Morgan Stanley

Ten Things You Should Know About 529 College Savings Plans

As a consumer, you are probably aware that the cost of living is steadily increasing, and college costs are no different. In fact, college tuition and fees have increased at approximately two times the inflation rate—with the average cost of a private four-year college education topping $191,000 for a student starting next year.[1]

There are several options available to help you prepare for this important milestone, including 529 college savings plans which have revolutionized the way investors save for college. The plans offer both flexibility and control, and provide benefits that other education savings programs don't offer.

Here's what you should know if you are considering a 529 savings plan:

1. THEY'RE NOT JUST FOR KIDS.
Although most 529 savings plans are used to fund higher education for children, they are ideal for *anyone* with college funding needs. Whether you're a retiree who wants to pursue lifelong learning or a professional who is returning to school to advance your career, 529 savings plans may have a place in your investment portfolio.

2. IT'S A COLLEGE SAVINGS VEHICLE THAT ALLOWS TAX-FREE ACCUMULATION OF SAVINGS AND TAX-FREE WITHDRAWALS.
Money in a 529 savings plan accumulates free of federal taxes, and as long as funds are used for qualified college expenses, the withdrawals from your account are also tax-free.[2]

3. YOU MAY BE ELIGIBLE FOR ADDITIONAL TAX BENEFITS BY OWNING THE 529 SAVINGS PLAN OFFERED BY YOUR STATE.

Many states offer tax deductions to residents who contribute to their own state's plan. A few states offer a state tax deduction, regardless of which 529 plan you invest in. Your Financial Advisor can help you select the right plan from the available options.

4. IF YOU'RE THE ACCOUNT OWNER, YOU HAVE COMPLETE CONTROL OVER HOW 529 ASSETS ARE USED.

Some vehicles traditionally used for education funding — such as uniform gift to minors accounts — require that the assets be turned over to the beneficiary at a certain age. With a 529 plan, you maintain control. This means that if the beneficiary decides not to go to college, you can choose another beneficiary or use the plan for your own educational funding needs.

5. 529 PLANS TYPICALLY HAVE HIGH MAXIMUM CONTRIBUTION LIMITS, WHICH ALLOW YOU TO SAVE MORE FOR HIGHER-EDUCATION EXPENSES.

Most 529 plans have contribution limits in excess of $200,000 per beneficiary.[3]

6. CONTRIBUTING TO A 529 PLAN CAN REMOVE TAXABLE ASSETS FROM YOUR ESTATE, WHICH MAY REDUCE YOUR TAX LIABILITY.

Your contribution is treated as a gift to the named beneficiary (for gift-tax and generation-skipping transfer-tax purposes) and qualifies for the $14,000 annual gift-tax exclusion, allowing you to make fairly large contributions without incurring the gift tax. What's more, if you make a contribution between $14,000 and $70,000[4] for a beneficiary, you can elect to treat the contribution as if it were made over a five-calendar-year period for gift-tax purposes. This means the money gets out of your estate faster than if you made contributions each year. And the best part? Even though the asset leaves your estate, it doesn't leave your control if you are the owner of the 529 plan.[2,5]

7. THEY'RE NOT JUST FOR IN-STATE COLLEGES AND UNIVERSITIES.

Whether the goal is to spend a semester abroad or pursue a degree stateside, you can use a 529 savings plan at any in-state, out-of-state or international institution, as long as it's used with an accredited program.

8. THERE ARE NO INCOME OR AGE LIMITATIONS.

Some education funding vehicles have age and income restrictions, which limit the amount you can save. Generally, anyone can fund or use a 529 savings plan for education purposes.

9. PLANS ARE PROFESSIONALLY MANAGED AND OFFER A RANGE OF INVESTMENT OPTIONS.

With 529 savings plans, you have access to professional money managers with years of experience managing assets. Most plans also offer several investment options, such as age-based portfolios that become more conservative as the beneficiary nears their college attendance date.

10. ONLY A SMALL PERCENTAGE OF 529 ASSETS ARE INCLUDED IN FINANCIAL-AID CALCULATIONS.

Although the rules may vary slightly by state, generally, a 529 account owned by a parent for a dependent student is reported on the federal financial-aid application (FAFSA) as a parental asset and is assessed at a (maximum) 5.6% rate in determining the student's expected family contribution (EFC).[6]

As you can see, 529 savings plans have many features and benefits that can address your education funding needs. Call your Financial Advisor to help you develop the comprehensive education-planning strategy that is best suited to your needs and objectives.

[1] Represents the average cost at a private four-year institution for tuition, fees, room and board, books and supplies. Assumes an average 5% inflation rate. Sources: Edvisors.com (2015); The College Board (2015).

[2] Assets can accumulate and be withdrawn federally tax-free only if they are used to pay for qualified expenses. Earnings on nonqualified distributions will be subject to income tax and a 10% federal income tax penalty.

[3] Contribution limits vary by state. Refer to the individual plan for specific contribution guidelines.

[4] Double for married couples to $28,000 annually or $140,000 over a five-year period.

[5] If the donor dies within five years of making the contribution, the estate will recapture a portion of the assets.

[6] Family Guide to College Savings, 2014–2015 edition, www.savingforcollege.com.

The 529 Plan Program Disclosure contains more information on investment options, risk factors, fees and expenses, and potential tax consequences. Investors can obtain a 529 Plan Program Disclosure from their Financial Advisor and should read it carefully before investing.

Prior to investing, investors should consider whether their resident state or the resident state of the beneficiary offers any state tax or other benefits that are only available in that state's qualified tuition program.

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