

## MEMORANDUM

To: All Employees

From: James D. Barbret, Controller and AVP of Fiscal Operations

Subject: Taxability of Tuition Assistance Benefit Program

Date: January 4, 2013

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Wayne State University offers eligible employees the opportunity to pursue higher education free of charge for both undergraduate and graduate coursework. In addition, an eligible employee's spouse and/or dependent children may qualify for a tuition discount for undergraduate and graduate courses. Undergraduate tuition benefits are not deemed by the Internal Revenue Service (IRS) to be a taxable benefit; however, graduate tuition benefits are considered taxable income. In order to be compliant with IRS regulations, we will begin additional tax withholding associated with the taxable benefit during the term for which the benefit is received.

**In order to receive these benefits, an application form must be submitted to the Office of Total Compensation and Wellness (TCW) no later than 10 business days after the Last Day for Tuition Cancellation of the same term (Census Day). We will not accept applications for the tuition assistance benefit after the listed due dates.**

### **Why are Tuition Benefits Taxed?**

In general, IRS regulations consider anything of value provided to an employee by an employer to be a form of compensation. All compensation must be reported as taxable wages and is subject to income tax withholding, unless specifically excluded by the Internal Revenue Code (IRC).

Under IRC §117(d), educational institutions offering tuition reductions to employees, their dependent spouses and/or children for undergraduate coursework may exclude the value of this education from their employees' taxable wages. **The exclusion under this section does not extend to graduate courses.** IRC §127 allows employers to provide their employees with educational assistance for both undergraduate and graduate work. Employers may provide each eligible employee with up to \$5,250 of educational assistance per year on a tax-free basis. The tuition assistance that the University offers eligible employees for graduate level courses is eligible for this exclusion. IRC §127 requires any assistance in excess of \$5,250 be included in the employees' taxable wages and employment and income taxes must be withheld. **This exclusion does not apply to any spouse and/or dependent children.**

## **What does that Mean for a WSU Employee?**

As an employee taking graduate level coursework, you are allowed up to \$5,250 of tuition assistance per calendar year without any tax implications in accordance with the educational assistance exclusion under §127. Any amount over \$5,250 in a calendar year will be subject to taxation. If a spouse and/or dependent child are taking graduate level courses, you will be subject to tax on the entire value of the University tuition assistance received. As noted above, the additional tax associated with the taxable benefit will be withheld during the term the benefit is received.

## **How is the Taxable Amount of the Benefit Determined?**

Over the course of the calendar year, the benefits will be accumulated to determine if and when the employee has reached the \$5,250 limitation and the point at which the benefit becomes taxable.

Payroll will receive a summary of graduate tuition benefit for employees and their spouse/dependent children at the beginning of each term. The amount of taxable income will be calculated and will be spread out over a number of pay periods in the term, as the taxation must occur when the benefits are received per IRS regulations. Employees will be notified no later than 20 business days after the **Last Day for Tuition Cancellation** of each term as to the amount of additional tax withholding.

Graduate education assistance is considered supplemental income and is therefore subject to the highest federal withholding rate. The IRS defines a flat supplemental tax withholding rate which is gauged to the middle tax rate of the IRS graduated tables.

We cannot change the rate of withholding on this additional income. If you feel that your total federal income tax withholding for the year will exceed your tax liability, you may submit a new W-4 Form to the Payroll office changing the number of exemptions you claim. Please see IRS Publication 919, available on the IRS website, for instructions on how to estimate your income tax liability and update your W-4 accordingly. Please consult with your tax advisor to ensure that you have the appropriate withholding.

### **Example 1:**

An employee receives \$10,250 in graduate tuition assistance for the term. The one time annual employee assistance reduction of \$5,250 is applied resulting in a taxable value of \$5,000. This \$5,000 will be recognized as income and reported on the employee's Form W2 with all applicable taxes being withheld during the term it was received. Social Security, Medicare and Federal, State and City withholding taxes are required to be withheld. The calculations are:

Federal	\$5,000 x 25%	=	\$1,250.00
Social Security	\$5,000 x 6.2%	=	\$ 310.00
Medicare	\$5,000 x 1.45%	=	\$ 72.50
Michigan	\$5,000 x 4.35%	=	\$ 217.50
Detroit Resident	\$5,000 x 2.5%	=	\$ 125.00
Detroit NonResident	\$5,000 x 1.25%	=	\$ 62.50

Total taxes to be withheld on the \$5,000 are \$1,975.00 (city residents) and \$1,912.50 (city nonresidents). This amount divided over the number of pays in the term (typically 7 pays) equals an additional tax withholding per pay of \$282.14 (or \$273.21 for nonresidents of Detroit).

### **Example 2:**

Assume the same facts from Example 1, except that it is the employee's spouse or dependent child receiving graduate tuition assistance. Neither a spouse nor dependent child qualifies for tax-free treatment; therefore the entire \$10,250 tuition assistance received is recognized as income and

reported on the employee's Form W2 with all applicable taxes being withheld during the term it was received. Social Security, Medicare and Federal, State and City withholding taxes are required to be withheld. The calculations are:

Federal	$\$10,250 \times 25\% =$	\$2,562.50
Social Security	$\$10,250 \times 6.2\% =$	\$ 635.50
Medicare	$\$10,250 \times 1.45\% =$	\$ 148.63
Michigan	$\$10,250 \times 4.35\% =$	\$ 445.88
Detroit Resident	$\$10,250 \times 2.5\% =$	\$ 256.25
Detroit NonResident	$\$10,250 \times 1.25\% =$	\$ 128.25

Total taxes to be withheld on the \$10,250 are \$4,048.76 (city residents) and \$3,920.76 (city nonresidents). This amount divided over the number of pays in the term (typically 7 pays) equals an additional tax withholding per pay of \$578.39 (or \$560.11 for nonresidents of Detroit).

### **How Many Times Will Deductions Occur Within the Term?**

Typically the deductions are spread over 5-7 pays within the term. **Please be aware that the number of pays can vary depending on when information is available and is able to be processed. It will also depend on when your application form is processed by Total Compensation and Wellness.**

Please note that Wayne State University does not give tax advice, does not guarantee, and is not responsible for any final tax results. As such, we strongly encourage you to speak with a qualified tax advisor to answer questions specific to you and the tax implications resulting from receiving tuition assistance benefits.

For questions concerning the taxation of your tuition assistance or any of the items mentioned above, please contact:

Julie Denomme  
Director – Tax  
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Associate Director – Payroll  
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For any questions regarding the administration of the tuition assistance or completion of the forms, please continue to contact the Office of TCW.

Brett Green  
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