

# Radford University

## Tuition Waiver

**REVISED:** October 31, 2002

**Purpose:** To explain the taxability or non-taxability of tuition waivers for employees based on the Internal Revenue Code.

**Procedures:** For semesters beginning after December 31, 2001, tax laws will be reviewed to ensure the continued exclusion from taxes for undergraduate and graduate courses.

For semesters prior to January 1, 2002 the following procedures apply. Each semester the Tax Compliance Office determines the taxability of tuition waivers submitted and approved by the Department of Human Resources. Each tuition waiver determined to be taxable is then submitted to the Payroll Office for inclusion in the employee's reportable income. Taxable waivers are subject to state and federal withholding and social security and Medicare taxes. Appropriate taxes are withheld from the employee's wages based on the taxable income. The income and withheld taxes will be reported on the employee's W-2 statement. Each employee with a taxable waiver is notified by mail with the amount of the reportable income and the dates of payroll inclusion. The reportable income is spread out over three payroll periods.

### Evaluation of Internal Revenue Code Regulations

The purpose of this section is to briefly summarize the requirements for employer sponsored education to be considered tax-free to the benefiting employee. In general, there are three Internal Revenue Code sections that are applicable.

**Working condition fringe benefit (IRS Code Section 132):** For purposes of this section, the term "working condition fringe" means any property or services provided to an employee by the employer to the extent that, if the employee paid for such property or services, such payment would be allowable as a deduction under IRS Code Section 162 (the following rules relate to IRS Regulation 1.162.5, Expenses for Education).

Education, training, etc. **must be job related.** The nature, type, length, cost, level (graduate or undergraduate) of the course, class, or training is not relevant. Tax-free job-related education is that which:

1. maintains or improves skills required by the employee in his employment, includes refresher courses or courses dealing with current developments or
2. is expressly required by the employer or is legally required in order to retain an established employment relationship, status or rate of compensation, only if such requirements are imposed for a bona fide business purpose by the employer.

**In no event, however, is education paid for or provided by the employer, tax-free to the employee, if the purpose for the education qualifies as one of the following.**

Courses, classes or training that do not qualify as tax-free job-related education is education which meets:

1. minimum education requirements necessary to qualify for employment, requirements normally established at the time the individual is first employed or
2. education that will qualify an employee for a new trade or business. Education which leads to a degree in an area unrelated to present employment, could lead to a new trade or business and is taxable to the employee. However, university policy, based on a review of court opinions, includes as

taxable any education which leads to a graduate degree whether or not it is related to present employment.

Travel away from home primarily to obtain education is a deductible expense and therefore, a tax-free fringe benefit to the employee. Travel, meals and lodging, directly related to the education, are tax-free items to the employee.

### **Education assistance (IRS Code Section 127).**

In general, gross income of an employee does not include amounts paid or expenses incurred by the employer for educational assistance to the employee if:

1. the assistance is furnished pursuant to a written educational assistance program established for the benefit of employees who qualify under a classification set up by the employer (see the [Department of Human Resources](#) web site);
2. the program is not discriminatory in favor of highly compensated employees, and
3. reasonable notification of the availability and terms of the program is provided to eligible employees.

Congress retroactively re-enacted this section (with changes) for the eighth time with passage of the Taxpayer Relief Act of 1997. Legislation passed in November of 1999, extended this tax protection through Dec. 31, 2001 for undergraduate courses only. It did not include graduate courses. The Economic Growth and Tax Relief Reconciliation Act of 2002 extended the provisions for Code Section 127 through 2010 with the inclusion of graduate classes. The current regulations include:

1. all course/class work beginning before December 31, 2010;
2. undergraduate and graduate course work. (The graduate provision was not include from July 1, 1996 to December 31, 2001.);
3. a maximum cap of \$5,250 for non-taxable educational assistance per calendar year and
4. payment of or provision for (waiver) tuition, fees, books, supplies, and equipment (does not include tools and supplies retained by the employee after completion of course). The Commonwealth Accounting Policies and Procedures Manual (CAPP) does not allow payment of employee personal expenses which includes books for classes (unless they remain the property of the State).

The current regulations **disallow** the following:

1. any payment for a course or education involving sports, games or hobbies (unless the course is required as part of a degree program) and
2. any payment for meals, lodging, or transportation.

**NOTE: In June 2002 an IRS Chief Counsel Field Service Advice was issued and concluded that waivers of job-related graduate tuition cannot qualify as a section 132 working condition fringe benefit. The rationale is based on IRC §132(1), which says that where a fringe benefit does not qualify under a specific code section (e.g., the §117(d) (except for those provided to graduate teaching and research assistants), the taxpayer cannot look to IRC §132 to exclude the benefit.**

**Qualified tuition reduction (IRS Code Section 117(d)).** This is a special provision that only applies to the educational assistance offered by educational institutions to their employees (including retired or disabled former employees, spouses and dependent children). Regulations include the following:

1. qualified tuition reductions (waivers) are tax-free. Qualified expenses are required tuition, fees, books, and equipment. The CAPP Manual does not allow payment of employee personal expenses which includes books for classes (unless they remain the property of the State);

2. only undergraduate courses/classes are tax-free with the following exception. Graduate level courses taken by **teaching or research assistants** are entitled to the income exclusion (tax -free status). Note, however, that payments for services, even if required of all students receiving assistance, are taxable wages. A classification of Graduate Teaching Fellow, Graduate Teaching Assistant, or Graduate Research Assistant by the Graduate College qualifies graduate employees for the tax-free benefit of this code section;
3. there is no requirement that the education be job related, nor is there a maximum dollar limitation;
4. the program must not favor the highly compensated;
5. there are no restrictions on the type of courses/classes taken except that they may not be graduate classes (exception as noted above) and
6. there is no requirement that the employee be a candidate for a degree (only recipients of scholarships and fellowships are required to be candidates for a degree).

### State and university policies.

The Commonwealth Accounting Policies and Procedures Manual prescribes that "agency purchases must be considered essential to the operation of the agency to justify use of State funds." The list of examples of improper uses of State funds includes employee personal expenses such as books for classes unless they remain the property of the State.

For instructions and university rules governing the Employee Tuition Waiver Program, please see the Department of Human Resources web site.

### Summary of Taxability of Employee Educational Aid

The table below summarizes the provisions of three Internal Revenue Code (IRC) sections that address employer supported financial assistance of continuing educational programs for employees. This table encapsulates the content of the information previously provided in this section. Employer funded education is nontaxable to the benefiting employee if the requirements of any one of the three IRC sections is satisfied.

	<b>Code Section 132</b>	<b>Code Section 127</b>	<b>Code Section 117</b>
<b>Job related Undergraduate level Non-degree seeking</b>	N/A	Nontaxable	Nontaxable
<b>Job related Undergraduate level Degree seeking</b>	N/A	Nontaxable	Nontaxable
<b>Job related Graduate level Non-degree seeking</b>	Taxable beginning June 2002(see <b>NOTE</b> )	Nontaxable 01/01/02 to 12/31/10	Taxable except for GTFs, GTAs & GRAs
<b>Job related Graduate level Degree seeking</b>	Taxable	Nontaxable 01/01/02 to 12/31/10	Taxable except for GTFs, GTAs & GRAs

<b>Not job related Undergraduate level Degree seeking or not</b>	Taxable	Nontaxable	Nontaxable
<b>Not job related Graduate level Degree seeking or not</b>	Taxable	Nontaxable	Taxable except for GTFs, GTAs & GRAs

**NOTE:** Section 132: Education or training is job related if it (1) maintains or improves skills that an employee is required to have for employment or (2) is expressly required by the employer or is legally required to retain an established employment relationship, status or rate of compensation. The foregoing notwithstanding, education is NOT job related if it (1) provides the minimum education requirements necessary to qualify for employment or (2) is education that will qualify an employee for a new trade or business. University policy is that anyone who is a degree seeking individual will more than likely be qualified for a new trade or business upon completion of the program, therefore, tuition reductions under this code section for degree seeking employees will always be taxable to the employee.

**Section 127:** There is a cap on nontaxable courses of \$5,250 per year. Restrictions apply to the type of classes employees may take. The relevant provisions of this section were reinstated through December 31, 2010.

**Section 117:** With respect to GTFs, GTAs, and GRAs, a tuition reduction award is TAXABLE to the extent it represents a payment for services required as a condition of receiving the award.

## **Hope and Lifetime Learning Tax Credits**

Employees who have taxable tuition waivers are eligible for the Hope or Lifetime Learning credits as established by the Internal Revenue Service with the Taxpayer Relief Act of 1997. For more information, see the web page for Student Tax Information.