

Tax Implications

Graduate assistantships are compensatory awards, subject to federal, state and local tax and income reporting. Depending on the appropriateness of cash compensation, the educational benefit of a waiver could also be subject to tax and income reporting.

Graduate Assistantship Tuition Waiver



Note: See page III.8 for Room and Board Waivers.

Employee Educational Assistance

Summary

Educational benefits in the form of undergraduate tuition waivers granted to individual employees up to \$5,250 per year are not taxable or reportable for federal income tax. The excess over \$5,250 is subject to federal tax withholding and income reporting unless work related.

Educational benefits in the form of undergraduate qualified waivers granted to a spouse and/or dependent(s) of an employee are not subject to tax withholding and income reporting at the federal level. Graduate level waivers granted to a spouse and/or dependent(s) of an employee is subject to federal, but not state and local withholding and income reporting.

Educational benefits in the form of a graduate waiver to an employee when the benefit is a condition of employment are not subject to tax withholding and income reporting.

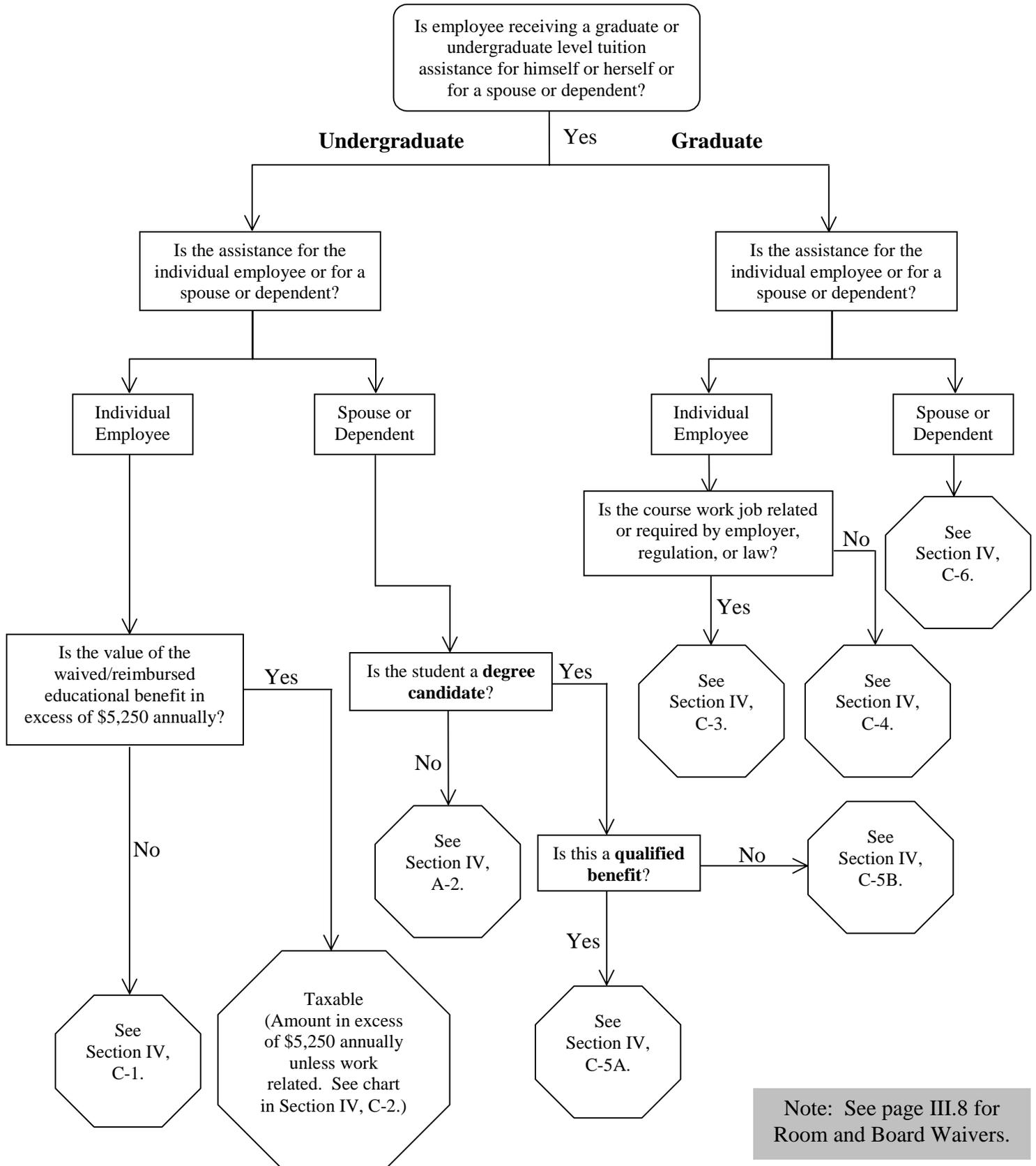
Background

In general, an educational assistance program is a plan of an employer for the exclusive benefit of its employees to provide such employees with undergraduate level educational assistance. Educational assistance is defined as the payment or waiver of tuition charges made by the employer for expenses incurred by or on behalf of an employee, for education of the employee. To be eligible, employees must meet the definition of an employee as listed in the Terms and Definitions section. For the State System of Higher Education, assistance is usually given to employees in the form of a qualified tuition waiver. However, in some cases, employees of the System universities along with employees of the Office of the Chancellor may be reimbursed for qualified tuition expenses incurred. State System university employees pursuing education at their place of employment usually are granted a tuition waiver to cover the cost of tuition, provided those employees are eligible for the assistance under the universities' plan. Certain eligible dependents of State System university employees pursuing education at other State System universities can be granted a tuition waiver to cover 50 percent of the cost of tuition.

Tax Implications

Educational assistance benefits are generally covered under Section 127 of the IRC. Section 127 of the Code excludes, from an employee's income, amounts paid by an employer for certain specified educational assistance provided to an employee for an undergraduate education up to a maximum of \$5,250 per calendar year. For purposes of the Section 127 exclusion, employee includes only the individual employee. Educational assistance provided to an employee's spouse and/or dependent(s) may not be excluded under Section 127 of the Code. However, the taxability of undergraduate tuition waivers provided to an employee's spouse or dependent(s) is covered under Section 117 of the IRC. Graduate level tuition waivers made to employees may only be excluded from income as a working condition fringe under Section 132 of the IRC.

Employee Educational Assistance



Note: See page III.8 for Room and Board Waivers.

Room and Board Waivers

Summary

All room and board waivers offered as educational assistance or compensation for service rendered are taxable income to the student recipients, unless they are provided for the convenience of the university (e.g., condition of employment). It is strongly suggested that System students who receive room and board waivers be notified that such waivers are considered taxable non-qualified scholarships or compensation for services rendered. In instances where compensation for services rendered is involved, each university must consider appropriate procedures to identify these types of arrangements and process appropriate tax withholding and reporting. Since no cash is paid out to the student, it is anticipated that tax withholding and remitting obligation must be borne by the university, and subsequently recovered through student accounting/billing procedures.

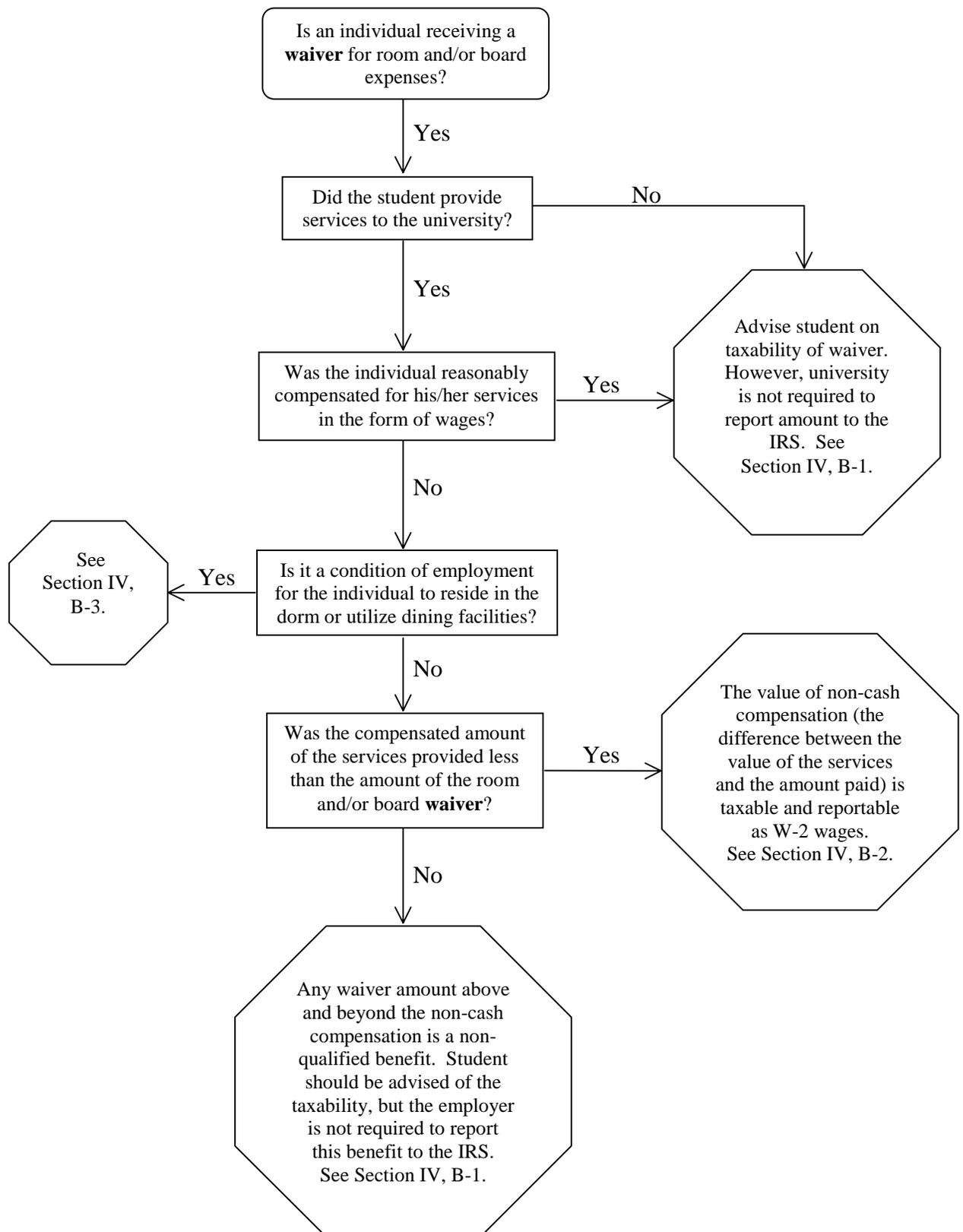
Background

Room and board waivers are forms of educational assistance provided to students. They can take the form of traditional educational assistance (e.g., non-qualified scholarships) or the form of non-cash compensation for services rendered. Authority for the granting of room and board waivers used for scholarship purposes is limited to eight specific classes of students, defined in Board of Governors Policy 1983-18-A. Subject to the Board of Governors' policies, authority for the granting of room and board waivers used for non-cash compensation for services rendered lies with Section 20-2010-A (1) of Act 188. This section delegates authority to university presidents to “. . .fix the salaries and benefits of employees, professional and non-instructional, and to establish policies and procedures governing . . . salary schedules.”

Tax Implications

Room and board waivers granted as educational assistance, non-cash compensation, or employment-related fringe benefits may be taxable income to the recipient and require the university to perform tax withholding and reporting obligations.

Room and Board Waivers



Nonresident Alien Scholarship/Waiver

Summary

Scholarship/waiver benefits provided to nonresident aliens fall under Section 117 of the IRC. They are divided into two classes of benefits: qualifying and non-qualifying. Reporting for the nonresident alien benefit is different than the U.S. resident as referenced in the tax implication section. This area of reporting is very complex and will be addressed at a later date.

Background

In general, all amounts paid to a nonresident alien in the form of a scholarship/waiver must be reported to the IRS, regardless of the amount paid or whether the amounts are taxable. This is accomplished on either Form 1042S or W-2, depending on whether services were performed to obtain the financial aid. Unless exempted under the IRC or by a tax treaty, all amounts are subject to federal income tax withholding at the rate of 30 percent. However, nonresident aliens who are temporarily present in the U.S. on an F-1, J-1, M-1, or Q-1 Visa are subject to withholding at only 14 percent of the taxable portion of the scholarship/waiver. Any scholarship/waiver or other financial aid paid to, or on behalf of, a nonresident alien which requires the recipient to perform services in exchange for the financial aid (such as graduate assistantships) is taxable as wages and reportable to the IRS, subject to the withholding rules.

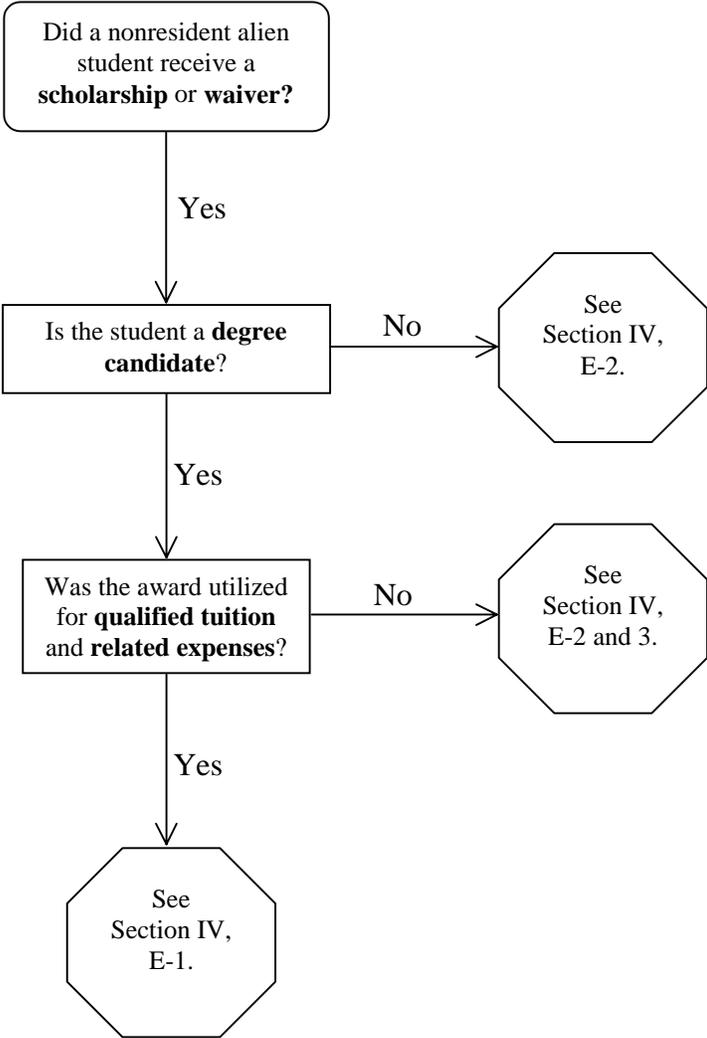
This section has the same application as the student scholarship/waiver section with the exception of the application of the nonresident alien status referenced earlier.

Tax Implications

Scholarship/waivers are excludible from income to the extent they are qualified benefits used for tuition and course-related expenses during the benefit period. Non-qualifying benefits used for incidental expenses such as room and board, travel, and research are taxable and includible in the students' income. If the student performed services, the value of the services is taxable. However, if the value of the qualified benefit exceeds the value of the services performed, the excess value is not taxable to the student, but it must be reported. Any benefit used for the non-qualified portion of the benefit is reportable and taxable to the nonresident alien.

Unlike the student scholarship/waiver application, the employer is required to report and/or withhold on all scholarship/waiver benefits. If the benefit is qualified, then reporting via Form 1042S is required but not subject to taxation. However, if it is a non-qualified benefit, withholding is required, reportable on Form 1042S. When services are performed for the benefit, reporting and taxation must occur, using the applicable percentages and/or Forms W-4 or 8233 exemption rules, reporting the wages and taxation on Form W-2 and exempt wages on Form 1042S.

Nonresident Alien Scholarship/Waiver



Section IV.

Withholding and Reporting Obligations

Withholding and Reporting Obligation Chart for Scholarships and Tuition Waivers

Subsection	Type of Scholarship/Waiver	Taxable			Form to be Filed		Benefits Code		
		Federal/ Social Security	State	Local	W-2	1042S			
Student Scholarship and Waivers									
A.	1.	The benefit(s) is a qualified scholarship/waiver. If benefit is for a spouse or dependent, see C-5a.	No	No	No	N/A	N/A	N/A	
	2.	The benefit(s) is a non-qualified scholarship/waiver. *Letter issued by university to student advising of possible tax liability. Taxable to student but not reportable by university. If benefit is for a spouse or dependent, see C-5b.	Yes*	No	No	N/A	N/A	N/A	
	3.	The dollar value of uncompensated work or services provided to the university for the waiver, up to the amount of waiver, is taxable and reportable as wages.	Yes	Yes	Yes	W-2	N/A	703	
	4.	The benefit(s) is a qualified waiver not for services or above the value of services. If benefit is for a spouse or dependent, see C-5a.	No	No	No	N/A	N/A	N/A	
Room and Board Waivers									
B.	1.	This is the same as a non-qualified scholarship waiver; it is taxable but not reportable. *Letter issued by university to student advising of possible tax liability. If benefit is for a spouse or dependent, see C-5b.	Yes*	No	No	N/A	N/A	N/A	
	2.	The dollar value of uncompensated work or services provided to the university for the waiver, up to the amount of waiver, is taxable and reportable as wages.	Yes	Yes	Yes	W-2	N/A	712	
	3.	If waiver is condition of employment	No	No	No	N/A	N/A	N/A	
Employee Educational Assistance									
C.	1.	Employee, undergraduate level, up to \$5,250 per calendar year.	No	No	No	N/A	N/A	N/A	
	2.	Employee, undergraduate, and over \$5,250 per calendar year.	Yes	No	No	W-2	N/A	722	
	3.	Employee, graduate level, condition of employment., or job related.	No	No	No	N/A	N/A	N/A	
	4.	Employee, graduate level, not a condition of employment, or job related.	Yes	No	No	W-2	N/A	724	
	5.	Spouse or dependent of an employee at the university undergraduate level.							
		a. Qualified Benefits	No	No	No	N/A	N/A	N/A	
		b. Non-qualified benefits	Yes	No	No	W-2	N/A	725	
	6.	Spouse or dependent of an employee at the university graduate level.	Yes	No	No	W-2	N/A	726	

Subsection	Type of Scholarship/Waiver	Taxable			Form to be Filed		Benefits Code
		Federal/ Social Security	State	Local	W-2	1042S	
Graduate Assistant Tuition Waiver							
D.	1. Provided services and received waiver:						
	a. Service	Yes	Yes	Yes	W-2	N/A	741
	b. Waiver	Yes	Yes	Yes	W-2	N/A	742
	c. Difference between value of the services provided and the cash compensation is taxable as wages.	Yes	Yes	Yes	W-2	N/A	743
	2. Waiver received was greater than value of services:	No	No	No	N/A	N/A	N/A
Nonresident Alien Scholarship/Waiver							
E.	1. Qualified scholarship/waiver not taxable but reportable by employer.	No	No	No	N/A	1042S	802
	2. Non-qualified scholarship/waiver	Yes (14% or 30%)	No	No	N/A	1042S	804
	3. Services provided for benefit, but not paid. *If no tax treaty exemption is claimed.	Yes*	Yes	Yes	W-2*	N/A	808
	¹ If tax treaty exemption is claimed and 8233 is filed. ² Note: W-2 must be filed for state and local regardless of federal form filed.	No ¹	Yes ²	Yes ²	W-2 ²	1042S ¹	809
Nonresident Alien Graduate Assistant Tuition Waiver							
E.	4. A. Provides services for benefit and is paid. No treaty—taxed as W-2 wages when individual receives pay check Treaty exempt—wages reported on 1042S as wages (for state and local wages W-2)						
	I. Qualified—value of waiver	No	No	No	No	1042S	811
	II. Nonqualified—value of waiver	Yes (14% or 30%)	No	No	No	1042S	812
	B. Provides services in exchange for waiver—not paid (no treaty) Value of services equal to value of waiver (if not equal, see E7)	Yes	Yes	Yes	W-2	N/A	813
	5. Did not provide service—qualified. *Not taxable but reportable by employer.	No*	No	No	N/A	1042S	815
	6. Did not provide service—non-qualified. Reportable and taxable	Yes (14% or 30%)	No	No	N/A	1042S	816

Subsection	Type of Scholarship/Waiver	Taxable			Form to be Filed		Benefits Code
		Federal/ Social Security	State	Local	W-2	1042S	
7.	Provides services, value of work or service is not equal to value of waiver and the individual is not paid. A.						
	I. Value of Services—no treaty	Yes	Yes	Yes	W-2	N/A	818
	II. Value of Services—treaty ² Note: W-2 must be filed for state and local regardless of federal form filed	No	Yes	Yes	W-2 ²	1042S	820
	B.						
	I. Value of Waiver —qualified	No	No	No	No	1042S	822
	II. Value of Waiver—nonqualified	Yes (14% or 30%)	No	No	No	1042S	824
Nonresident Alien Educational Assistance							
E. 8.	Undergraduate	No	No	No	N/A	1042S	828
9.	Spouse or dependent *Not taxable but reportable by employer.	No*	No	No	N/A	1042S	830
10.	Graduate employee *Not taxable but reportable by employer.	No*	No	No	N/A	1042S	832
11.	Graduate spouse or dependent	No	No	No	N/A	1042S	834

Withholding/Reporting Obligations

Background

The State System of Higher Education (System) has obtained a legal opinion identifying issues for reporting the taxability and withholding of income tax on certain scholarships, tuition waivers, and other related benefits. This reporting and withholding responsibility is in relation to the following.

Student Scholarships/Waivers for Tuition and/or Room and Board

Unless a scholarship, tuition, room, and board waiver represents payment for services by the student, neither the grantor nor the System is required to report information regarding the taxability of this type of scholarship. However, the Internal Revenue Service has recommended that the grantors and/or the educational institution advise the recipient in writing that selected amounts of this benefit are to be included in income. These amounts would include the amount of the scholarship in excess of the amount of any qualified tuition or related benefit (see definition of qualified benefit) and would generally be included in gross income.

If services are provided, the value of this service is reported on Form W-2 subject to FICA, federal, state, and local income tax. If this benefit is provided to a nonresident alien, depending on the Visa type and exemption filed using Form 8233, report the federal information on Form 1042S. Form W-2 is filed based on the applicable tax treaty, withholding requirements, or single and \$16 dollars biweekly. All services performed by a U.S. resident/nonresident alien are taxable and reportable on Form W-2 at the state and local levels.

Employee Educational Assistance

This assistance consists of a separate written plan by an employer to provide an exclusive benefit to an employee for educational assistance. This specific benefit is exclusive to Section 127 of the Internal Revenue Code and targets undergraduate programs up to \$5,250 per calendar year. Amounts in excess of \$5,250 for undergraduate assistance in a calendar year are taxable and reportable at the federal, but not the state and local levels. Graduate level benefits within this section of the code expired on June 30, 1996. However, if the benefits were for the convenience of the employer under a written plan, these benefits would not be taxable or reportable under Section 132 of the Internal Revenue Code.

You must be an employee providing services to receive this benefit. Services are taxable at the federal, state, and local levels and reportable on Form W-2. However, this benefit is not taxable at the state and local levels.

However, if this benefit is provided to an individual employee at the graduate level and is a condition of employment, it is not taxable at the federal, state, or local levels, nor is reporting required.

Under Section 117, undergraduate educational benefits provided to a spouse or dependent is considered not taxable at the federal, state, or local levels. Non-qualified undergraduate benefits are taxable at the federal level but not at the state and local levels.

Graduate educational assistance for a spouse or a dependent is taxable and reportable at the federal level.

Graduate Assistantship Tuition Waivers

This benefit is subject to Section 117 of the Internal Revenue Code and usually services are performed to receive this benefit. The value of service is taxable and reportable at the federal, state, and local levels. If a benefit is provided and the cash compensation does not equal the value of services provided, then the difference is taxable and reportable at the federal, state, and local levels on Form W-2. If services were not provided for a benefit, no taxability or reporting requirements occurs.

Nonresident Alien Scholarships/Waivers

The classifications of scholarships/waivers, room and board, employee educational assistance, including spouse and dependent benefits and the graduate assistantship are all treated the same as a U.S. resident for the nonresident alien with the exception, that all benefits must be reported regardless if they are taxable. If no exemptions were claimed, reporting and taxation would be reflected on Form W-2. If an exemption is claimed, the value of the scholarship or tuition waiver is reported on Form 1042S. It should be noted, where no federal tax is applicable but a 1042S is required, a form W-2 must be used to report the applicable state and local tax reporting and withholding requirements.

Concern for Collecting Taxes when Individual is not on Payroll

Issue

How do you collect taxes for an individual who receives a non-cash taxable benefit?

Background

Since the individual may be receiving a non-cash benefit and not physically receiving cash, the concern remains; how do you collect applicable payroll taxes from the employee for a taxable benefit? Because of the nature of the payment, the income and taxes must be accounted for and recorded via employer tax reporting on a Form 941 or 1042 to the IRS. In addition to the federal level, selected taxes must be collected and remitted to state and local levels, as well.

Collection Application

The State System of Higher Education's Human Resource Information System (HRIS) uses various earnings, taxes, deduction, and benefit codes to record, deduct, and charge labor and benefit costs as well as record the employer liability to a third party vendor. Through the application of a benefit code, and employee's social security, Medicare, federal, state, and local income tax can be applied to enable the system to record a taxable payment via tax application codes in the form of yes (Y) or no (N) indicators. This method allows appropriate costing and recording of labor and payroll expenses via an automated process.

This creates a receivable to the university. It is incumbent upon the appropriate university staff to identify and collect this debt.

Reference should be made to the HRIS earnings benefits table to map the appropriate taxable earnings and benefits code with the taxable benefit to ensure the taxable income is generated, taxes are applied, deducted, and reported.

Section V.

Failure to Withhold and Report

State System Liability for Failure to Withhold and Report on Certain Scholarships, Tuition Waivers, and Other Benefits

In general, the State System must deduct and withhold Social Security and federal income taxes on the amount of wages that are actually or constructively received by an employee within a given calendar year. If the tax is not withheld, the employer is liable for the amount of Social Security and federal income taxes required to be withheld from the employee's pay, as well as the employer's share of Social Security taxes.

However, if the State System can demonstrate that the employee paid his or her required taxes, the employer is relieved of this liability.

In addition to the established liability, the State System may be assessed penalties for failure to file and report taxable income. If the State System fails to file an employment tax return within one month of its due date, a penalty may be assessed equal to five percent of the tax required to be remitted. For each additional month for which there is a failure to file, an additional five percent penalty is added, to a maximum of 25 percent.

In addition to the penalty for failure to file, the Internal Revenue Service may impose a penalty on the failure to pay employment taxes. This penalty may not exceed 25 percent of the tax; however, the penalty for failure to file may be reduced by the penalty for failure to pay. Where the return is not filed within 60 days of the due date, a minimum penalty of the lesser of \$100 or 100 percent of the tax required to be shown on the return is imposed.

Also, the State System may be liable for a failure to deposit penalty (up to 15 percent of the tax) of the employer's share of employment taxes. This penalty would only apply to the employer's share of the tax not deposited.

In addition to these civil penalties, IRS may impose criminal penalties for intentional non-filing, the filing of false returns, and non-payment.

Section VI.

Sample Documents

These documents are provided as sample forms and, if desired, may be customized to meet university needs.

Date

Student Name
Address

Dear **(Student Name)**:

On behalf of the **(University)** Scholarship Committee, I am pleased to learn of your interest in **(University)**, and I am excited about offering you a scholarship to help defray your expenses. You should be commended for your fine academic credentials.

Specifically, you have been selected to receive the **(Name of Scholarship)**. This is a **\$XX** award for your **(school year of student such as freshman)** year. The amount of the scholarship will be deducted directly from your bill of **(amount per semester)**, thus reducing the amount you will owe. This is a renewable scholarship for up to **(X)** semesters of enrollment provided that you maintain minimal academic progress at the end of each academic year. You will be expected to complete a minimum of **(X)** credits successfully each year and have at least a **(X.X)** grade point average.

Under Internal Revenue Code, state, and local tax law certain scholarship awards are deemed to be taxable to the recipient. It is not the responsibility of **(University)** to determine the taxability, nor tax and report the value of any awarded scholarship to the Internal Revenue Service, state, or local authorities. However, you should be aware that all, or a portion, of this award may be taxable, and you are required to appropriately report the taxable value of the award when filing your tax returns. If you are not able to determine the taxability of an award, you should consult a tax professional to obtain assistance in appropriately reporting any taxable value of the award to the taxing authorities when filing your returns.

In order to confirm your interest in the scholarship listed above, please complete and return the enclosed scholarship notification form by **(Date)** to:

Address

Best wishes for continued academic success as you pursue your educational goals at **(University)**.

Sincerely,

(Signature)

Enclosure

Date

To: Employee
From: University Representative
Subject: Employee Tuition—Graduate Courses

University records indicate that you, your spouse, or dependent are enrolled in the **(Semester and Year)** for a graduate course(s) at **(University)**. The value of the graduate tuition employer-provided graduate educational assistance is taxable and subject to certain payroll taxes and withholding unless specific requirements are met. Generally, the value of your tuition may remain non-taxable if the course bears a direct relationship to your employment at **(University)**. This direct relationship is evidenced by employment of the following conditions: (1) the course is necessary to maintain or improve employment skills required for **your current position**, or (2) the course is an express **written** requirement at **(University)** in order for you to retain your **current position**.

However, regardless of the aforementioned, if the course is necessary for you to meet the minimum educational requirements of your current position or is part of a program that, when completed, will qualify you for a new profession, business, or trade, the value of the tuition will be taxable. Similarly, the value of the tuition will be taxable if you are otherwise paid or reimbursed by a tax-credit scholarship or other tax-exempt payment for the graduate course.

Please complete the attached questionnaire(s) **(one for each course)** and, if necessary, the course information sheet(s) and return them to the HRIS office by **(date)**.

The document should be completed and returned even if you dropped the class (unless your drop resulted in a 100 percent refund). If you fail to respond to this request, **(University)** is obligated to consider the value of your tuition taxable income on the **(Year)** W-2 form as well as subject to the applicable payroll tax withholding.

If you have any questions or require additional information, please contact the HRIS office at **(Address or phone number)**.

Attachment

Educational Assistance/Tuition Waiver Application Faculty, Staff, and Managers

All applicants are responsible for (1) completely filling out this form, (2) obtaining verification from the Human Resource office and a voucher before semester deadlines, and (3) submitting the approved voucher at time of registration.

Part I: Name of Faculty, Staff, or Management Employee Member (please print)

(Last)	(First)	(Initial)	(Semester)
(Social Security Number)	(University Department)	(Cost Center Number)	
<input type="checkbox"/> APSCUF Employee	<input type="checkbox"/> AFSCME Employee	<input type="checkbox"/> Manager	
<input type="checkbox"/> SCUPA Employee	<input type="checkbox"/> UPGWA Employee	<input type="checkbox"/> PNA Employee	
<input type="checkbox"/> Athletic Coach	<input type="checkbox"/> ROTC Staff	<input type="checkbox"/> Student Org. Employee	
<input type="checkbox"/> Physicians	<input type="checkbox"/> PSSU		

Part II: Name of Student (please print)

(Last)	(First)	(Initial)	(Semester)
(Mailing Address)	(City)	(State)	(Zip Code)
(Date of High School Graduation)	(Phone)		
	Do you have a bachelor's degree from this university or any other university?		<input type="checkbox"/> Yes <input type="checkbox"/> No
	How many credits have you completed as of the end of the most recent semester attended?		
What is your student status?	<input type="checkbox"/> Full-time <input type="checkbox"/> Part-time	<input type="checkbox"/> Undergraduate <input type="checkbox"/> Graduate <input type="checkbox"/> Non-credit	
How many credits are you planning to schedule for?	Undergraduate	Graduate	Non-credit
Education Assistance/Tuition Waiver is requested because:	<input type="checkbox"/>	student is an eligible employee of the university or affiliated organization.	
	<input type="checkbox"/>	student is an eligible dependent of an employee of the university.	
	<input type="checkbox"/>	student is the spouse of an employee of the university.	

Part III: Department Head/Supervisory Approval:

The student, who is also my employee, has my permission to attend courses during working hours.

(Signature)

If graduate level courses are being taken under this educational assistance program by employees of the university, the value of the educational assistance may **or** may not be taxable to the employee, depending on the nature of the courses taken. Graduate level courses are non-taxable if they are job-related according to the IRS definition. With respect to the listed graduate level courses taken by employees under this program, the supervisor or department head must complete the following questions:

Course 1: _____

Course 2: _____

Course 3: _____

Course 4: _____

Course 5: _____

1. Are these courses required by the university, or by law or regulation, to keep the employee's current salary, status, or job?

Yes	No

2. Do these courses maintain or improve skills required in the employee's present work?

Yes	No

3. Are these courses required in order to meet the minimum educational requirements to qualify the employee in his/her work or business?

Yes	No

4. Are these courses part of a program of study that will lead to qualifying the employee in a new trade or business?

Yes	No

Courses meet the IRS definition of job-related if the answer to **either** questions 1 **or** 2 is yes **and** the answers to questions 3 **and** 4 are **both** no. Below, provide any additional information about the employee's job, and how the course relates to his/her work. If the education provides the employee in the new profession, trade or business, it is taxable even if they do not intend to enter that trade or business.

I certify that I am the employee's supervisor or department head, this form is completed accurately, and the course is job-related.

(Signature)

Enrollment Verification and Questionnaire

Name and Address	Social Security No.	Term	Course	Full- or Part-time

Check the appropriate answers. Provide additional information where indicated.

1. Is this course necessary for you to meet the minimum education requirements of your current position at (university)? Yes No

If **yes**, do not continue. Simply sign and return this form. Your benefit is taxable.
If **no**, go to question 2.

2. Is this course part of a program of study that will qualify you for a new trade, business, or profession? Yes No

If **yes**, do not continue. Simply sign and return this form. Your benefit is taxable.
If **no**, go to question 3.

3. Are you otherwise paid or reimbursed by a tax-exempt scholarship or other tax-exempt education assistance payment for this course? Yes No

If **yes**, do not continue. Simply sign and return this form. Your benefit is taxable.
If **no**, go to question 4.

4. Are you taking this course as an express (written) requirement of (university) to retain your current position? Yes No

If **yes**, attach a copy of the agreement that contains the written requirement, sign, and return this form. Your benefit is not taxable. (Subject to review.)
If **no**, go to question 5.

5. Does this course maintain or improve the skills you need in your current position at (university)? Yes No

If **yes**, fill out the attached course information sheet, sign, and return along with this form. Your benefit is not taxable. (Subject to review.)
If **no**, sign and return this form. Your benefit is taxable.

I declare that I have examined this statement and that the information I have provided is true, correct, and complete to the best of my knowledge and belief.

Signature _____
Date

Course Information Sheet

Employee Name: _____

Department: _____

Job Title: _____

Course Name: _____

Course Content: _____

Specific skills used on your job on a **regular basis** that are maintained or improved by this course.

1. _____
2. _____
3. _____
4. _____
5. _____
6. _____



State System of Higher Education Application for Tuition Waiver Benefit

To be completed by Employee or Annuitant (please print)

Name of: Employee
 Annuitant

Social Security Number: _____ Bargaining Unit: _____

Name of Employing University: _____

Name of Student: _____

Social Security Number: _____ Date of Birth: _____

Relationship of Student to Employee/Annuitant: _____

Name of Attending University: _____

Semester/Year _____ / _____

Percentage of Tuition Waiver: _____ %

Employee or Annuitant Verification: I hereby certify that the above-named student qualifies as my child or spouse and meets the qualifications as defined by the Board of Governors' policy. I agree to provide to the university proof of relationship and age as may be required. I understand it is my responsibility to meet the deadlines for tuition payment at the university attended by the student.

Employee/Annuitant Signature

Date

(Guardian or Beneficiary may provide verification of relationship in the event of employee's/annuitant's death)

Return to Employing University's Human Resources Department

University Use Only

Human Resources Department at employing university: The employee's/annuitant's eligibility and student's qualifications for the tuition waiver have been reviewed, and I hereby certify that the information submitted is true and accurate to the best of my knowledge.

Signature

Date

Forward to Business Office at university attended by student.

Business Office must forward copies to other appropriate offices at attending university.