

Tax Deductions, Credits, and Tuition/Fee Deductions

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Overview

- Education tax benefits can be a confusing and frustrating process and some students leave money on the table.
- The information in this presentation has been vetted by a CPA, however, to navigate your personal financial situation, please use either Turbo Tax or contact an accountant.
- The University is not able to offer tax advice due to liability issues, however, we hope this information will be helpful as an educational tool.

What this presentation will cover

- Tax Credits vs. Tax Deductions
- Three ways a taxpayer can deduct educational costs
- Tax Credits
- Tuition and fees deduction from income
- Student loan interest expense deduction
- Claiming MBA costs as unreimbursed business expenses
- Fairly recent Court Cases/Citations
- Miscellaneous

Tax Credit vs. Deduction

- A tax **credit** will reduce income tax liability dollar for dollar
- A tax **deduction** will lower taxable income

3 ways a taxpayer can deduct education costs

- A. Tax credits (American Opportunity Tax Credit a.k.a. Hope Credit or Lifetime Learning)
 - Qualified tuition costs can be used to compute tuition tax credits. A tax credit is a direct reduction of tax liability.
- B. Tuition and fees deduction (Flat \$4K deduction)
 - Qualified costs are deductible from gross income subject to limitations.
- C. Itemized deduction of tuition and related costs (unreimbursed business expense)
 - Qualified MBA tuition costs *may* be deductible from your personal income taxes as unreimbursed costs on form 1040 Schedule A Line 23. A tax deduction reduces taxable income.

A. Tax Credits

- American Opportunity Tax Credit
 - Max credit is \$2,500 per student for the first student and 25% of the next \$2,000 for each additional student
 - Usually for undergraduates
- Lifetime Learning Credit
 - For graduate school and professional degrees
 - Up to 20% of the first \$10,000 in qualified costs or \$2,000
 - Only allowable for taxpayers with income less than \$64K and double for those married (if married, must file jointly to claim the credit)

A. Tax Credits, con't

- Columbia University will issue a 1098-T form in February for all students showing qualified tuition and related costs. Credits are computed on Form 8863
- To retrieve your 1098-T, go to www.1098T.com.
 - You will need to log in with your SS# or Columbia ID C# and Date of Birth
- Student loans are deemed as tuition payments to an institution by a taxpayer in the year of borrowing due to the fact that they are almost impossible to discharge in bankruptcy or otherwise
 - Case – Lockhart vs. US affirmed unanimously by Supreme Court (12/05) that Social Security benefits can be garnished (67 year old and disabled – 15%) to repay student loans.

B. Tuition & Fees – Income Deduction

- Maximum allowable deduction is \$4,000 for taxpayers with AGI (adjusted gross income) less than \$65K
- Allowable deduction reduced to \$2,000 when AGI exceeds \$65K but less than \$80K
- Incomes are doubled for married filing jointly
- It's considered an "Above the Line" deduction to arrive at the AGI
- No tuition & fees deduction is permitted if the Lifetime Learning or Hope credit is taken (must pick one or the other)
- Reported on Line 34 of Form 1040 Page 1 with supporting form 8917

Student Loan Interest – Income Deduction

- In order to take this deduction, interest must be have been paid and NOT accrued
- Maximum allowable deduction from income is \$2,500 per year
- Allowable deduction is reduced when income exceeds \$65K and is eliminated at \$80K
 - Amounts are doubled for married taxpayers
- Reported on Line 33 of Form 1040 Page 1

C. Claiming MBA costs as unreimbursed business expenses

*This is the most intriguing of the three given the cost of business school, however, there are very explicit rules that govern whether one can utilize this method. **The IRS may challenge MBA program deductions due to generality of course load and the large size of the deduction – more and more people are being audited. Cases are being sent to tax court and students are using any savings toward legal fees!** The list of requirements to be considered for the Unreimbursed Business Expense (from income tax regulations (Reg. Sec. 1.162-5)) are:*

- The MBA must be the expressed requirement of employer or law/regulations
- The MBA must improve your skills
- You must be in the field already. A change of duties is not a new trade or business if the new duties and the taxpayer's employment involve the same general work.
- Non-deductible costs are those that qualify an individual for a new trade or business or that meet the minimum education requirements for qualification in your employment or other trade/business
- Self-employed individuals – unless you have been actively engaged as a self-employed individual, you should not attempt to deduct education costs on Schedule C (profit/loss from business).

Claiming MBA costs as unreimbursed business expenses (con't)

- We know many of you have questions regarding whether or not you can claim tuition expenses as a unreimbursed business expense.
- Deducting your tuition expenses as an MBA is risky. You may have solid business reasoning behind claiming the deduction. However, if the IRS audits you may have to pay back taxes, plus interest and penalties.
- You may have read [the article in the Journal](#) where a University of Phoenix graduate won in her case against the IRS. Please keep in mind this woman went to school part-time (on the internet) and stayed working in the same field throughout the process.
- It is generally understood that those people who receive an MBA have an eye on a new trade, or job, and that disqualifies you for the deduction.

Claiming MBA costs as unreimbursed business expenses (con't)

- The Court enforces a *commonsense approach*. Under this standard, if the education qualifies the individual to perform significantly different tasks and activities than previously, the education qualifies the individual for a new trade or business.
- It does not matter if you enter into a position after your MBA in which you are performing tasks different than your prior job, but rather, are you **qualified** to perform different tasks. An MBA may have no intention or desire to move into another position with significantly different tasks and activities, the point is that the Court believes that the MBA label *qualifies* him/her to do significantly new things and to move on to a significantly new job.
- In IRS audits, they will literally go through your class schedule, dissect what skills you have acquired and how they are relevant to your current position. For example, you may not need that Marketing course, and you may not ever use a Break-even analysis or a Lifetime Value analysis, but the fact is that you are now qualified for a Marketing position, and therefore, you may not deduct the expenses *so please research this thoroughly before taking the deduction*.

Court Cases/Citations

- Galligan – Law Librarian
- Lewis – Telecommunications Exec
 - Per Lewis, he was called upon to negotiate increasingly complex contracts for a variety of clients. The tax court ruled that this was not specific enough. Lewis became eligible for a new trade/business
- Zheng – Overall improvement in skill level. No deduction
- Weyts – Columbia JD/MBA student
 - Summer Associate in employee directory
 - Unable to prove same pay scale as full-time
 - Not assigned the same work
 - Earned three credits
 - Court denied deduction by stating that the petitioner had “an uninterrupted continuity in his legal education”.
- Singleton-Clarke vs. U.S. – the recent case. Tax court summary opinion 2009-182
 - Deduction granted.
- It is necessary to break the education cycle and engage in a trade/business before deducting educational expenses. The fact that the break is only for a short period of time will not necessarily deny the deduction. An actual break must occur!

Miscellaneous Items

- New York State and New York City do not offer any tax benefits for graduate education
- Education Assistance Programs from Employers
 - Up to \$5,250 received by an employee for qualified educational expenses may be excluded from gross income under an EAP
 - See IRS publication 15-B
- Forgiveness of Debt
 - Pursuant to certain student loan agreements, if timely payments are made, a percentage of loan debt may be forgiven. Forgiveness of debt is taxable in the year the debt is forgiven unless taxpayer is in bankruptcy. You will get a 1099 from the lender/loan servicer and need to declare the amount as taxable income.
- Job Search Costs
 - Job search costs incurred in seeking employment in your trade or business are allowable as a unreimbursed business expense.
 - Not contingent upon job offer or acceptance
 - Subject to a 2% AGI discount

Questions?

- 1) Visit www.irs.gov and review Tax Benefits of Education and Publication 15-b
- 2) Contact a competent tax advisor

Thank you