Tax tips for parents with kids heading to college this fall

A higher education is expensive, and many parents spend years saving up. Others haven't had the financial bandwidth to save or have hit unexpected financial roadblocks along the way. Regardless of your situation, current tax breaks may be available to you (or to your children or even their grandparents) once your child begins attending college or other post-secondary school. Here are some tax tips.

Claim tax credits

If you have one or more children in college — or graduate school — you might be eligible for valuable tax credits. Remember, credits reduce your tax liability dollar-for-dollar, so they're more valuable than deductions of the same amount, which only reduce the amount of income subject to tax. So it's important to see if you're eligible for one or both of these credits:

American Opportunity Tax Credit (AOTC). You may be able to take this credit of up to $2,500 for the first four years of postsecondary education in pursuit of a degree or recognized credential — a 100% credit for the first $2,000 in tuition, fees and books, and a 25% credit for the second $2,000. The AOTC is 40% refundable, meaning you can get a refund if the credit amount is greater than your tax liability.

The credit is available on a per-student basis. For example, if you have a child who's a freshman and another who's a fourth-year senior, you can claim a credit of up to $2,500 for each child — as long as you otherwise qualify.

Lifetime Learning Credit (LLC). If your child is beyond the first four years of college or in graduate school, you may be able to take the LLC. It can be up to $2,000 for every additional year of college or graduate school — a 20% credit for up to $10,000 in tuition and fees.

However, only one LLC is available per tax return. If, say, you have one child in the fifth year of college finishing up his or her bachelor's degree and another child in grad school, you can claim only one LLC of up to $2,000. But if the first child instead is in his or her first four years of college, you can potentially claim the AOTC for that child and the LLC for your child in graduate school, as long as you otherwise qualify for both credits.

Speaking of qualifying, both credits are phased out for married couples filing jointly with modified adjusted gross income (MAGI) between $160,000 and $180,000, and for singles and heads of household with MAGI between $80,000 and $90,000. (Married taxpayers filing separately can't claim either credit.) If your income is too high for you to qualify, your child might be able to qualify on his or her own tax return.

Finally, only one education credit can be claimed for the same student in any given tax year. For instance, if your child graduated from college (in four years) in May of 2026 and starts graduate school in September of 2026, you can't claim both the AOTC for the last semester of your child's undergraduate education and the LLC for his or her first semester of graduate education. Other rules also apply to these credits.

Take advantage of tax-free 529 plan and ESA distributions

Does your child have a tax-advantaged education account, such as a Section 529 plan or Coverdell Education Savings Account (ESA)? Tax-free withdrawals can be taken to pay qualified expenses.

Section 529 plan distributions used to pay most postsecondary school expenses are income-tax-free for federal purposes and potentially for state purposes as well. Qualified expenses include tuition, mandatory fees, books, supplies, computer equipment, software, internet, and, for students enrolled at least half-time, room and board.

The postsecondary expenses that qualify for tax-free 529 plan distributions generally also qualify for tax-free ESA distributions. However, you can't take tax-free distributions from both accounts for the same expenses. Also, expenses paid with tax-free distributions from a 529 plan or ESA can't be used to claim education credits.

(If you have younger children and are deciding whether to contribute to a 529 plan or an ESA, keep in mind that there are other important differences to consider, such as the rules for using the funds for K-12 expenses, age-related limits for beneficiaries, and contribution limits — including income-based limits. Contact us to learn more.)

Think twice before tapping your retirement accounts

You can take money out of your traditional IRA or Roth IRA to pay college costs without incurring the 10% early withdrawal penalty that usually applies to distributions before age 59½. However, the distributions are subject to tax to the extent otherwise applicable.

You also may be able to borrow against your employer retirement plan, such as a 401(k) plan, or take withdrawals from it to pay for college. But before you do so, make sure you understand the tax implications, including any penalties you may incur.

And any time you make a withdrawal or take a loan from a retirement account, you're sacrificing the tax-deferred (or tax-free in the case of a Roth account) potential growth on that money. So first think carefully about the future impact on your retirement security.

Be aware of scholarship tax treatment

Has your child been awarded a scholarship? Congratulations! But it's also important to understand the tax impact.

Scholarships are exempt from income tax if certain conditions are satisfied. The three most significant are that, generally, the scholarship:

1. Must be for a student who is a degree candidate at an eligible educational institution,
2. Can't be compensation for services, and
3. Must be used for tuition, fees, books and supplies (not for room and board).

Also, a tax-free scholarship reduces the amount of expenses that may be taken into account in computing the AOTC and LLC and may reduce or eliminate those credits.

Advise grandparents and others to pay tuition directly

If someone gives you or your child money to pay some or all of your child's college expenses, it's generally treated as a taxable gift to the extent the payments exceed the gift tax annual exclusion of $19,000 per recipient for 2026. Married couples who split gifts may exclude gifts of up to $38,000 for 2026. (Gift tax generally applies to the giver, not the recipient.)

However, if the person (say, a grandparent) pays your child's tuition *directly* to an educational institution, it won't be treated as a taxable gift regardless of the amount. This applies only to payments of direct tuition costs (not room and board, books, supplies, etc.).

Consider your specific situation

Additional rules apply to many of these tax breaks, and there are other tax consequences to consider when it comes to your children and their post-secondary education. Contact us for more information about these breaks and to discuss your specific situation. We can help you take advantage of all the breaks available to you and your family and avoid tax pitfalls.