

**DESCRIPTION OF H.R. 3393, THE  
“STUDENT AND FAMILY TAX SIMPLIFICATION ACT”**

Scheduled for Markup  
by the  
HOUSE COMMITTEE ON WAYS AND MEANS  
on June 25, 2014

Prepared by the Staff  
of the  
JOINT COMMITTEE ON TAXATION



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## INTRODUCTION

The House Committee on Ways and Means has scheduled a committee markup of H.R. 3393, the “Student and Family Tax Simplification Act,” on June 25, 2014. This document,<sup>1</sup> prepared by the staff of the Joint Committee on Taxation, provides a description of the bill.

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<sup>1</sup> This document may be cited as follows: Joint Committee on Taxation, *Description of H.R. 3393, the “Student and Family Tax Simplification Act”* (JCX-71-14), June 23, 2014. This document can also be found on our website at [www.jct.gov](http://www.jct.gov).

**A. Modification of Tax Benefits For Tuition and Tax Treatment of Certain Scholarships  
(secs. 25A, 117, and 222 of the Code)**

**Present Law**

**Tax credits for qualified tuition and related expenses**

Hope credit and American Opportunity credit

For taxable years beginning before 2009 and after 2017, an individual may claim a tax credit, the Hope credit, for qualified tuition and related expenses paid for the first two years of the student's post-secondary education in a degree or certificate program.<sup>2</sup> Although temporarily superseded by the American Opportunity tax credit (described below), the Hope credit in 2014, if it were in effect, would be 100 percent on the first \$1,300 of qualified tuition and related expenses, and 50 percent on the next \$1,300 of qualified tuition and related expenses, for up to \$1,950 per eligible student per year.<sup>3</sup> These dollar amounts are indexed for inflation, with the amount rounded down to the next lowest multiple of \$100.<sup>4</sup> Thus, for example, the Hope credit for a taxpayer who incurs \$1,300 of qualified tuition and related expenses for an eligible student (subject to the modified adjusted gross income ("MAGI") phaseout described below) would be \$1,300. If a taxpayer incurs \$2,600 of qualified tuition and related expenses for an eligible student, then the Hope credit would be \$1,950.

The Hope credit that a taxpayer may otherwise claim is phased out ratably for taxpayers with MAGI between \$55,000 and \$65,000 (\$110,000 and \$130,000 for married taxpayers filing a joint return) for 2014.<sup>5</sup> MAGI includes certain otherwise excludable income earned by U.S. citizens or residents living abroad or in certain U.S. territories.<sup>6</sup> The beginning points of the MAGI phaseout ranges are indexed for inflation, with the amount rounded down to the next lowest multiple of \$1,000. The size of the phaseout ranges for single and married taxpayers are always \$10,000 and \$20,000 respectively.<sup>7</sup>

A taxpayer may not claim the Hope credit if the qualified tuition and related expenses for the enrollment or attendance of a student, if the student has been convicted of a Federal or State

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<sup>2</sup> Sec. 25A(a)(1).

<sup>3</sup> Sec. 25A(b)(1). The \$1,300 amount, determined by the staff of the Joint Committee on Taxation, is the statutory amount of \$1,000, indexed for inflation from 2001.

<sup>4</sup> Sec. 25A(h).

<sup>5</sup> Based on inflation adjustments determined by the staff of the Joint Committee on Taxation.

<sup>6</sup> Sec. 25A(d)(3).

<sup>7</sup> Sec. 25A(d)(2)(B).

felony offense consisting of the possession or distribution of a controlled substance before the end of the taxable year.<sup>8</sup> Additionally, a taxpayer must include the name and taxpayer identification number of the student on whose behalf the qualified tuition and related expenses were paid in order to be eligible for the credit.<sup>9</sup>

The credit is allowable against both the regular tax and the alternative minimum tax (“AMT”).

For taxable years beginning after December 31, 2008, and before January 1, 2018, an individual may claim the American Opportunity tax credit (“AOTC”), which is a modified version of the Hope credit.<sup>10</sup> The maximum allowable AOTC is \$2,500 per eligible student per year for qualified tuition and related expenses paid for each of the first four years of the student’s post-secondary education in a degree or certificate program. The AOTC rate is 100 percent on the first \$2,000 of qualified tuition and related expenses, and 25 percent on the next \$2,000 of qualified tuition and related expenses.<sup>11</sup> For purposes of the AOTC, the definition of qualified tuition and related expenses is expanded to include course materials. Forty percent of a taxpayer’s otherwise allowable AOTC is refundable. The AOTC that a taxpayer may otherwise claim is phased out ratably for taxpayers with MAGI between \$80,000 and \$90,000 (\$160,000 and \$180,000 for married taxpayers filing a joint return).<sup>12</sup> Neither the credit rate nor the phaseout thresholds are indexed for inflation.

#### Lifetime Learning credit

An individual taxpayer may claim a nonrefundable tax credit, the Lifetime Learning credit, equal to 20 percent of qualified tuition and related expenses incurred during the taxable year on behalf of the taxpayer, the taxpayer’s spouse, or any dependents.<sup>13</sup> Up to \$10,000 of qualified tuition and related expenses per taxpayer return are eligible for the Lifetime Learning credit (i.e., the maximum credit per taxpayer return is \$2,000). In contrast with the Hope credit, the maximum credit amount is not indexed for inflation.

In contrast to the Hope and American Opportunity tax credits, a taxpayer may claim the Lifetime Learning credit for an unlimited number of taxable years.<sup>14</sup> Also in contrast to the

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<sup>8</sup> Sec. 25A(b)(2)(D).

<sup>9</sup> Sec. 25A(g)(1).

<sup>10</sup> Sec. 25A(i).

<sup>11</sup> Sec. 25A(i)(1).

<sup>12</sup> Sec. 25A(i)(5).

<sup>13</sup> Sec. 25A(c).

<sup>14</sup> Sec. 25A(a)(2).

Hope and American Opportunity tax credits, the maximum amount of the Lifetime Learning credit that may be claimed on a taxpayer's return does not vary based on the number of students in the taxpayer's family—that is, the Hope credit is computed on a per student basis while the Lifetime Learning credit is computed on a family-wide basis. The Lifetime Learning credit amount that a taxpayer may otherwise claim is phased out ratably for taxpayers with MAGI between \$55,000 and \$65,000 (\$110,000 and \$130,000 for married taxpayers filing a joint return) in 2014. These phaseout ranges are the same as those for the Hope credit as it applies for tax years beginning before 2009, and are similarly indexed for inflation.

### **Deduction for qualified tuition and related expenses**

For taxable years ending prior to January 1, 2014, an individual who has not elected to take the above-described credits is allowed an above-the-line deduction for qualified tuition and related expenses for higher education paid by the individual during the taxable year.<sup>15</sup> Qualified tuition includes tuition and fees required for the enrollment or attendance by the taxpayer, the taxpayer's spouse, or any dependent of the taxpayer with respect to whom the taxpayer may claim a personal exemption, at an eligible institution of higher education for courses of instruction of such individual at such institution. The expenses must be in connection with enrollment at an institution of higher education during the taxable year, or with an academic term beginning during the taxable year or during the first three months of the next taxable year. The deduction is not available for tuition and related expenses paid for elementary or secondary education.

The maximum deduction is \$4,000 for an individual whose AGI for the taxable year does not exceed \$65,000 (\$130,000 in the case of a joint return), or \$2,000 for other individuals whose AGI does not exceed \$80,000 (\$160,000 in the case of a joint return).<sup>16</sup> No deduction is allowed for an individual whose AGI exceeds the relevant AGI limitations, for a married individual who does not file a joint return, or for an individual with respect to whom a personal exemption deduction may be claimed by another taxpayer for the taxable year.<sup>17</sup> The deduction is not available for taxable years beginning after December 31, 2013.

Additionally, a taxpayer must include the name and taxpayer identification number of the student on whose behalf the qualified tuition and related expenses were paid in order to be eligible to claim the deduction.<sup>18</sup>

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<sup>15</sup> Sec. 222(a).

<sup>16</sup> Sec. 222(b)(2)(B).

<sup>17</sup> See secs. 222(c) and (d).

<sup>18</sup> Sec. 222(d)(2).

## **Tax treatment of qualified scholarships**

Present law provides an exclusion from gross income and wages for amounts received as a qualified scholarship by an individual who is a candidate for a degree at a qualifying educational organization.<sup>19</sup> Generally, the exclusion does not apply to amounts received by a student that represent payment for teaching, research, or other services by the student as a condition for receiving the scholarship.<sup>20</sup>

In general, a qualified scholarship is any amount received by such an individual as a scholarship or fellowship grant if the amount is used for qualified tuition and related expenses.<sup>21</sup> Qualified tuition and related expenses include tuition and fees required for enrollment or attendance, or for fees, books, supplies, and equipment required for courses of instruction, at the qualifying educational organization.<sup>22</sup> This definition does not include regular living expenses, such as room and board. Thus, for example, the portion of a Federal Pell Grant under section 401 of the Higher Education Act of 1965<sup>23</sup> (“Pell Grant”) that exceeds qualified tuition and related expenses is not a qualified scholarship and is included in an individual’s gross income. A qualifying educational organization is an educational organization which normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on.<sup>24</sup>

## **Coordination of tax benefits for qualified tuition and scholarships**

The amount of qualified tuition and related expenses paid, for purposes of computing the value of the Hope, American Opportunity, or Lifetime Learning credits, as well as the deduction for qualified tuition and related expenses, generally includes only out-of-pocket expenses. Qualified tuition and related expenses do not include expenses covered by employer-provided educational assistance and scholarships that are not required to be included in the gross income of either the student or the taxpayer claiming the credit. Thus, total qualified tuition and related expenses are reduced by any scholarship or fellowship grants excludable from gross income under section 117 and any other tax-free educational benefits received by the student (or the taxpayer claiming the credit) during the taxable year.

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<sup>19</sup> Secs. 117(a) and 3121(a)(20).

<sup>20</sup> Sec. 117(c).

<sup>21</sup> Sec. 117(b)(1).

<sup>22</sup> Sec. 117(b)(2).

<sup>23</sup> 20 U.S.C. 1070(a).

<sup>24</sup> Sec. 117(b)(2)(A).

## **Description of Proposal**

### **Consolidation and modification of tuition credits and deduction**

The proposal permanently replaces the Hope credit with a modified version of the AOTC, and repeals both the Lifetime Learning credit and the now-expired deduction for qualified tuition expenses. As under present law, the credit rate is 100 percent on the first \$2,000 of qualified tuition and related expenses, and 25 percent on the next \$2,000 of qualified tuition and related expenses, for a maximum credit of \$2,500. Under the proposal, the taxpayer's credit for the first \$1,500 of qualified tuition and related expenses is refundable.

The proposal lowers the phaseout range of the credit. The credit phases out for joint filers with MAGI between \$86,000 and \$126,000, and for all other filers with MAGI between \$43,000 and \$63,000. Both the credit amounts and the phaseout ranges are indexed for inflation for taxable years beginning after 2018.

The proposal repeals the provision that denies the credit with respect to qualified tuition and related expenses for the enrollment or attendance of any student who has been convicted of a felony offense consisting of the possession or distribution of a controlled substance.

The proposal adds a provision requiring a taxpayer to include the employer identification number of the institution to which qualified tuition and related expenses was paid.

### **Coordination of Pell Grants with credit for tuition**

The proposal contains a provision that alters the determination of qualified tuition and related expenses for students who are recipients of Pell Grants. Under the proposal, for purposes of reducing the amount of qualified tuition and related expenses owing to receipt of scholarships, the recipient of the Pell Grant may disregard an amount of the Pell Grant equaling the amount of expenses (other than qualified tuition and related expenses) that are taken into account in determining the cost of attendance (as defined in section 472 of the Higher Education Act of 1965). That is, the student may first apply the Pell Grant to certain living expenses before any excess is deemed to reduce the amount of tuition and related expenses eligible for the AOTC. For example, under present law, if a student had \$2,000 in tuition and related expenses, \$4,000 in living expenses related to the cost of attendance, and received a \$3,000 Pell Grant, the student would not be eligible for any AOTC because the qualified tuition and related expenses (\$2,000) is reduced by the amount of the Pell Grant (\$3,000), leaving no qualified tuition and related expenses. Under the proposal, the \$3,000 Pell Grant is disregarded to the extent of living expenses related to the cost of attendance (\$4,000), thus leaving the full \$2,000 in qualified tuition and related expenses eligible for the AOTC.

### **Modification of treatment of Pell Grant scholarships**

The proposal modifies the exclusion for qualified scholarships by providing that Pell Grants are excluded from gross income, without regard to whether the grant is used for qualified tuition and related expenses.



**Effective Date**

The proposal applies to taxable years beginning after December 31, 2014.

## B. Estimated Revenue Effects

Fiscal Years [Billions of Dollars]												
<u>Item</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>2024</u>	<u>2015-19</u>	<u>2015-24</u>
Revenues [1]...	0.2	4.7	5.0	4.7	-8.0	-7.6	-8.5	-8.3	-8.3	-8.9	6.7	-35.0

**NOTE:** Details do not add to totals due to rounding.

	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>	<u>2023</u>	<u>2024</u>	<u>2015-19</u>	<u>2015-24</u>
[1] Estimate contains the following outlay effects...	---	3.0	2.8	2.7	9.6	9.6	10.2	10.2	10.2	10.8	18.1	69.2