Financially Speaking

School Refunds May have a Tax Impact

To say that life has changed over the last couple of months would certainly be an understatement.

I am writing this today from my home office as my staff and I have been working primarily remotely since the Safer at Home restrictions took effect. Like many of you, I went through the sudden change to working out of my house with trepidation about all sorts of things, like how our technology would function and how we would be able to continue effectively communicating with our clients. Fortunately, I found that our technology was up to the task and our clients have been very receptive to emails and phone calls in place of face to face meetings. I even have a Zoom Pro account now – welcome to the age of virtual meetings!

While the temporary transition of my work environment has been fairly problem free, the same can not be said about my home dynamic.

Like so many out there, I have school age children that are struggling to adjust. My 15-year-old went from daily workouts with his fellow football players and a robust social calendar to socializing via Xbox and arguing with me about why noon isn't too late to get out of bed. My just turned 13-year-old is missing his AAU basketball season terribly and is expending the massive amounts of pent up energy that he has in all sorts of mischievous ways. And while they are both fairly good students, on-line school certainly isn't the same as being physically in class for the bulk of the day and getting them to prioritize doing their work isn't always easy.

Parents with children of all ages have faced their own set of challenges, from young children that need a lot of hands on assistance with their work to college age students that needed to pack up and move home, sometimes long distance, with very little notice. One bright spot is that because of the closure of colleges and universities, and the fact that students are no longer living on campus, many schools have refunded a portion of students' costs for the semester.

But it is 2020 after all so of course there is a catch.

If you receive a refund of school costs that were originally withdrawn from a tax-advantaged college savings plan, the most common being a 529 plan but also including Coverdell Education Savings Accounts, then the withdrawal that was originally taken to pay the expense will no longer be considered qualified for tax purposes. That means that the money you got back could end up costing you money in taxes.

Some common qualified education expenses that money can be withdrawn for include, but are not limited to, tuition, room and board, books and supplies. Since the money was returned to you via a refund it was no longer used for a qualified expense and is now considered a non-qualified withdrawal.

A non-qualified withdrawal can mean that you could owe taxes on the earnings portion of that withdrawal plus a 10% federal penalty. If you took a Wisconsin state tax deduction when you originally contributed the money to the 529 plan (the Wisconsin 529 is called EdVest or

Tomorrow's Scholar) that portion of the state deduction amount could also have to be repaid due to the now non-qualified withdrawal.

Fortunately, there are ways to avoid having the refund treated as a non-qualified withdrawal.

You can put the money back into the same type of plan, for the same beneficiary (that is the key), as a recontribution. Under the Protecting Americans from Tax Hikes Act of 2015 a rule was established that allowed 60 days from the receipt of any refund for the money to be recontributed. Due to the COVID-19 Coronavirus situation the IRS has recently issued guidance potentially extending the window to recontribute to the later of July 15th or 60 days after receipt of the refund. If you do elect to recontribute the money make sure that you work with the company to complete any paperwork that they require so that it is coded correctly as a recontribution in their system.

Another option that you may have would be to use the refunded money for different qualified education expenses, as long as the expenses are for the same beneficiary and in the same calendar year. For example, if you got a partial refund for the spring semester but that same student will be going to school again in the fall you could apply the spring refund toward the fall bill. Some schools may even allow you to keep the credit on file with them, rather than getting a check now and having to send it back later. Or, if there are other items that the student needs for school, like a specific calculator or new computer, you may be able to use the refund toward those purchases.

It is always best to consult with your tax advisor when considering issues such as these and to understand how you will personally be impacted. They can best advise you about not just the general rules but also your specific dollars.

We are all being inundated with news right now and it is often hard to determine which items are most important to us personally. If you have a student in school that received a refund of any type this is one of those items that you should pay attention to as it is something that can easily be addressed and that may cost if you if you don't.

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