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Paying for Education and Disability Expenses

"New Opportunities Created by Legislation Enacted"

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The recent legislation enacted, *Tax Cuts and Jobs Act of 2017*, was sweeping and touched many areas including Section 529 Education accounts. While many benefits taxpayers are accustomed to having like 'personal exemptions' were eliminated by this legislation, it left intact prior benefits like the American Opportunity and Lifetime Learning tax credits.

Section 529 accounts have been available for many years but could only be used for qualified expenses of higher education costs, those programs beyond grade 12. Beginning 2018, up to $10,000 per year can be withdrawn to pay for the costs of sending a child to public, private, or religious elementary or secondary school.

For high education costs, not only can they be paid using Section 529 accounts, they can also be used to create a reduction in income taxes owed by qualifying for one of the two education credits. The American Opportunities credit is available during the first four years of higher education with a maximum credit of $2,500 per year per student. To earn the maximum credit requires $4,000 of qualified higher education expense. The first $2,000 creates $2,000 of the credit. Of the next $2,000 spent, each four dollars of cost will create one dollar of credit, or $500 maximum. Education dollars spent can only be used once, either reimbursed by a 529 account or used to create a credit.

Once a student can no longer use the American Opportunities credit, the Lifetime Learning credit can be applied. Education expenses other than room and board can be used to create the credit. For every five dollars spent on qualified costs, one dollar of credit will be created up to the maximum credit of $2,000 so long as the student is enrolled in an eligible institution.

Reimbursing or paying for education costs with the use of a 529 account can be tricky. For these accounts there are two players, the Participant and the Beneficiary. Distributions from these accounts must be reimbursing or paying for expense in the same tax year as the distribution. If the Participant is someone other than the person most likely responsible for the costs, generally a parent, care must be given on the distributions. A Participant cannot take a distribution to reimburse a parent for an expense the parent paid. In these cases, the Participant can request a direct

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payment distribution where the funds are sent to the institution directly. Or, the parent must request the Participant pay the cost themselves and then a reimbursement request from the plan can be sent to the Participant. In this case, the Participant will receive a 1099 reporting the distribution but they will also have the expense which they paid and thus can offset the impact of the 1099. It might be helpful to change the Participant which is not a taxable event or combine 529 accounts. However, moving the 529 account may create a new commission which would not be desirable.

Another type of account entitled *ABLE*, Achieving a Better Life Experience, was enacted December 2014. ABLE accounts are sometimes referred to as 529-A accounts since they are also part of Section 529 of the IRS code. The focus of this account is to provide tax free growth on investments. When distributions are used to pay for disability-related expenses for the beneficiary, the distributions are tax free. Contributions up to the annual gift limit, currently $15,000, can be deposited into an ABLE account. This is an easy way to create a funding source for housing, transportation, assistive technology, or other lifestyle costs benefiting someone whose disability occurred prior to their 26th birthday. The beneficiary can be older than 26, but their disability must have had on onset date prior to their 26th birthday. To qualify for Federal or State assistance, many prior regulations required the beneficiary to be poor with assets or income below certain levels. An ABLE will not disqualify a beneficiary from most benefits but there are rules such as staying below the account value of $100,000 for SSI Disability payments to continue.

Unlike Education 529 accounts, a beneficiary of a ABLE 529-A can have only one account. This program is also state sponsored, but the beneficiary is not required to open an account with their state of residency. Like other tax beneficial accounts, when distributions are taken for non-qualified expenses a penalty may be due and the profits subject to income taxes. These accounts would be less costly, easier to open and potentially easier to manage than a special needs trust but may not include all the needed features. ABLE accounts are just another tool available to those who qualify.

Planning and knowing what tools are available is always beneficial and can help the users to lower their taxes and provide funding to meet some of the major expenses of their family.