

## **A Look at Education-Related Tax Incentives**

*Presented by CJ Ferrari and Mark Miller*

For families who are saving and paying for education, federal tax breaks are a great way to ease the financial burden. Here's an overview of some of the options:

### **Qualified tuition programs (529 plans)**

Sponsored by states or educational institutions, qualified tuition programs allow you to prepay, or contribute to an account for paying, a student's higher education expenses. The earnings grow tax-deferred, and distributions are tax-free when used for qualified postsecondary education costs.

### **Coverdell education savings accounts (ESAs)**

Similar to a 529 plan, a Coverdell ESA allows earnings to grow tax-deferred, and distributions are tax-free when used for qualified education costs. The American Taxpayer Relief Act of 2012 permanently extended the \$2,000 annual contribution limit. In addition to qualified postsecondary education costs, distributions from a Coverdell ESA can be used to pay for certain elementary and secondary school expenses, including computer equipment and Internet access used by the student and the student's family.

### **U.S. savings bonds**

EE and I bonds purchased after 1989 by someone at least 24 years old may be redeemed tax-free when the bondholder pays for qualified education expenses for himself or herself, his or her spouse, or a dependent. Qualified expenses are tuition and fees to attend a postsecondary school or contributions to a 529 plan or Coverdell ESA. For 2015, the tax exclusion is phased out for incomes between \$77,200 and \$92,200 (between \$115,750 and \$145,750 for married taxpayers filing jointly). These income limits increase each year.

### **Individual retirement accounts (IRAs)**

Early withdrawal penalties are waived when you use a Roth or traditional IRA to pay qualified higher education costs for yourself, your spouse, your children, or your grandchildren. (Taxes may still be due on the withdrawals, however.)

### **American Opportunity tax credit**

You can claim the American Opportunity credit for 100 percent of the first \$2,000 and 25 percent of the next \$2,000 of an eligible student's higher education tuition and mandatory fees—a maximum \$2,500 annual tax credit per student. An eligible student may be yourself, your spouse, or a dependent. Students may take the credit only if they are not claimed as a dependent on another person's tax return. For 2015, the credit is phased out for incomes between \$80,000 and \$90,000 (between \$160,000 and \$180,000 for married taxpayers filing jointly). The credit is reserved for students who are attending a degree program at least half-time, and it can only be used for the first four academic years of postsecondary education.

### **Lifetime Learning tax credit**

You may claim the Lifetime Learning credit for 20 percent of up to \$10,000 in combined postsecondary tuition and mandatory fees for yourself, your spouse, or your dependent—a

\$2,000 tax credit. For 2015, the credit is phased out for incomes between \$55,000 and \$65,000 (between \$110,000 and \$130,000 for married taxpayers filing jointly). You may not take the credit if you are claimed as a dependent on someone else's tax return. The Lifetime Learning credit cannot be used with the American Opportunity credit for the same student in the same year. Unlike the American Opportunity credit, the Lifetime Learning credit doesn't require the student to be enrolled in a degree program at least half-time, and there is no limit on the number of years the credit may be taken.

### **Deduction for student loan interest**

You can take an above-the-line deduction of up to \$2,500 for student loan interest as long as the debt was incurred to pay higher education costs for yourself, your spouse, or a dependent. For 2015, the deduction is phased out for incomes between \$65,000 and \$80,000 (between \$130,000 and \$160,000 for married taxpayers filing jointly). To qualify for the deduction, the student must be enrolled at least half-time in a degree program. A student claimed as a dependent may not take the deduction on his or her own return.

### **Tax-free scholarships**

Most scholarships and grants are tax-free if the recipient does not have to provide services in exchange for the award, the recipient is a degree candidate at an eligible institution, and the funds are used to pay qualified education expenses.

### **Tax-free educational assistance**

Under a Section 127 educational assistance plan, employers may pay and deduct up to \$5,250 in educational expenses (including tuition, fees, books, supplies, and equipment) for each employee. The education does not have to be job-related, and the benefit is tax-free to the employee. It cannot, however, be used for an employee's children or other family members.

For more information on tax incentives for education, see IRS Publication 970, Tax Benefits for Education, available at [www.irs.gov](http://www.irs.gov).

*This material has been provided for general informational purposes only and does not constitute either tax or legal advice. Although we go to great lengths to make sure our information is accurate and useful, we recommend you consult a tax preparer, professional tax advisor, or lawyer.*

### **IRS CIRCULAR 230 DISCLOSURE:**

To ensure compliance with requirements imposed by the IRS, we inform you that any U.S. tax advice contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing, or recommending to another party any transaction or matter addressed herein.

###

CJ Ferrari and Mark Miller are financial advisors located at Miller Ferrari Wealth Management, 400 SW Bluf Dr., Suite 107, Bend, OR 97702. They offer securities and advisory services as Investment Adviser Representatives of Commonwealth Financial Network<sup>®</sup>, Member FINRA/SIPC, a Registered Investment Adviser. They can be reached at 541-639-8055 or [cj@millerferrari.com](mailto:cj@millerferrari.com) or [mark@millerferrari.com](mailto:mark@millerferrari.com).

© 2015 Commonwealth Financial Network<sup>®</sup>