

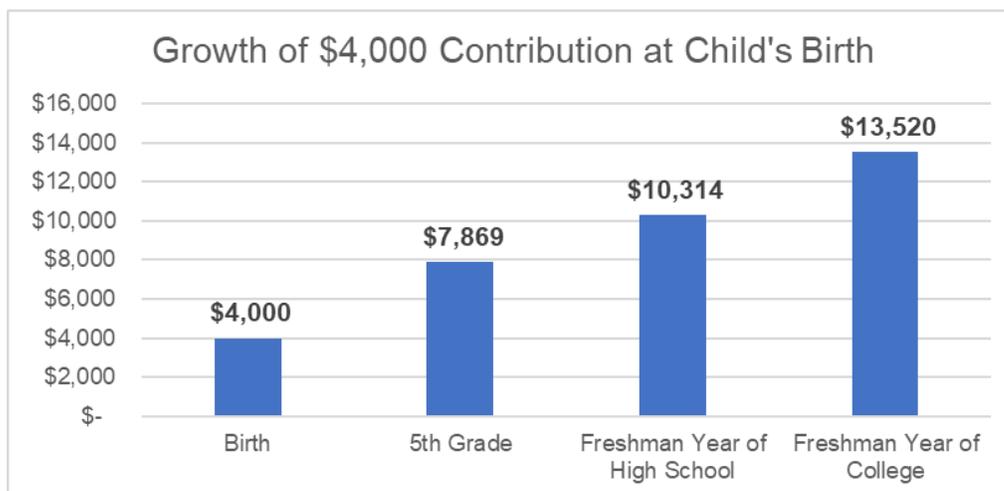
New Opportunities for 529 College Saving Plans

-By Billy Bruns, CFP® and Max Pauly

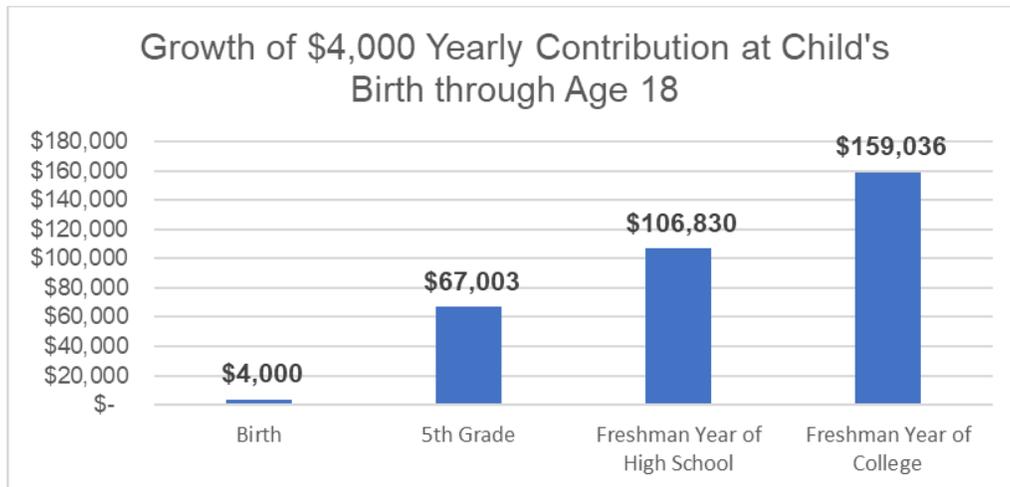
529 College Savings Plans have been a staple in financial planning since their creation in 1996. Named after Section 529 of the Internal Revenue Code, 529 plans were constructed to assist families in setting aside funding for their children's future college expenses. Historically, the major benefit of these plans has been tax-deferred growth accompanied by tax-free withdrawals to pay for qualified higher education expenses. These expenses include tuition, room and board (including off-campus with limitations), books, computers, and other miscellaneous expenses. Please note that these benefits are not limited to educational institutions within the state where the 529 plan was opened, but may be used at any accredited college, university, or private school within the United States and even some colleges abroad. Additionally, many states offer full or partial tax deductions or credits for contributions into the accounts. As a result of recent tax reform, a new benefit may be available to some of our clients: the ability to use as much as \$10,000 annually towards Kindergarten through 12th Grade tuition expenses at private schools.

Families have been able to save in Coverdell ESAs for K-12 tuition expenses, but they are fairly restrictive. ESAs have income limits with regards to who can contribute and a contribution cap of \$2,000 per year per beneficiary. Now, as a result of tax reform, you can use the more flexible 529 plan to pay for K-12 and college. Individuals no longer adding to their ESA can now also roll the account into a 529 without incurring a tax bill.

The benefits associated with a 529 plan are greater the longer you allow the money to remain invested in the account. If you use 529 assets to pay for education at a younger age you are diminishing the tax-free growth potential of the account. Here are two examples showing the power of tax-free growth in 529s (assuming a 7% annual rate of return).



Source: John D. Dovich & Associates, LLC



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Families that have been using 529s to save for college should be careful to avoid endangering their goal by taking assets out prematurely for K-12 tuition. If you're not on track with your college savings plan, taking money out to pay for K-12 education will only make it harder to reach your savings goals, as seen in the graphs above.

If you've been saving for college in the 529 and have been paying for private school out of pocket you may be able to benefit by doing both in the 529. For example, an Ohio family that started contributing to a 529 when their child was born made annual contributions for college but planned on stopping during high school to allow for more cash flow to go towards private high school tuition. Rather than paying for high school out of pocket they should first add the money to the 529. They can then use the account to pay for tuition while deducting their contributions (up to \$4,000/year) on their Ohio state income tax return.

The state tax deduction is an immediate benefit of contributing to a 529. Ohio recently raised their state tax deduction on contributions from \$2,000/year to \$4,000/year per beneficiary. If a couple wanted to contribute more than \$4,000 per year for a beneficiary, they can deduct the excess amount in a future tax year. Many states offer even greater deduction amounts than Ohio. For example, Illinois offers up to \$20,000 per year for a married couple filing jointly while Michigan is \$10,000 per year.

Overall this change gives families expanded access to a tax-advantaged account for education expenses. The longer your time horizon the more powerful the account can be. In addition, the state tax deductions from contributions are also a benefit. We would be happy to discuss how this expanded 529 offering fits into your financial plan.



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