



TAXATION OF SCHOLARSHIP GRANT AID

Summary: The tax treatment of scholarship aid creates unnecessary barriers for low-income students. Expanding the allowable tax-free uses of scholarship and grant aid would better support these students and enhance access.

Background: Since 1986, scholarship and grant aid, including Pell Grants, used for non-tuition costs like room and board have been taxed. Even when this policy was enacted, supporters of the overall tax reform package criticized this specific policy.

“I am also concerned about the effects of this bill on higher education,” [Rep. Tim Valentine \(D-NC\)](#) said, despite his overall support for the package. “Increased taxation of scholarships, fellowships, and academic awards and prizes, all taken together, could have a devastating impact on some institutions.”

While bipartisan concerns existed 40 years ago, the problem has been exacerbated as non-tuition higher education costs have risen and with the recent trend of more generous institutional financial aid programs. A significant share of the average student’s cost of attendance consists of expenses that—if covered by scholarship and grant aid—would make that portion of the aid taxable, [according to College Board data](#).

Figure 1: Average Estimated Full-Time Undergraduate Budgets (Enrollment-Weighted) by Sector, 2025–2026

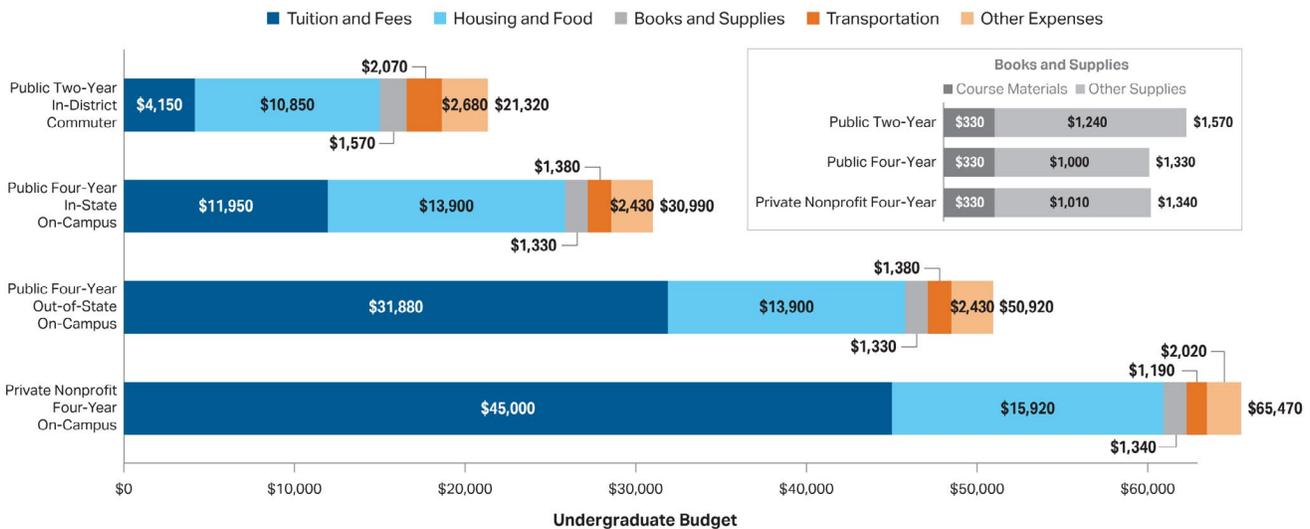


FIGURE CP -1 Average Estimated Full-Time Undergraduate Budgets (Enrollment-Weighted) by Sector, 2025-26, page 11, *Trends in College Pricing and Student Aid 2025*, College Board

In fact, non-tuition expenses that can make scholarship aid taxable account for well over half of the costs of attendance for community college students (79 percent) and students attending four-year, in-state public institutions (60 percent) as well as a significant portion of the costs (31 percent) for students attending private nonprofit institutions.

Table 1: 2025–2026 Taxable Expenses in Average Student Budgets

Public Two-Year In-District Commuter	79%
Public Four-Year In-State On-Campus	60%
Public Four-Year Out-of-State On-Campus	37%
Private Nonprofit Four-Year On-Campus	31%

Note: Calculations using data from College Board's *Trends in College Pricing and Student Aid 2025*

Not only are the share of these expenses high, but their overall costs have also risen dramatically since 1986. From 1998–99 (the earliest available College Board data) to the present, the inflation-adjusted costs of items that would make grant aid taxable has skyrocketed. For community college students, these costs have more than doubled.

Table 2: Inflation-Adjusted Average Cost of Taxable Expenses

	1998–1999	2025–2026	Increase
Public Two-Year	\$8,292	\$16,840	103%
Public Four-Year	\$12,975	\$18,710	44%
Private Nonprofit Four-Year	\$14,569	\$20,140	38%

Note: Calculations are based on data from the College Board's *Trends in College Pricing and Student Aid 2025* and *Trends in College Pricing 1998*. Definitions vary slightly across reports. The inflation adjustment (factor of 1.98) for 1998–2025 was calculated using data from the Federal Reserve Bank of Minneapolis

OTHER KEY POINTS

- The modest revenue generated does not outweigh the negative consequences of adding considerable financial barriers for low- and middle-income students and dissuading institutions from offering more scholarship aid.
- In 2024–2025, 60 percent of families depended on scholarships to help them access college; the vast majority of them (75 percent) said that scholarships enabled the student to attend college.
- This tax treatment undermines innovative and generous institutional aid models by penalizing students who receive such need-based financial aid, making it harder for institutions to expand aid for low- and middle-income students without increasing their tax burden.
- In many cases, students are taxed on scholarship funds they never actually receive. When those funds are used for on-campus room and board, the money often goes straight to the institution, leaving low-income students—who often have little savings—to face tax bills they cannot afford.
- Like other forms of grant aid, Pell Grants are taxable when used for non-tuition expenses, forcing hundreds of thousands of the lowest-income students attending the lowest-cost institutions to pay taxes on the very federal aid meant to help them access higher education.
- Veteran education benefits are exempt from taxation to avoid unnecessary complexity and financial burden for military learners. Providing consistent tax treatment for scholarships and grants would similarly simplify the system and better support low- and middle-income students.

FURTHER READING

[“Wait, What? Scholarships Are Taxable?”](#) Scholarship America, 2024

[“Taxes, Scholarships, and a College Freshman: No Such Thing as Free Money”](#) Tax Policy Center, 2023

[Tax Treatment of Scholarships](#), National Scholarship Providers Association, 2018