

TAX TIPS
PLANNING FOR COLLEGE
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As a parent with college-bound children, you are concerned with setting up a financial plan to fund future college costs. If your children are already college age, your goal is to pay for current or imminent college bills. I will address both of these concerns by suggesting several approaches that seek to take maximum advantage of tax benefits to minimize your expenses.

Qualified tuition programs. A qualified tuition program (known as a "529 Plan") allows you to buy tuition credits for a child or make contributions to an account set up to meet a child's future higher education expenses. Contributions to 529 Plans are not deductible. The earnings on the contributions accumulate tax-free until the college costs are paid from the funds. Distributions from qualified tuition programs are tax-free to the extent the funds are used to pay qualified higher education expenses. Distributions of earnings that are not used for qualified higher education expenses will be subject to income tax plus a 10% penalty tax.

Florida Prepaid Tuition Program. Many states offer state-sponsored "Prepaid Tuition" programs, and Florida is no exception. With the rising cost of education, these programs offer an attractive benefit and are, in effect, an insurance policy that essentially locks in the cost of your child's college education. Each state's plan is different. If you are interested in the details of Florida's plan, visit their website at www.MyFloridaPrepaid.com.

Series EE U.S. savings bonds. Series EE U.S. savings bonds offer two tax-savings opportunities when used to finance your child's college expenses: first, you don't have to report the interest on the bonds for federal tax purposes until the bonds are actually cashed in; and second, interest on "qualified" Series EE bonds may be exempt from federal tax if the bond proceeds are used for qualified college expenses. To qualify for the tax exemption for college use, you must purchase the bonds in your own name or jointly with your spouse - not the child's name. The proceeds must be used for tuition and fees. Room and board expenses are not considered "qualified" expenses.

Tax-exempt bonds. Another way to achieve economic growth while avoiding tax is simply to invest in tax-exempt bonds or bond funds. Interest rates and degree of risk vary on these, so care must be taken in selecting your particular investment. Please consult your investment advisor when selecting tax exempt bonds.

Coverdell education savings accounts. You may qualify for a Coverdell ESAs (formerly called Education IRAs) and make contributions of up to \$2,000 for each child under age 18. Contributions are limited for "Married Filing Joint" taxpayers whose income exceeds \$190,000 (\$95,000 for single). Although the contributions are not deductible, funds in the account are not taxed, and distributions are tax-free if spent on qualified education expenses.

Paying college expenses. In addition to the above funding suggestions, you may also be eligible for a federal income tax credit or deduction, whichever yields the highest tax benefit, for some of your child's tuition expenses. There are other payment methods which can yield substantial economic and tax benefits, as well.

Tuition tax credits. You can take a Hope tax credit of up to \$1,800 for 2008 per student for the first two years of college. You can take a Lifetime Learning credit of up to \$2,000 per family for every additional year of college or graduate school. Both credits are phased out for couples with incomes between \$96,000 and \$116,000 for 2008 or singles with income between \$48,000 and \$58,000 for 2008. Only one credit can be claimed for the same student in any given year.

Deductions for Tuition. In lieu of the above credits, a deduction of up to a maximum of \$4,000 is available to taxpayers with AGI of up to \$65,000 for singles and \$130,000 for joint filers. A maximum deduction of \$2,000 is allowed for singles with AGI up to \$80,000, or joint filers with AGI up to \$160,000. You should only take this deduction if it yields a greater tax benefit than the Hope or Lifetime Learning Credits discussed above.

Scholarships. Scholarships are exempt from income tax. For this exemption to apply, certain conditions must be satisfied. The most important are that the scholarship must not be compensation for services, and it must be used for tuition, fees, books, supplies and similar items, and not for room and board. Although a scholarship is tax-free, it will reduce the amount of expenses that may be taken into account in computing the Hope and Lifetime Learning credits, above, and may therefore reduce or eliminate those credits. Note also that in an exception to the rule that a scholarship must not be compensation for services; a scholarship received under a health profession scholarship program may be tax-free even if the recipient is required to provide medical services as a condition for the award.

Student loans. You can deduct interest on loans used to pay for your child's education at a post-secondary school, including some vocational and graduate schools. The maximum deduction is \$2,500. However, in 2008, the deduction phases out for taxpayers who are married filing jointly with AGI between \$115,000 and \$145,000 (between \$55,000 and \$70,000 for single filers). Some student loans contain a provision that all or part of the loan will be cancelled if the student works for a certain period of time in certain professions for any of a broad class of employers—e.g., as a doctor for a public hospital in a rural area. The student won't have to report any income if the loan is canceled and he or she performs the required services. This is an exception to the general rule that if a loan or other debt you owe is canceled, you must report the cancellation as income.

These rules are complex, and each person's circumstances are unique. As with any tax and financial planning strategy, you should first consult your tax and investment advisors prior to implementation.