

Reg. Section 1.25-5A(b)(3)

Special rules relating to characterization and timing of payments. . .

(a) Educational expenses paid by claimed dependent. For any taxable year for which the student is a claimed dependent of another taxpayer, qualified tuition and related expenses paid by the student are treated as paid by the taxpayer to whom the deduction under section 151 is allowed.

(b) Educational expenses paid by a third party.

(1) In general. Solely for purposes of section 25A, if a third party (someone other than the taxpayer, the taxpayer's spouse if the taxpayer is treated as married within the meaning of section 7703, or a claimed dependent) makes a payment directly to an eligible educational institution to pay for a student's qualified tuition and related expenses, the student is treated as receiving the payment from the third party and, in turn, paying the qualified tuition and related expenses to the institution.

(2) Special rule for tuition reduction included in gross income of employee. Solely for purposes of section 25A, if an eligible educational institution provides a reduction in tuition to an employee of the institution (or to the spouse or dependent child of an employee, as described in section 132(h)(2)) and the amount of the tuition reduction is included in the employee's gross income, the employee is treated as receiving payment of an amount equal to the tuition reduction and, in turn, paying such amount to the institution.



(3) Examples. The following examples illustrate the rules of this paragraph (b). In each example, assume that all the requirements to claim an education tax credit are met. The examples are as follows:

Example (1). Grandparent D makes a direct payment to an eligible educational institution for Student E's qualified tuition and related expenses. Student E is not a claimed dependent in 1999. For purposes of claiming an education tax credit, Student E is treated as receiving the money from her grandparent and, in turn, paying her qualified tuition and related expenses.

Example (2). Under a court-approved divorce decree, Parent A is required to pay Student C's college tuition. Parent A makes a direct payment to an eligible educational institution for Student C's 1999 tuition. Under paragraph (b)(1) of this section, Student C is treated as receiving the money from Parent A and, in turn, paying the qualified tuition and related expenses. Under the divorce decree, Parent B has custody of Student C for 1999. Parent B properly claims Student C as a dependent on Parent B's 1999 federal income tax return. Under paragraph (a) of this section, expenses paid by Student C are treated as paid

by Parent B. Thus, Parent B may claim an education tax credit for the qualified tuition and related expenses paid directly to the institution by Parent A.

Example (3). University A, an eligible educational institution, offers reduced tuition charges to its employees and their dependent children. F is an employee of University A. F's dependent child, G, enrolls in a graduate-level course at University A. Section 117(d) does not apply, because it is limited to tuition reductions provided for education below the graduate level. Therefore, the amount of the tuition reduction received by G is treated as additional compensation from University A to F and is included in F's gross income. For purposes of claiming a Lifetime Learning Credit, F is treated as receiving payment of an amount equal to the tuition reduction from University A and, in turn, paying such amount to University A on behalf of F's child, G.