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Above-the-Line Education Tax Deduction Reinstated

Article Highlights:

- Appropriations Act of 2020
- History of the Deduction
- Other Education Expense Benefits
- Which Tax Break Provides the Best Benefit

On December 20, 2019, President Trump signed into law the Appropriations Act of 2020, which included a number of tax law changes, among them retroactive extension of certain tax provisions that expired after 2017 or were about to expire, several retirement and IRA plan modifications, and other changes that will, as a whole, impact a large portion of U.S. taxpayers. This article is one of a series of articles dealing with those changes and how they may affect you.

Looking back a few years, a taxpayer who had higher education expenses could generally take advantage of four* possible tax benefits: an itemized deduction if the education was job-related, a higher education tuition and expenses tax credit using either the American Opportunity Tax Credit (AOTC) or the Lifetime Learning Tax Credit (LLC), or an above-the-line deduction for higher education tuition and fees. However, the 2017 tax reforms did away with the itemized deduction through 2025, and Congress allowed the above-the-line deduction for higher education tuition and fees to expire at the end of 2017, leaving only the two education credits as options.

As part of the Appropriations Act of 2020, Congress has retroactively reinstated the above-the-line deduction for 2018 through 2020.

For purposes of the higher education expense deduction, "qualified tuition and related expenses" generally has the same definition, with certain exceptions, as the AOTC and LLC use for higher education expenses, including tuition and fees paid for an eligible student attending school at an eligible higher education institution. The deduction can be claimed for the taxpayer, the taxpayer’s spouse or a dependent of the taxpayer for attending an eligible higher education institution. The deduction, up to $2,000 or $4,000 depending on adjusted gross income (AGI), is not allowed for joint filers with an AGI of $160,000 or more ($80,000 for other filing statuses, although no credit is allowed for taxpayers using the married filing separate status). These phase-out amounts are not inflation-adjusted.

Thus, taxpayers now have three* optional tax benefits for post-secondary education expenses, and the rules related to each are different. Although one of the education tax credits will generally provide the greatest benefit, deciding which option is best can sometimes be complex. Each has a different AGI phase-out limitation, and the AOTC, besides only applying to the first 4 years of post-secondary education, has an additional half-time student requirement. The above-the-line deduction, on the other hand, reduces AGI, and because AGI often limits other benefits on a tax return, the effect of a lowered AGI on other elements of the return needs to be considered.

If you have questions related to the extended above-the-line education deduction, please give this office a call.

*There is actually an additional possibility for self-employed individuals who have business-related education expenses. These costs may be claimed as a business expense in lieu of an education credit or the personal above-the-line deduction.

If you missed any of the earlier tax law change articles you can view those articles at the links below:

- Congress Allowing Higher Medical Deductions for 2019 and 2020
- Employer’s Pension Startup Credit Substantially Increased