

# COLLEGE of CHARLESTON

## OFFICIAL POLICY

2.2.1

**Scholarships, Fellowships, Stipends, Prizes, and Awards**

10/13/2020

### **Policy Statement**

The College of Charleston (CofC) will apply and follow the taxation rules of the Internal Revenue Service (IRS), the financial aid rules of the U. S. Department of Education, and the immigration laws of the U. S. Department of Homeland Security for all payments of scholarships, fellowships, stipends, prizes and awards.

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### **Policy Manager and Responsible Department or Office**

Admissions Office, Financial Aid Office, Center for International Education, Controller's Office, and Treasurer's Office.

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### **Departments/Offices Affected by the Policy**

All campus departments and students.

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## Policy

### SCOPE AND BACKGROUND:

- A. This information will serve as a guide to faculty, staff and students for preparing documents to pay scholarships, fellowships, stipends and other awards to students and individuals. Taxation of these amounts can vary greatly based on the provisions of the grant, the use of the proceeds, the status of the recipient, and whether the recipient is required to perform services in return for the award. These issues become ever more important in light of increased IRS scrutiny of the colleges and universities.
- B. Ordinarily, the amount of a qualified scholarship (refer to Section E under “Scope and Background” for the definition of a qualified scholarship) is not included in the income of the recipient for tax purposes if the recipient is a candidate for a degree at an appropriate educational institution (Internal Revenue Code (IRC) 117(a)). Consideration of a qualified scholarship requires using the amount received for qualified tuition and related expenses, in accordance with the terms of the scholarship, fellowship, or grant IRC 117(b) (1). The IRC provides that the qualified tuition and related expenses include: tuition and fees required for enrollment and attendance at the institution, and fees, books, supplies, and equipment required for specific courses of instruction at the institution (IRC 117(b) (2)).

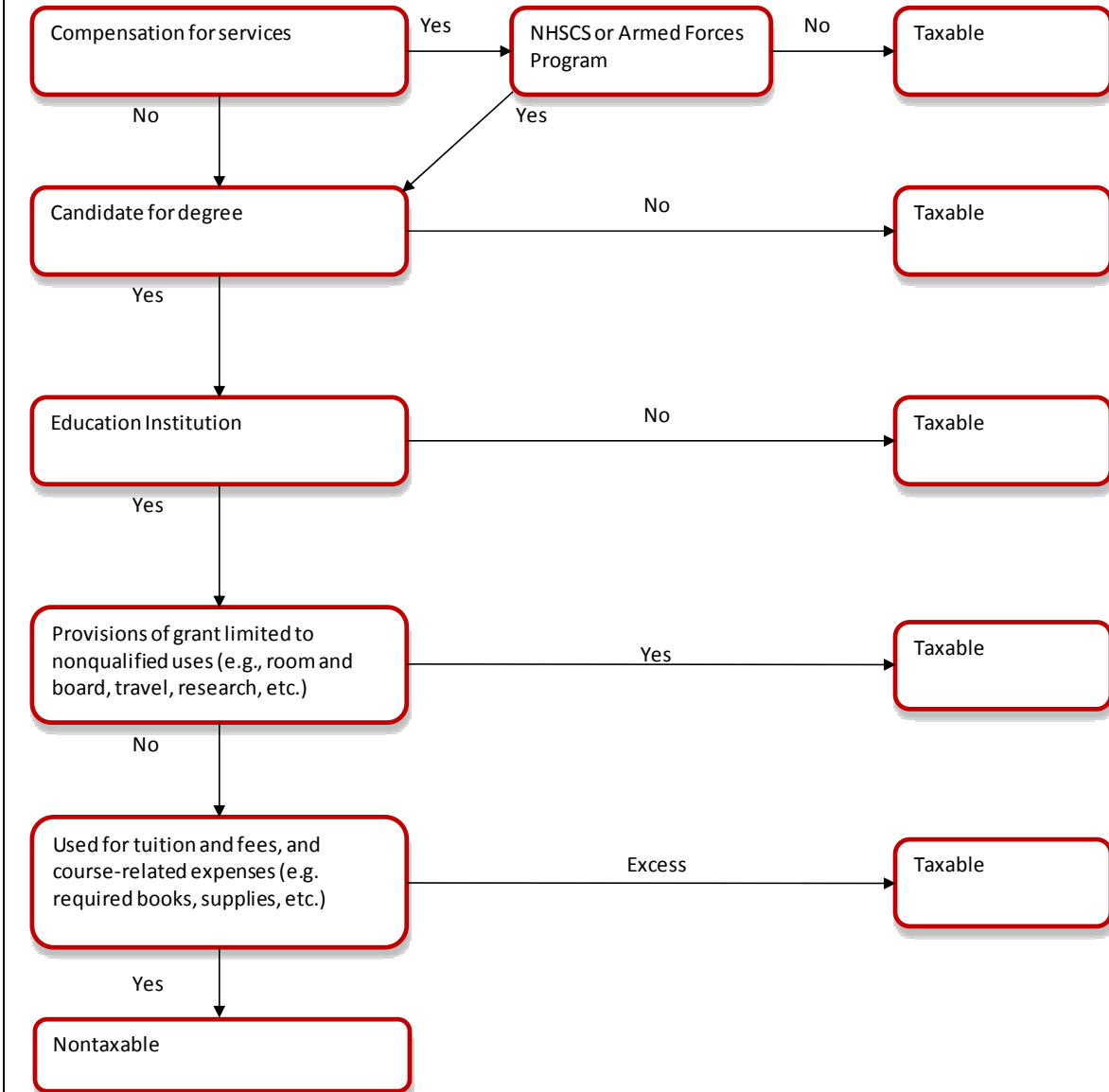
Nonetheless, if the recipient must provide current or future services (e.g., teaching, research, or other services by the student required as a condition for receiving the qualified scholarship or qualified tuition reduction) as a condition of the scholarship, the portion that represents payment for such services should not be excluded from the recipient’s income (IRC 117(c)). Amounts received under the National Health Service Corps Scholarship (NHSCS) Program and the F. Edward Hebert Armed Forces Health Professions Scholarship and Financial Assistance (Armed Forces) Program are eligible for tax-free treatment without regard to any service obligation imposed on the recipient after December 31, 2001.

- C. Essentially, three basic criteria determine whether a scholarship award is taxable.
1. Is payment a qualified scholarship – If the payment is considered a qualified scholarship (i.e. 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), then such amount should not be included in the student’s income. If not, then the amount may be included in a student’s income but the College need not report the amount as wages unless the scholarship constitutes compensation for services.
  2. Is payment compensation for services – ***Even if the payment is considered a qualified scholarship, the College must determine whether any portion of the amount constitutes payment for services.*** To the extent an amount constitutes payment for services; the student should include the amount in his or her income.

3. Reporting and recordkeeping requirements – The College may have a withholding obligation and duty to report amounts constituting payment for services/wages to the Internal Revenue Service (IRS). Additionally, a student should retain records to substantiate any scholarship or fellowship amount not included in income. Finally, students may need to report amounts included in income for purposes of filing an individual income tax return.

### Exclusion of Scholarships, Fellowships, or Stipends

*(This chart is used to illustrate whether taxability of the income)*



**D. Qualified Scholarships** – To qualify for exclusion under IRC section 117, the first inquiry is whether the funds paid or credited to a student’s account constitute a scholarship or fellowship grant.

1. Scholarship or Fellowship Grants

A scholarship or fellowship grant is a cash sum paid to aid an individual in the pursuit of study or research and may come from an educational institution, government agency, charity, or other source. This payment would include any reduction in the amount owed by an individual for tuition, room and board, and other fees. For tax law purposes, the focus is on whether the amounts meet the definition of a scholarship or fellowship as provided in the IRC. Upon determination that a payment meets the definition of a scholarship or fellowship grant, the payment must be assessed to establish whether it is a qualified scholarship.

a. Relationship between the Grantor and the Recipient

The relationship between the grantor and the recipient may affect whether the amount involved is considered a scholarship or fellowship grant.

b. Employment Relationship

Generally, the courts have developed a “quid pro quo” (an equal exchange or substitution) test to determine whether the amount received is the result of the employer’s “disinterested generosity” or whether the amount is “bargained for consideration” (see *Bingler v. Johnson*, 394 U. S. 741 (1969)).

c. Athletic Scholarships

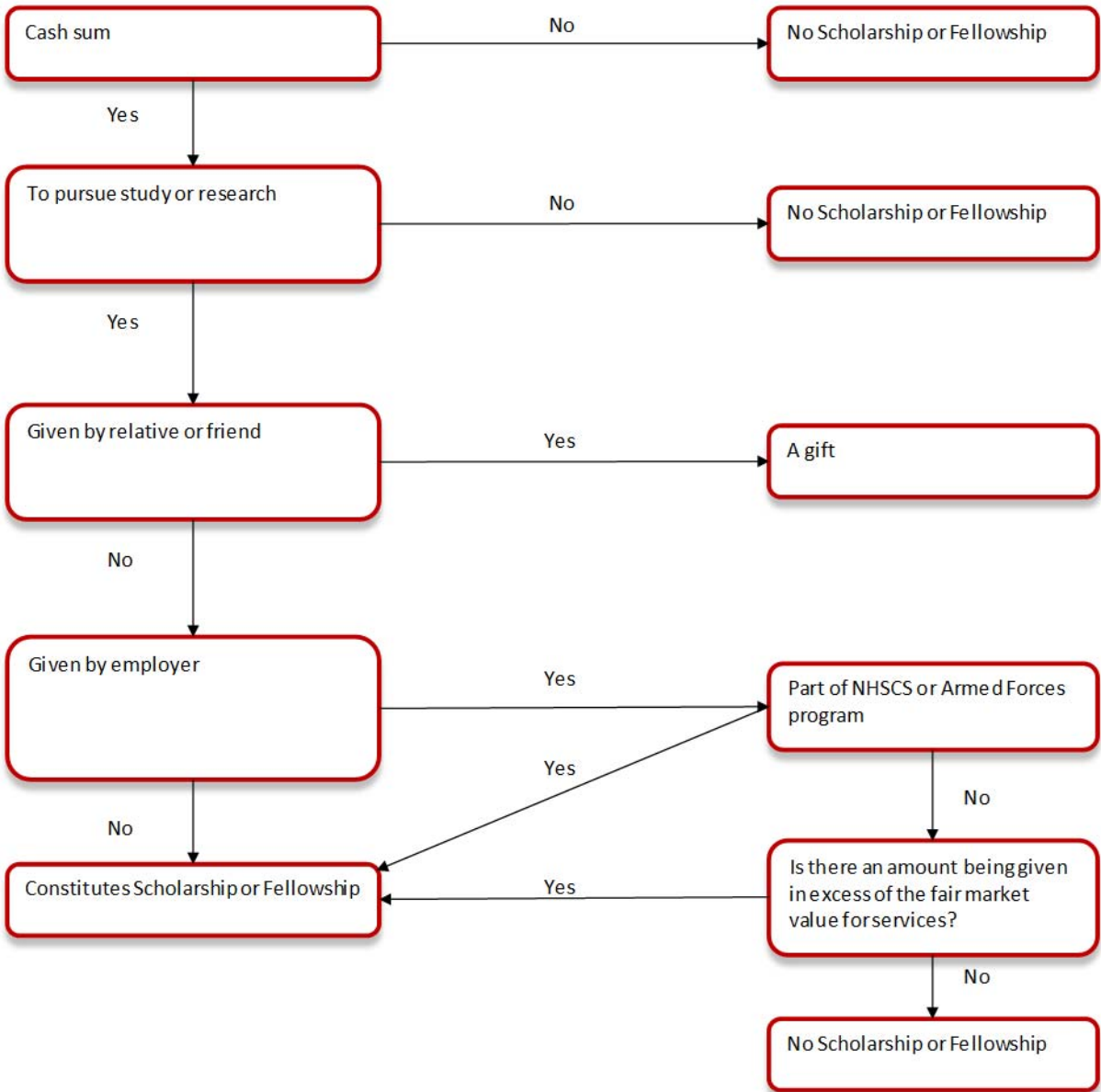
Per the IRS ruling (Publication 970), athletic scholarships are not taxable. Under current law, scholarship amounts used for tuition and required fees, books, supplies, and equipment are not considered income, subject to the requirements and limitations outlined in this policy. The exclusion, however, does not apply to incidental expenses such as room and board.

d. Is it a Scholarship or Fellowship Grant?

Scholarships usually refer to grants in support of undergraduate education, and fellowships usually refer to grants in support of post-baccalaureate projects, or to pre-baccalaureate projects pursued outside the normal curriculum. All scholarships and fellowships are grants.

The terms “scholarship” and “fellowship” are often used interchangeably to describe a grant or another type of funding for academic achievement. More often than scholarship awards, fellowship grants will include an internship or other service commitment, often for a period of one or more years.

### Scholarship or Fellowship?



## 2. Qualified Tuition and Related Expenses

- a. A qualified scholarship is excluded from the recipient's taxable income only if the proceeds are used for qualified tuition and related expenses. It is the responsibility of the recipient to establish that the amounts received qualify. To the extent the student is not able to substantiate the appropriate use of funds if asked by the IRS; the student could be required to recognize taxable income. If the grant specifies that funds cannot be used for qualified tuition and related expenses, then the award cannot be considered a qualified scholarship and would be taxable to the recipient.
- b. With respect to related expenses, to qualify for exclusion from income, the fees, books, supplies and equipment must be required of all students taking the particular course. Incidental expenses are taxable to the recipient.

## 3. Candidate for a Degree

A scholarship or fellowship grant is tax free (excludable from gross income) only if you are a candidate for a degree at an eligible educational institution.

You are a candidate for a degree if you:

- a. Attend a primary or secondary school or are pursuing a degree at a college or university, or
- b. Attend an educational institution that:
  - 1) Provides a program that is acceptable for full credit toward a bachelor's or higher degree, or offers a program of training to prepare students for gainful employment in a recognized occupation; and
  - 2) Is authorized under federal or state law to provide such a program and is accredited by a nationally recognized accreditation agency.

## **E. When is a Scholarship, Fellowship, or Grant Considered Compensation for Services?**

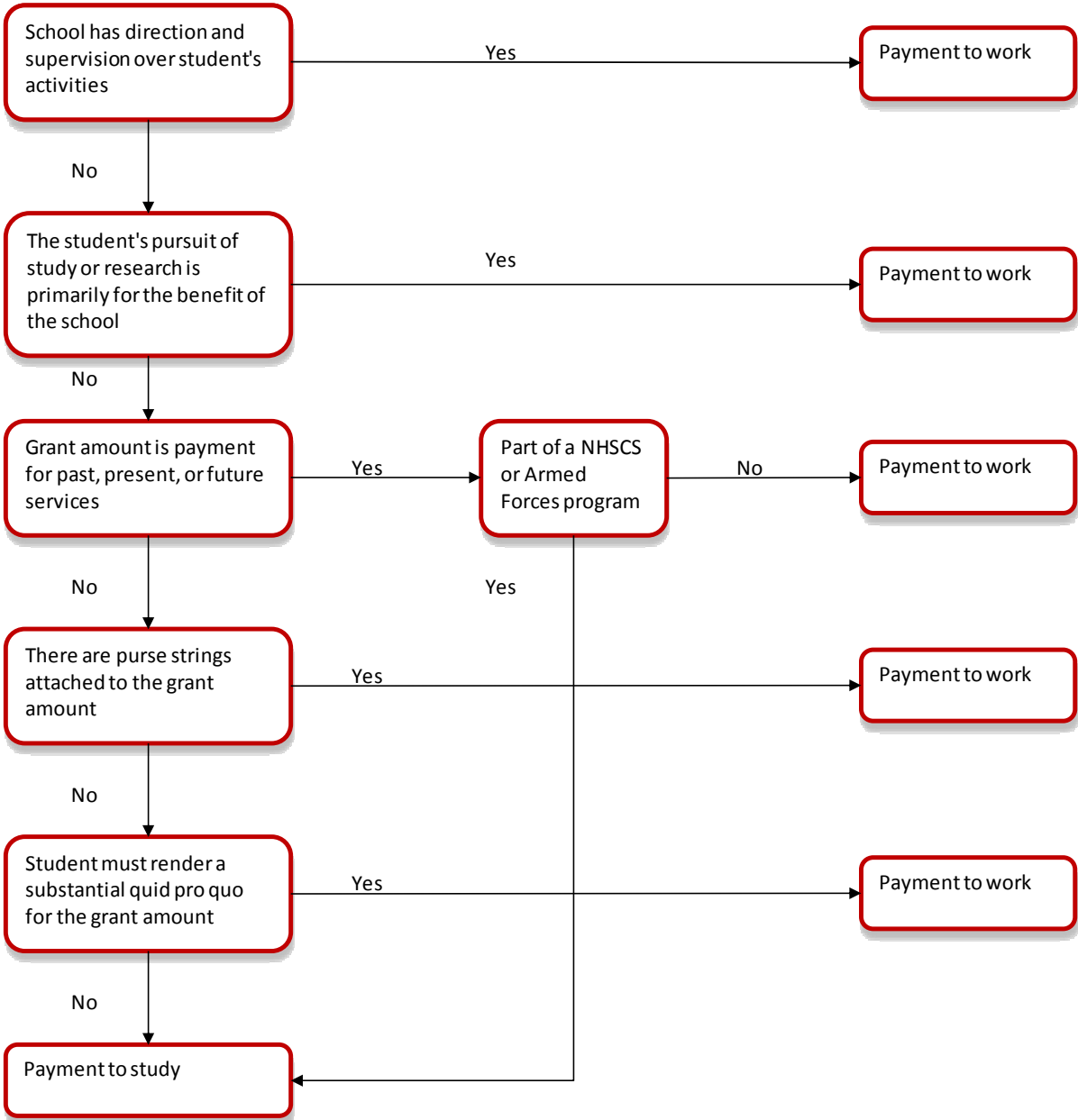
Amounts received by a student for teaching, research, or other services that are a condition of receiving a scholarship are not excluded from the student's income except in the case of NHSCS or Armed Forces programs. Two standards developed under prior law help to distinguish payment for services from scholarship, fellowships or grants eligible for exclusion. These two standards include the "primary purpose" test and the "primary benefit" test. A determination must be made as to whether a student's activities are for the "primary benefit" of the College or whether the student's activities have the "primary benefit" of furthering the student's education and training.

Basically, the query is whether the funds were primarily designed to further the education of the recipient or to compensate them for their services. Stated another way, is the money for development of the individual or for the development of a product, i.e., specific research? The following information lists some of the key considerations in determining the primary/purpose benefit of a scholarship award.

1. Does the College have direction or supervision over the student's activities?
2. Is the student pursuing studies or research "primarily for the benefit" of the College?
3. Does the scholarship, fellowship, or grant represent payment for services in the past, present, or future?
4. Is the College "relatively disinterested" (IRS specifically stated, "the awards are not paid for or in connection with the performance of services, and appear to be relatively disinterested grants to participants to enable them to pursue programs of independent development, training, and original study, focusing on the experience to be gained by the recipient rather than on any guarantor benefit)."
5. Is the student required to render a substantial quid pro quo for the scholarship, fellowship, or grant?
6. The fact that the student must submit periodic reports to the College is not determinative. The requirement to submit reports, by itself, does not indicate it represents compensation for services.

See table on next page.

### Payment to Study or Work?





## PROCEDURES:

### A. Reporting Obligations of the College of Charleston

1. If the student is a U.S. resident for tax purposes, the College has no reporting responsibility with respect to scholarship awards if such amounts are:
  - a. Considered a qualified scholarship (as defined in the Scope and Background section of this policy); and
  - b. Not considered compensation for services.
2. The Controller (or designee), the principal investigator, and the Director of the Office of Research and Grants Administration (ORGA) will determine whether a payment is a qualified scholarship by reviewing the grant documentation to verify the following assertions. To determine if a payment is a qualified scholarship within the externally funded grant document, the award must state to the effect that:
  - a. The payment must be for tuition and required fees required for enrollment and attendance at the institution;
  - b. Books, supplies, and equipment are required for courses of instruction at the institution; and
  - c. The recipient is not required to render current or future services as a condition of the scholarship.
3. If the externally funded grant document is silent on what use is to be made of the funds, then the College will take the position that it is for qualified purposes.
4. If the externally funded grant document states that the funds are to be used for something other than tuition and fees, then it is **not** for a qualified purpose.
5. Taxation and Method of Payment of Scholarships, Fellowships and Stipends.
  - a. Unless a scholarship or fellowship grant is subject to the provisions of Section 117(c) of the Internal Service Revenue Code and that is “. . . gross income includes any portion of amounts received as a scholarship or fellowship grant representing payment for teaching, research, or other services required as a condition for receiving the qualified scholarship,” **the College will not file a return of information with respect to such grant.**

Furthermore, unless section 117(c) of the Code applies, the amount of scholarship or fellowship grant is not considered wages. Thus, such amount is not subject to section 3402 (relating to withholding for income taxes), section 3102 (relating to withholding under the Federal Insurance Contribution Act

(FICA) or section 3301 (relating to the Federal Unemployment Tax Act (FUTA)).  
**Therefore, the payment must be initiated through the Financial Aid Office.**

- b. A scholarship or fellowship grant that is includible in gross income under section 117(c) of the Code is considered wages for purposes of section 3401(a). The application of FICA and FUTA depends on the nature of the employment and the status of the organization. In addition, the College or grantor is subject to IRS provisions related to reporting of wages of employees, and is required to file Form W-2 with respect to amounts provided as a scholarship or fellowship grant. For example, if the college reduces a student's tuition solely in return for performing services that are required as a condition to receiving the scholarship, the college must file Form W-2 reflecting the amount of the reduction. **In this case the scholarship or fellowship is taxable, and payment must be initiated through the College's Career Center.**
- c. Where a **portion** of a scholarship is granted in return for services described in IRC section 117(c), the Controller (or designee), the principal investigator, and the Director of ORGA will make a good faith allocation, based on all the facts and circumstances, to determine that portion of the amount that represents compensation for services provided by the recipient.
  - 1) The recipient of the income will be required to complete a Student Employment Hire form for payment of the portion that constitutes employment services.
  - 2) The portion of income for payment of employment services will be reduced from the amount reported to the Financial Aid Office.
- d. *Form 1099-MISC will not be used to report scholarship or fellowship grants. Scholarships or fellowship grants that are taxable to the recipient because they are paid for teaching, research, or other services as a condition for receiving the grant are considered wages and must be reported on Form W-2. Other taxable scholarship or fellowship payments (to a degree or non-degree candidate) may be reported to the IRS on Form 1042-S (e.g. taxable scholarships to nonresident aliens (NRA's)).*
- e. As for 1098-T (Tuition Statement) reporting, the College is required by the Internal Revenue Service to report to students the amount of qualified tuition and related expenses that have been billed to the student during the calendar year, if those expenses are greater than qualified scholarships received during the same calendar year. The amount paid on the student's behalf is not recorded on the 1098T. Only qualified expenses billed during the calendar year are recorded on the form.

## B. Stipends, Prizes, Awards

### 1. Stipends

- a. The first consideration for paying a stipend to an individual is to determine why the person is receiving the income. Does the payment represent compensation for past, present or future employment services or represent payment for services which primarily benefits the grantor? Or does it enable the individual to further his education and training in his individual capacity? And, explained another way were the funds designed to further the education of the student or to compensate him for his services?
- b. Upon review of documentation in the grant proposal, the Controller (or designee), the principal investigator, Human Resources, and the Director of ORGA will use the IRS criteria to determine whether the income constitutes compensation for services versus an educational or a training experience for the student or individual. In some cases, where the proposal demonstrates that the student is engaged in both, the parties (principal investigator, Human Resources, ORGA and Controller's Office) will determine a percentage of services performed versus educational experience.
- c. The payments of stipends follow the same guidelines as described under I. Procedures, E. Taxation and Method of Payment of Scholarships, Fellowships, and Stipends.

### 2. Prizes and Awards

- a. Prizes and awards are amounts received primarily in recognition of religious, charitable, scientific, educational, artistic, literary, or civic achievement, or are received as the result of entering a contest. A prize or award is taxable to the recipient unless **all** of the following conditions are met:
  - 1) the recipient was selected without any action on his or her part to enter the contest or proceeding;
  - 2) the recipient is not required to render substantial future services as a condition to receive the prize or award; and
  - 3) the prize or award is transferred by the payer to a governmental unit or tax-exempt charitable organization as designated by the recipient.
- b. Prizes or awards paid to students can be processed through the Accounts Payable Unit using the Expense Authorization (EA) form but must be reported to the Financial Aid Office. It is the responsibility of the requestor of the payment to notify the school.

- c. Payments to non-CofC employees or State employees otherwise that meet the definition of prizes and awards as described above may be processed through the Accounts Payable Unit using the EA. Payments to State including CofC employees require processing through the appropriate payroll offices.
- d. If restrictions are imposed, such as for travel, or room and board, then it is no longer considered a prize or award, and should be treated as a scholarship.

### C. Requirement to Flow through the Financial Aid System

1. Per Title IV of the Higher Education Act of 1965, the College signs a participation agreement that requires the coordination and communication of all aid awarded to a student. If the scholarship/fellowship income (stipend) is primarily to educate the student in an individual capacity and the student is enrolled in a course at the College of Charleston, the portion of the payment not deemed employment must flow through the Financial Aid Office. When the payment flows through Financial Aid, the activity will post to the student information system and any payment of surplus aid will result in a system-generated student refund check. For any surplus aid, the student has the obligation of reporting the tax liability associated with the income, thereby relieving the College of the obligation.
2. If the individual is a CofC student but not enrolled in a course at the College of Charleston – usually circumstances surrounding summer school, the payment will be made through the accounts payable process using an EA. The Controller's Office will notify the Financial Aid Office of the payment so that the student's financial record is adjusted accordingly.
3. If the payment is to a CofC student for compensation of employment services or research/studies primarily benefiting the grantor, the payment must be handled by the Career Services Center (the office that handles student employment.)
4. If the individual is a student but not a College of Charleston student and the payment is considered an award to educate in an individual capacity, the College will pay the appropriate Financial Aid Office of the school where the student is enrolled. If the income is for compensation of employment services, the payment requires handling through the CofC Human Resources and Payroll Offices.
5. If the income is for a prize or award as described under Procedures, Section I. F.2. Prizes and Awards above, the payment may be processed through the accounts payable process if it is determined that the prize/award money is not compensation for services.

**D.** Guide to what portion of the use of the proceeds of a scholarship, stipend, or fellowship grant is to be treated as taxable or nontaxable.

<b>Scholarships, Fellowships, and Stipend awards</b>	
Payment for:	Taxable / Non-taxable
Tuition	Non-taxable
Fees	Non-taxable*
Books	Non-taxable*
Supplies	Non-taxable*
Equipment	Non-taxable*
Room	Taxable
Board	Taxable
Travel	Taxable
Teaching	Taxable
Research Services	Taxable
Other Services	Taxable
* If required of all students taking the course	

**E.** How should payments made to nonresident aliens be treated with respect to tax withholding?

1. Once the College has determined the residency status of the payee, the Controller (or designee), the principal investigator, Payroll Officer and the Director of ORGA will determine the type of payment being made. After the payment type has been determined, the College will begin with the premise that all payments from U.S. sources made to or on behalf of a nonresident alien are taxable unless the payment can be excluded or exempted from tax withholding.
2. The Controller (or designee) and Payroll Officer will determine whether the College has a withholding obligation and duty to report amounts constituting payment for services/wages.
3. In the event that a scholarship represents payment for services, the College will comply with any applicable withholding and reporting requirements including:
  - a. Wage reporting on Form W-2, "Wage and Tax Statement," and Form 941, "Employer's Quarterly Federal Tax Return;"
  - b. Withholding of federal and state income taxes;
  - c. Withholding of FICA, if applicable; and
  - d. Payment of federal or state unemployment tax, depending upon the circumstances.

4. FICA rules provide an exception for services performed by a student who is enrolled and regularly attending classes at a college, university, or school.

**DEFINITIONS:**

**Scholarship** – generally an amount paid for the benefit of a student at an educational institution to aid in the pursuit of studies. The student may be either an undergraduate or graduate. These payments generally support educational needs, such as tuition, fees, room, board, and supplies.

**Fellowship** – generally an amount paid for the benefit of an individual to aid in the pursuit of study or research. No past, present, or future services are expected in return for the support.

**Stipend** – as defined by the Internal Revenue Service regulations is a “fixed sum of money paid periodically for services or to defray expenses. The fact that remuneration is termed a “fee” or “stipend” rather than salary or wages is immaterial. Wages are generally subject to employment taxes and should be reported on Form W-2.

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**Related Policies, Documents or Forms**

Internal Revenue Service (IRS) Publication 970 (Tax Benefits for Education)

Internal Revenue Service Code (IRC) 117 (Qualified Scholarships)

National Health Service Corps Scholarships Program (NHSCS) – <https://nhsc.hrsa.gov/>

U. S. Department of Education Higher Education Act of 1965 Title IV (Student Assistance); Part A (Grants to Students in Attendance at Institutions of Higher Education); Section 454 [20 U.S.C. 1087d] (Agreements with Institutions)

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**Related Policies, Documents or Forms**

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**Review Schedule**

<b>Issue Date: 5/16/2007</b> <b>Date of Policy Review: 10/13/2020</b>	<b>Next Review Date:10/15/2025</b>
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<b>POLICY APPROVAL</b> <b>(For use by the Office of the Board of Trustees or the Office of the President)</b>	
Policy Number: 2.2.1 (Scholarships, Fellowships, Stipends, Prizes, and Awards)	
President or Chairman, Board of Trustees	 _____
	Date: <u>10/13/2020</u>