

Employee Educational Fringe Benefits Under the 2017 Tax Act

TAX SECTION



By John G. Hodnette

One of the most appealing benefits of working for a university is an educational assistance program. Free or discounted college education is extremely valuable given tuition continues to increase at an average of 8% per year. Whether these benefits are taxed as compensation or excluded from income is vitally important to university employees.

Three code sections are especially important when an employer provides an employee or employee's family with free or discounted college education. The first is Section 117, which excludes from gross income qualified scholarships granted to an individual who is a candidate for a college degree. Section 117(d)(1) additionally provides where an educational institution at the university level grants qualified tuition reduction to an employee for an undergraduate degree, that tuition reduction is not included in gross income.

Second, Section 127 addresses educational assistance programs. It provides that gross income of an employee does not include amounts paid or expenses incurred by an employer for educational assistance, whether at the undergraduate or graduate level. The exclusion, however, is limited to \$5,250 per year. Although Section 127 provides an excellent streamlined way for employers to exclude educational assistance, for employees of expensive universities, \$5,250 may only scratch the surface.

Third, Section 132(a)(3) provides an exclusion from gross income for working condition fringes. Section 132(j)(8) provides "amounts paid or expenses incurred by the employer for education or training provided to the employee which are not excludable from gross income under section 127 shall be excluded from gross income under [section 132] if (and only if) such amounts or expenses are a working condition fringe." Thus, educational expenses in excess of the Section 127 limitation may be excluded from gross income under Section 132, provided they are a working condition fringe. A working condition fringe is defined in Section 132(d) as "any property or service provided to an employee of the employer to the extent that, if the employee paid for such property or services, such payment would be allowable as a deduction under section 162 or 167." The Section 162 regulations clarify the excludable expenses must be "job-related and either maintain or improve job skills." Treas. Reg. § 162-5(a)(1). However, the education must not be "needed to meet the minimum educational requirements of the current job" or "qualify the employee for a new trade or business." Treas. Reg. § 162-5(b)(2)-(3).

Whether an employee qualifies for the working condition fringe exclusion for educational assistance provided by the employer depends on the facts and circumstances of that employee. If the employee qualifies, the tax savings make employer provided educational benefits even more valuable.

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