

**Division of Accounting
Payroll Compliance Group**

Education Assistance/Tuition Reimbursement Bulletin

INTRODUCTION

The Division of Accounting (DOA) is responsible for working with State of Delaware (State) Organizations to ensure appropriate tax treatment of education assistance offered to State employees.

This bulletin provides guidance on tax implications associated with education assistance and tuition reimbursement to ensure that employers are tracking the benefit appropriately, and that the State complies with federal tax laws and regulations.

FACTS

Unless a specific Internal Revenue Service (IRS) exemption applies, all payments made from State funds or items of value given to employees are considered compensation, and are subject to federal, state, and local (if applicable) income tax and associated other employment costs (OECs)

Please contact your Human Resources (HR) office for your Organizations' policy regarding education assistance.

DEFINITIONS

Accountable Plan: Plan that meets the requirements as specified by the IRS.

- Reimbursed expenses paid in connection with the performance of services for the employer.
- The employee substantiates the reimbursed expense to the employer.
- The employee returns amounts paid by the employer that exceed substantiated expenses.

Nonaccountable Plan: Payment or reimbursement arrangement that does not meet requirements of an accountable plan; payments under such plans are wages and subject to withholding.

Job Related Education: One of the following conditions are met:

- It maintains or improves skills required to do the job.
- It is expressly required by the employer or by law.

Working Condition Fringe Benefit: Services that would have been deductible on the employee's individual income tax return had they not been reimbursed. In the context of educational assistance, to be a working condition fringe benefit, the instruction should improve or develop the job-related capabilities of an employee. The course is a *Working Condition Fringe Benefit* if the following conditions are met:

1. Must not be needed to meet minimum education requirements of the current job;
2. Not taken to qualify employee for a promotion/transfer to different type of work;
and
3. The topic is related to the employee's current job.

Qualified Tuition Reduction: Tax-free reduction in tuition provided by an eligible educational institution.

Qualified Education Expenses: Tuition & fees, books, and supplies for both undergraduate and graduate education.

FINDINGS

To determine if education assistance reimbursements are excludable from wages, employers must consider general fringe benefit rules as well as regulations included in several sections of the Internal Revenue Code (IRC).

REGULATORY REFERENCES

In rendering this opinion, DOA reviewed the applicable Code, Regulations, laws, and publications as cited.

IRC § 132(d) – Education as Working Condition Fringe Benefit
Reg. § 162 and Treas. Reg. § 1.162-5(e) – Expenses for Education
IRC § 127 – Qualified Educational Assistance Program
IRC § 117(d) – Qualified Tuition Reductions
IRS Publication 970 – Tax Benefits for Education
IRS Publication 5137 – Fringe Benefit Guide

Two primary sections of the IRC must be considered when determining the proper taxation of education assistance/reimbursement:

- Education under a Qualified Educational Assistance Program (IRC § 127) – Allows up to \$5,250 to be excluded from an employee’s gross income per calendar year.
- Education that qualifies as a Working Condition Fringe Benefit (IRC § 132(d)) – Not taxable, no limitation of the dollar amount on reimbursements for qualified education expenses.

IRC § 127 – Qualified Educational Assistance Program

Educational Assistance Programs must meet the following requirements:

- Must be a separate written plan.
- Must be for the exclusive benefit of the employees.
- Must not provide benefits for employees’ spouses or other dependents.
- Must not discriminate in favor of highly compensated employees.
- Employees cannot choose between educational assistance and compensation.
- Employers must provide reasonable notification of the availability and terms of program to eligible employees.
- Can require successful completion of a course or a specific grade to be reimbursed.
- May not include payment for the cost of tools or supplies (other than textbooks) your employee is allowed to keep at the end of the course (calculators, etc.).
- Must require employees to substantiate that the assistance qualifies.

Expenses over \$5,250 are taxable to the employee and reported on the W-2 unless the expense could be deducted as a qualified business expense on the employee's personal tax return.

Note: Section 127 does not require courses to be job-related; however, certain exceptions apply for courses related to sports, games, or hobbies, which are only covered if required as part of a degree program.

IRC § 132 (d) – Education as a Working Condition Fringe Benefit

Job-related educational expenses may be excludable from an employee's income.

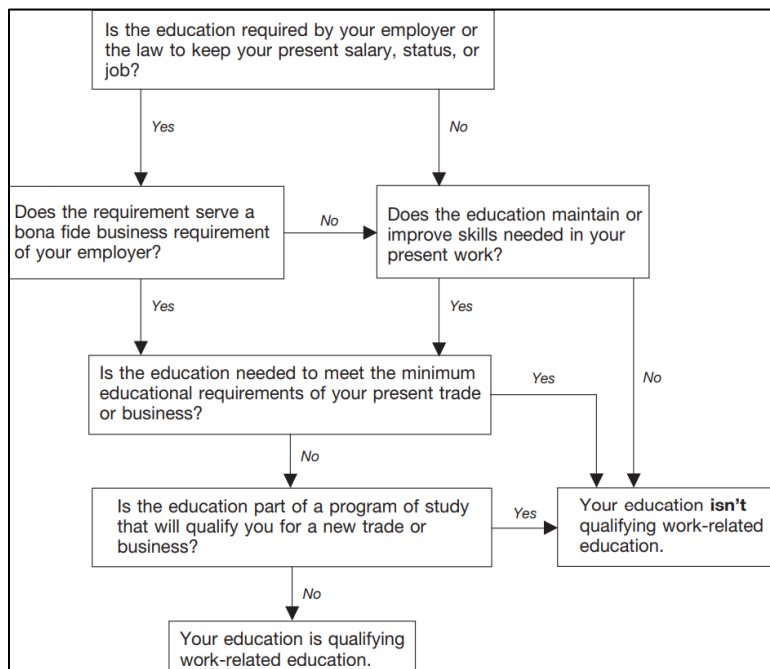
- Must improve or develop the job-related capabilities of an employee, or be expressly required by the employer or by law.
- Cannot be needed to meet the minimum educational requirements of current job.
- Cannot qualify the employee for a new trade or business.

Treas. Reg. § 1.162-5(b)(3) – Courses Qualifying for New Trade or Business

If an employee is taking courses that could qualify them for a new trade or business, it is not a working condition fringe benefit. In essence, the education could be preparing the person for a new line of work. An example is an accountant taking engineering classes; when the education was completed, the individual would be qualified for a new trade.

IRS Publication 970 – Tax Benefits for Education

Publication 970 provides the following chart to determine if a course is job related and a working condition fringe benefit:



In the field of education, certain job transitions are not considered to be to a new trade or business if the new duties involve the same general type of work as is involved in the individual's present employment. Examples include:

- Elementary to secondary school classroom teacher.
- Teacher in one subject to teacher in another subject (i.e., math to science).
- Classroom teacher to guidance counselor.
- Classroom teacher to principal.

IRC § 117(d) – Qualified Tuition Reductions

Free or reduced tuition for employees of educational institutions may be excludable to employees. Whether a tuition reduction is a qualified tuition reduction, and therefore excludable from income, depends on the level of the courses being taken (see below). The qualified tuition reduction must not represent payment for services.

Generally, a qualified tuition reduction cannot discriminate in favor of highly-compensated employees.

Eligibility – Below Graduate Level

- An “educational organization” for this purpose must:
 - Maintain a faculty and curriculum, and
 - Normally have a regularly enrolled student body on site. (IRC § 170(b)(1)(A)(ii))
- For purposes of a qualified tuition reduction, an employee may be a:
 - Current employee or spouse.
 - Former employee who retired or left work on disability.
 - Spouse, widow or widower of deceased employee.
 - Spouse, widow or widower of employee who retired or left on disability.
 - Dependent child of employee.
 - Child of employee, under age 25, with both parents deceased.
- The education need not be at the same institution where the employee works

Eligibility – Graduate Level

Tuition reductions for graduate education are considered “qualified” and are excludable if they are provided by an eligible educational institution to a graduate student performing teaching or research activities for the educational institution.

- The courses must be taken at the school where the employee is working.
- The employee must include in income any other tuition reductions received for graduate education.

NOTE: There is no dollar limitation on qualified tuition reductions for education under IRC § 117(d).

DELAWARE CODE

- 14 Del. C. 11A, § 1101A – 1111A allows for qualified applicants to apply for a payment from the State to the applicant's lending agency, to pay a portion of the applicant's student loan debt.

- The High Needs Educator Student Loan Payment Program will provide loan repayment for qualified educational loans for eligible candidates employed in high needs areas.
- The amount of loan payments paid on behalf of the eligible candidate must be included in gross income for tax purposes (IRS Publication 970).

OTHER

Specific information concerning reporting guidelines is provided annually in the PHRST *Calendar Year-End Processing Memorandum*.

Delaware State Employee Merit Rules

Chapter 5.8.1 Employee Benefits

- Educational reimbursement shall be offered by agencies consistent with their budgetary allowances. Reimbursement will be made only upon submission of evidence of satisfactory completion accompanied by paid receipts. In exceptional circumstances, agencies may pay in advance of course completion. In such case, employees shall reimburse agencies if they do not submit evidence of satisfactory completion. Employees shall reimburse agencies for tuition and paid education leave if they do not submit evidence of satisfactory course completion or if they leave State employment within 6 months of course completion.

TAX ADVICE DISCLAIMER

Although the opinion provided here is presented in good faith and believed to be correct, it is general in nature and is not intended as tax advice. Furthermore, the facts and regulatory references applicable to this scenario may not be applicable to or suitable for other similar scenarios that may require consideration of other factors.

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