

EDUCATION EXPENSES TAX BENEFITS - TAX CREDITS OR DEDUCTIONS

EDUCATION TAX CREDITS

While preparing for college, students and parents budget the costs including tuition, fees, supplies and room and board. However, there are tax benefits connected with a college education which includes several education tax credits and/or deductions.

Credits vs. Deductions

A *tax credit* lowers a tax liability, while a *tax deduction* lowers the amount of income of the tax liability. For example, a \$1,000 *tax credit* will lower the amount of taxes due by \$1,000. A *tax deduction*, will lower the taxable income. For example, if you are in the 15% tax bracket, your \$1,000 deduction will lower your tax liability by \$150.

Parents looking at possible education benefits on their tax returns should consider the available education credits: the *American Opportunity Credit* or the *Lifetime Learning Credit*. These two credits have similar requirements and qualified education expenses that they will cover, however there are distinguishing traits for each and only one of these credits may be claimed for a qualifying student each year.

American Opportunity Credit

Our friends at HR Block report a summary of the credits: The American Opportunity Credit (AOC) is a tax credit of up to \$2,500 for qualifying expenses such as tuition and fees. The credit is available for an eligible student attending an eligible educational institute and is calculated for 100% of the first \$2,000 and 25% of the next \$2,000 of the student's expenses. The AOC may be claimed by a taxpayer for fees paid that year from a qualifying student, their spouse, or their dependent. Qualifying students are students in their *first four* years of post-secondary education, pursuing a degree **and** are enrolled at least half-time for at least one academic period. The amount of this credit is reduced depending on the taxpayer's income and cannot be claimed for more than four years. Expenses paid with tax-free funds may not also be used for this credit. Up to 40% of the credit may be refunded to certain taxpayers. Qualifying educational expenses include tuition and required fees as well as course materials that are required as a condition of enrollment or attendance of the school.

Another requirement is that the student cannot be convicted of a felony at the end of the tax year that the credit is claimed. The taxpayer may not file separately from their spouse, if married, and neither spouse may be a nonresident alien. In general, the taxpayer claiming the credit may not be the dependent of another taxpayer, however if the dependent is not claimed they may still be allowed to claim the non-refundable portion of the credit.

Lifetime Learning Credit

The Lifetime Learning credit (LL) is available for up to \$2,000 per year, however this credit may not be claimed in the same year that the AOC for the same qualifying student. Like the AOC, the LL is phased out depending on the taxpayer's income and the qualifying expenses will be the same and you may claim expenses paid for the taxpayer, spouse, or dependent may also claim the credit so long as the dependent is not claimed by another taxpayer. This credit is *not refundable*, so it is limited by the tax liability of the person claiming the credit. Unlike the AOC, the LL is not limited to the number of years that it may be claimed, and the student is not required to take a minimum number of classes nor are the classes required to be part of a degree seeking program. Also, a student's felony conviction will not prohibit the taxpayer from claiming this credit.

Extra Resource: Tuition and Fees Deduction

Students and their parents may be able to deduct qualified college tuition and related expenses of up to \$4,000. This tax *deduction* is an adjustment to income, so it will reduce the amount of your income subject to tax. It may be beneficial to you if you do not qualify for the American Opportunity or Lifetime Learning credits. While it is not a tax credit, it is still a tax benefit for taxpayers.

EDUCATION TAX DEDUCTIONS

What Are Qualified Education Expenses?

Qualified educational expenses are school expenses like tuition, fees and other related expenses for an eligible student at an eligible institution.

- Tuition
- Fees: (fees charged by the university at enrollment; not application fees)
- Course Materials
- Computers
- Room and Board*

*Room and Board

Room and Board is not a qualifying education expense for most credits and deductions, it is a qualified education expense for the student loan interest deduction and for students with qualified tuition (529) and Coverdell Education Savings plans. The amount of room and board that is allowed as an education expense is the amount that is determined by the school and is included in the cost of attendance for federal financial aid purposes for any specific academic period OR the actual amount that the student is charged for a student living in student housing owned or operated by the school.

Keep in mind these expenses may be qualified education expenses; however, some credits and deductions include these expenses only if they are required as a condition of enrollment, and in some cases the expenses must be paid directly to the institution.

Expenses Paid with Loans

Any qualifying education expenses paid for with loans will still be qualifying education expenses in the year the expenses are paid even if the money comes from a student loan. If a loan is paid directly to the school, then the payment is treated as paid on the date that the school credits the students account with the payment.

What Expenses Are NOT Qualified Education Expenses?

In general insurance, medical expenses, transportation, and living expenses are not qualified as school expenses that qualify as a tax. Likewise, non-credit courses are not qualified education expenses, unless they are part of a degree program.

Keep Documentation

Most importantly, keep documentation of the educational expenses to aid in verifying the amounts that may use to claim these credits on the tax return.

Schools will send the student a Form 1098-T which will reflect tuition and fees and amounts that are billed by the school, and the amounts that the school receives in payment. Taxpayers may also use payment receipts or any other kind of statements showing the payment of qualified education expenses.

Contact your tax professional for further questions or clarification at info@mirtaxes.com.