

**Division of Accounting  
Payroll Compliance Group**

**Bulletin # 2012-003  
Education Assistance/Tuition Reimbursement**

**INTRODUCTION**

Based on findings from the Statewide Compliance Examination of non-wage fringe benefits, the Division of Accounting Payroll Compliance Group (PCG) is publishing guidance on appropriate tax treatment of Tuition Reimbursements and Educational Assistance Programs.

**FACTS**

Fringe benefits include any compensation other than cash wages. The general rule is that the compensation is taxable; however, the Internal Revenue Code provides exclusions for numerous forms of non-cash compensation provided to employees.

Taxation rules vary according to whether the instruction is *Job-Related* or *Non Job-Related Education*. IRS regulations require that certain non-job related educational assistance and tuition payments are reported as taxable income on Form W2.

As a benefit to State of Delaware employees, Organizations may provide Educational Assistance and/or Tuition Reimbursement, provided the funds are available in the budget.

**REGULATORY REFERENCES**

**IRS**

Qualified education expenses do not include the cost of tools or supplies (other than textbooks) an employee is allowed to keep at the end of the course.

To determine if tuition reimbursements or the value of the education is excludable from wages to the employee, employers must consider general fringe benefit rules as well as the following sections of the Internal Revenue Code:

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

## Taxable Fringe Benefits Guide – Federal, State, and Local Governments

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

**Working condition fringe benefits** include services that, if the employee had paid for the service, the cost would have been deductible on the employee's individual income tax return. 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 all the following conditions are met:
  - Must not be needed to meet minimum education requirements of the current job.
  - Not taken to qualify employee for a promotion/transfer to different type of work.
  - The topic is related to the employee's current job.
- The course is *Job-Related* if either 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.

### Treas. Reg. § 1.132-5(a)(v) – Cash Payments for Educational Assistance

If the employer provides a cash advance to cover the education expenses, the employee must:

- use the advance for education expenses that qualify as a working condition fringe benefit,
- verify that the advance was actually used for such expenses, and
- return any unused portion of the advance.

### Treas. Reg. § 1.162-5(b)(3)(i) – Expenses for Education

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.

- Courses taken to qualify teachers for transition examples below are excludable:
  - Elementary to secondary school classroom teacher.
  - Teacher in one subject (i.e., math) to teacher in another subject (i.e., science).
  - Classroom teacher to guidance counselor.
  - Classroom teacher to principal.

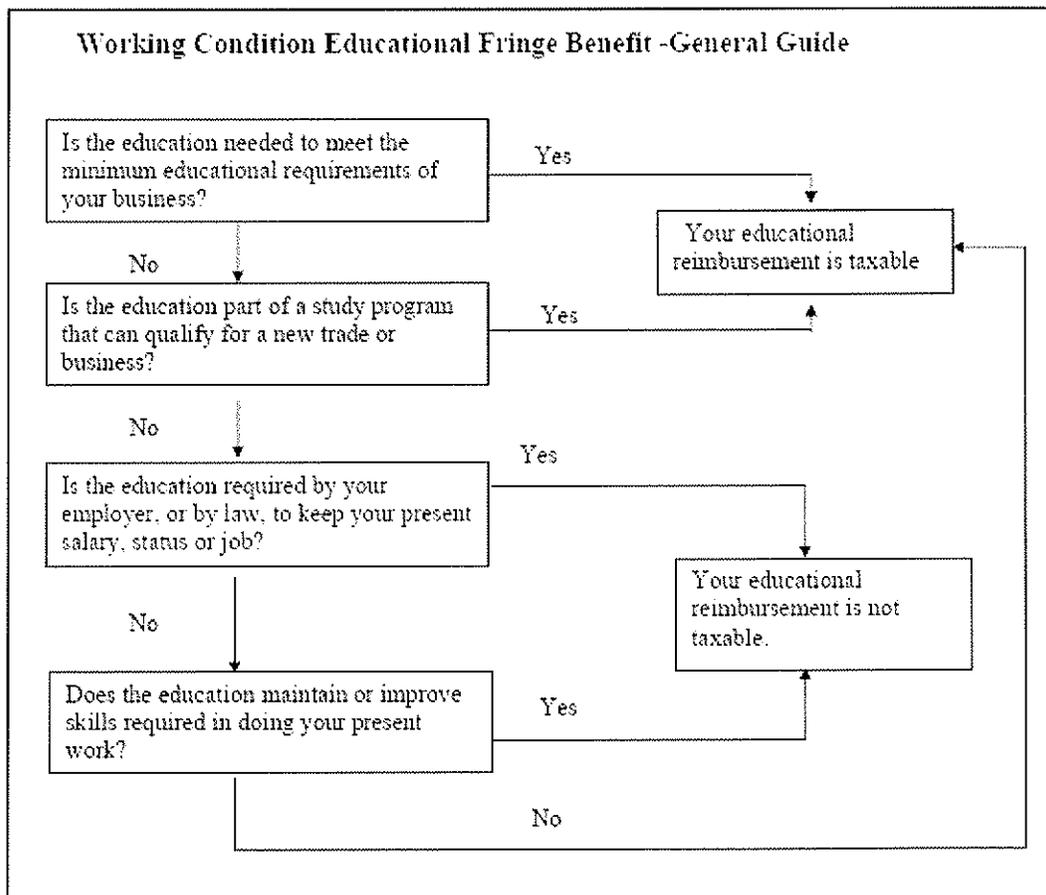
### IRC §127 – Qualified Educational Assistance Program

IRC §127 is tax relief that expires and must be voted on by Congress periodically. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 extended this provision through the end of 2012.

Section 127 provides an exclusion from an employee's gross income of up to \$5,250 per calendar year for amounts paid by an employer through a sponsored educational assistance program. Qualified education expenses include: tuition, fees, books, and supplies for both undergraduate and graduate education. 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.

- Educational Assistance Programs must meet the following requirements:
  - Must be a separate written plan.
  - Must be for the exclusive benefit of the employees.
  - Does not provide benefits for employees' spouses or other dependents.
  - May not discriminate in favor of highly compensated employees.
  - Employees cannot choose between educational assistance or compensation.
  - Employers must provide reasonable notification of the availability and terms of program to eligible employees. Consider including the plan in New Hire Packets, Employee Handbooks or other onsite location (i.e., Organization website).
  - Can require successful completion of a course or a specific grade in determining reimbursement under the program.
  - 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 (i.e., calculators, etc.).
  - Employees must substantiate that the assistance qualifies under IRC §127.
  - Expenses over \$5,250 are taxable to the employee and reported on the W-2 unless the reimbursement was for an expense that could be deducted as a qualified business expense if the employee paid for the educational expenses.

The IRS Taxable Fringe Benefit Guide provides the following chart:



## **IRC §117(d) – Qualified Tuition Reductions**

Free or reduced tuition for employees of educational institutions may be excludable to employees. The term “qualified tuition reduction” means a tax-free reduction in tuition provided by an eligible educational institution. At the undergraduate level, the education need not be at the same institution where the employee works. Whether a tuition reduction is a qualified tuition reduction, and therefore excludable from income, depends on whether it is for education below or at the graduate level. The qualified tuition reduction must not represent payment for services.

Generally, a qualified tuition reduction cannot discriminate in favor of highly-compensated employees (for 2012, employees with total compensation exceeding \$115,000).

### **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 at 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.

### **Tuition Waiver for State Employees**

Some state laws permit state colleges and universities to waive all or a portion of tuition, services and activities fees for state employees. For example, the benefit is made available to those employed half-time or more in the following classifications for permanent employees:

- Classified and exempt paraprofessional employees of technical colleges,
- Faculty, counselors, librarians, and exempt professional and administrative employees at institutions of higher education.

If the waiver or reduction does not meet the requirements for a qualified tuition reduction, it may still qualify for an exclusion as an educational assistance plan or as a working condition fringe benefit, discussed earlier.

**NOTE:** Currently, the State of Delaware does not offer tuition waivers to state employees.

**Comparison of Code Sections Covering Educational Assistance**

The following table is for quick reference. For more information, see the text, the relevant Internal Revenue Code sections, or Publication 570.

Feature	§127 Qualified Educational Assistance	§132(d) Working Condition Fringe	§117(d) Qualified Tuition Reduction
Written Plan Required	Yes	No	No
Undergraduate Courses Covered	Yes	Yes	Yes
Graduate Courses Covered	Yes	Yes	No*
Must Be Job Related	No	Yes	No
Courses Qualifying Employee for New Trade or Business Covered	Yes	No	Yes
Courses Needed to Meet Minimum Job Requirements Covered	Yes	No	Yes
Can Discriminate in Favor of Highly Compensated Employees	No	Yes	No
Dollar Limitation	Yes-\$5,250	No	No
Expiration date	None	None	None
<b>Definition of Employee Includes:</b>			
Current Employees	Yes	Yes	Yes
Family Members	No	No	Yes
Laid-Off Employees	Yes	No	No
Employees Retired or on Disability	Yes	No	Yes
Independent Contractors	No	Yes	No
<b>Educational Expenses Covered:</b>			
Tuition, Books, Supplies, Equipment	Yes	Yes	Tuition Only
Tools or Supplies, for class use only	No	No	No
Education Involving Sports, Games, Hobbies	No**	No**	Yes
Meals, Lodging or Transportation	No	Yes	No

\* See text for exceptions

\*\* Yes, if specifically job related

**Note:** These are general rules. For details, refer to the text and 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 5.0 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.

Additionally, personnel of the Department of Finance do not advise on personal income tax requirements or issues. Use of any information provided by PCG is for general information only and does not represent personal tax advice either express or implied. State employees are encouraged to seek professional tax advice for personal income tax questions and assistance.



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