

Tax Benefits & School Savings Plans

Tax Benefits

IRS Publication 970, Tax Benefits for Higher Education, is a source for the most current information. Download it from the IRS web site at www.irs.gov.

There are two tax credits available to help you offset the costs of higher education by reducing the amount of your income tax. They are the Hope Credit and the Lifetime Learning Credit, also referred to as education credits.

Lifetime Learning Credit

You may be able to claim a Lifetime Learning Credit of up to \$2,000 for qualified education expenses paid for all students enrolled in eligible educational institutions. There is no limit on the number of years you can claim the Lifetime Learning Credit for each student.

A tax credit reduces the amount of income tax you may have to pay. Unlike a deduction, which reduces the amount of income subject to tax, a credit directly reduces the tax itself. The Lifetime Learning Credit is a nonrefundable credit. This means that it can reduce your tax to zero, but if the credit is more than your tax, you don't get a refund.

The Lifetime Learning Credit you are allowed may be limited by the amount of your income and the amount of your tax.

Hope Credit

You may be able to claim a Hope Credit of up to \$1,500 for qualified education expenses paid for each eligible student.

A tax credit reduces the amount of income tax you may have to pay. Unlike a deduction, which reduces the amount of income subject to tax, a credit directly reduces the tax itself. The Hope Credit is a nonrefundable credit. This means that it can reduce your tax to zero, but if the credit is more than your tax, you don't get a refund.

The Hope Credit you are allowed may be limited by the amount of your income and the amount of your tax.

Comparison of Education Credits

Lifetime Learning Credit	Hope Credit
Up to \$2,000 credit per return	Up to \$1,500 credit per eligible student
Available for all years of postsecondary education and for courses to acquire or improve job skills	Available ONLY until the first 2 years of post-secondary education are completed
Available for an unlimited number of years	Available ONLY for 2 years per eligible student
Student does not need to be pursuing a degree or other recognized education credential	Student must be pursuing an undergraduate degree or other recognized education credential
Available for one or more courses	Student must be enrolled at least half time for at least one academic period beginning during the year
Felony drug conviction rule does not apply	No felony drug conviction on student's record

School Savings Plans

With more than 80 different 529 college savings plans available, plan time for your research. Visit www.savingforcollege.com, www.bankrate.com, and www.finaid.org for help. Be aware that these sites may contain advertisements for services. Remember to check federal tax laws for any recent updates or changes.

529 Plans

529 plans (named after the section of the federal tax code that governs them) are state-sponsored college savings plans. They are open to anyone, regardless of income. Each state determines the maximum amount that may be contributed annually per child and may be as high as \$300,000. While future withdrawals are federally tax free, you may owe gift tax or not depending on the amount of the contribution and when it is made. Grandparents can contribute too, especially if they want to reduce their estate tax liability. Parents may want to consult a tax advisor about 529 Plans.

529 plans are like a mutual fund, you can either pay a commission to a broker or go it alone. With more than 80 different plans to choose from, this may be a confusing task because each plan comes with its own fee structure and investment options. Almost every state offers a no-load (that means you don't pay a fee) option in addition to adviser-sold plans. Taking the time to do your own research can save you up to a 5% commission fee on your investment.

Two types of 529 plans are available: prepaid tuition plans and college savings plans.

1) Prepaid tuition plans let parents lock in future tuition at any in-state public college at today's prices.

2) College savings plans allow parents to use their plan funds for college plans at any college.

Coverdell Education Savings Account (CESA)

The annual contribution limit is \$2,000. Contributions can be made until the child is age 18. If you decide not to attend school, the account can be rolled over to another family member. Income limitations apply to account owners based on filing status.

Coverdell accounts can be owned by either the parent or the student. Qualified distributions from a Coverdell account are not counted as income on the FAFSA and therefore do not reduce financial aid eligibility. They can be rolled over to a family member of the previous beneficiary.

Contributions are not deductible on federal or state income tax, but earnings accumulate tax-free. Qualified distributions are exempt from federal income tax. Withdrawals can be made for primary, secondary, and postsecondary education expenses, including tuition, fees, tutoring, books, supplies, related equipment, room and board, uniforms, transportation, and computers.

Many credit unions offer Coverdell accounts. If your's doesn't check with other credit unions in your community as you may be eligible to join.