

Financing Higher Education

Planning for the expenses associated with the ever increasing costs of higher education can appear daunting. However, understanding a few of the different options available can help minimize your stress.

529 College Savings Plans

A 529 College Savings Plan is a tax advantaged investment plan designed to help families save for higher education expenses. Earnings in the account are free of Federal taxes, and may be free of taxes in other states as long as the money stays in the account. When funds are distributed from the account for qualified higher education expenses, the distributions are exempt from Federal tax, and sometimes state income tax (where applicable). Generally, the funds in 529 plans are not considered part of the account owner's estate for federal estate tax purposes. You can contribute up to \$13,000 annually, and contributions can be made until the accounts for the same beneficiary reach a total of \$260,000. [as of 2011]

The beneficiary of the 529 can use the funds for qualified post-secondary education expenses such as tuition, required fees, room and board, textbooks, and supplies at qualified post-secondary institutions in the US and in some other countries. Post-secondary education includes: Community colleges, technical schools, vocational schools, colleges and universities, and graduate schools.

UGMA/UTMA Custodial Account

The Uniform Gift to Minors Act (UGMA) established a simple way for a minor to own investments and bank accounts

without requiring the services of an attorney to prepare trust documents or the court appointment of a trustee. The terms of this trust are established by a state statute instead of a trust document. The Uniform Transfer to Minors Act (UTMA) is similar, but also allows minors to own other types of property, such as real estate, fine art, patents and royalties, and for the transfers to occur through inheritance. UTMA is slightly more flexible than UGMA.

To establish a custodial account, the donor must appoint a custodian (trustee) and provide the name and social security number of the minor. The donor irrevocably gifts the money to the trust. The money then belongs to the minor but is controlled by the custodian until the minor reaches the age of trust termination (18 to 21, depending on the state and whether it is an UGMA or an UTMA). The custodian has the fiduciary responsibility to manage the money in a prudent fashion for the benefit of the minor.

The income from a custodial account must be reported on the child's tax return and is taxed at the child's rate, subject to the Kiddie Tax rules. The parent is responsible for filing an income tax return on behalf of the child. There is no special tax treatment for UGMA accounts. Children aged 14 and older must sign their own tax returns.

Unlike a 529 plan, neither the donor nor the custodian can place any restrictions on the use of the money when the minor becomes an adult. At that time the child can use the money for any purpose whatsoever without requiring permission of the custodian, so there's no guarantee that the child will use the money for his

or her education. Also, since UGMA and UTMA accounts are in the name of a single child, the funds are not transferrable to another beneficiary.

Finally, it should be mentioned that for financial aid purposes, custodial accounts are considered assets of the student. This means that custodial bank and brokerage accounts have a high impact on financial aid eligibility.

Federal Student Loans

Whether the student or the parent does the borrowing, your first and best option for securing a loan may be to go directly to the federal government. Stafford loans designed for students and Parent Loans for Undergraduate Students (PLUS) for parents are the most frequently used federal loans.

The key benefits of Stafford loans include:

- Low, fixed interest rates
- Income-based eligibility (indicated by data filed on the

Free Application for Federal Student Aid [FAFSA])

- Repayment deferral until after graduation

Like many borrowing programs, Stafford loans present both benefits and drawbacks. On the upside, they allow borrowers to defer repayment until after graduation. On the downside, Stafford loans carry annual borrowing limits that often are not high enough to cover a year of college costs.

For students and parents alike, borrowing through the federal education loan program, as well as through private loan issuers, offers tax deductions on interest paid.

Paying for college is a long-term commitment. Determining how to cover the costs should take into consideration a family's current financial needs as well as its short- and longer-term financial goals. Be sure to talk to your financial advisor and tax professional.

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