

Taxation of Noncompensatory Scholarships and Fellowships¹

I. General

In general, a noncompensatory scholarship or fellowship grant is a cash amount paid or allowed to, or for the benefit of, an undergraduate or graduate, to aid such individual in the pursuit of his/her study or research. A scholarship or fellowship grant may also be a reduction in the amount owed by the recipient to an educational organization for tuition, room and board, or any other fee.

If services are required in exchange, the payment is classified as compensation rather than scholarship or fellowship. Please refer to Compensatory Stipend vs. Noncompensatory/Scholarship Stipend Guidelines :

<http://www.depts.ttu.edu/payroll/tax-compliance/tax-manual/documents/stipend-guidelines.pdf>

II. Qualified Scholarships (Excludable from Income)

A qualified scholarship is the amount of a scholarship or fellowship grant that is used for tuition and fees, books, supplies, and equipment required for courses. Items must be required of *all* students in your course of instruction to be tax free. If equipment or supplies is merely "suggested" for the course, the amounts do not qualify as qualified scholarships.

The amounts representing qualified scholarships are not subject to tax withholding or tax reporting requirements. However, **all** scholarships or fellowship grants received by a *non-degree* candidate are considered income.

III. Non-Qualified Scholarships (Includable in Income)

Any amounts received for incidental expenses or by a non-degree candidate are taxable scholarships/fellowships. Incidental expenses include room and board, travel, and expenses for equipment and other items that are not required for either enrollment or attendance in a course of instruction.

Internal Revenue Service (IRS) Notice 87-31 states that the payor of a taxable scholarship/fellowship is not required to withhold income tax and is not required to report the payment either to the student or the IRS. This "no withholding/no reporting" rule only applies to *non-compensatory* scholarship/fellowship payments. Please be aware of the fact that Texas Tech University/Health Sciences Center (TTU/TTUHSC) follows this "no withholding/no reporting" rule. ***As a result, it is the student's responsibility to maintain records and properly report all non-qualified scholarships received as income on such student's tax return regardless of the fact that TTU/HSC will not report the payment to the student or the IRS.***

¹ The information contained herein applies to U.S. citizens and resident aliens (as determined for tax purposes) only. Nonresident aliens that receive scholarships or fellowship grants should review the information contained in the document titled "Taxation of Nonresident Aliens".

IV. Compensation for Services (Includable in Income)

An amount represents *compensation for services*, and **not** a scholarship or fellowship grant if:

1. the amount represents compensation for past, present, or future employment services;
2. the activity the payments fund is subject to the direction or supervision of TTU/TTUHSC; or
3. the payment enables the recipient to pursue studies or research *primarily for the benefit of TTU/TTUHSC*.

With respect to research activities, an issue often arises whether the research activities constitute "services" or "independent research." Factors that the IRS and the courts have taken into account in making this determination include:

- The grant was awarded to the institution rather than the student.
- The extent of faculty supervision of the student's work, including planned time schedules and required progress reports.
- The student's ability to direct the course and direction of the research activities.
- Whether the student is able to retain any patents or copyrights resulting from his or her efforts.
- Whether the research services are directly related to the fulfillment of a contractual commitment by the university.
- Whether the student is required to work a specified number of hours a week on the research project.
- Whether the payment made to the student was relatively small (generally indicative of a fellowship) or relatively large (generally indicative of compensation).
- Whether the student would continue to receive payments if he/she did not continue to perform the required services.
- Whether the university treated the student as an employee as evidence by withholding tax on the payments as wages and providing faculty privileges and other employee benefits.

These compensated services are considered wages for employment tax purposes and are subject to employment tax withholding and reporting requirements.