



WHAT's on TAP

at Fulcrum

529 PLANS

PAYING FOR A CHILD'S COLLEGE EDUCATION WITH A 529 PLAN

Every parent wants their children to succeed in life, both personally and financially, and going to college after high-school plays an important part in achieving both. For example, according to the U.S. Department of Commerce, the average annual earnings for high school graduates is approximately \$26,000, whereas college graduates earn closer to \$46,000.

What Does It Cost to Send a Child To College? Anyone who has ever looked into the cost of a four year college education knows that with the exception of purchasing a home, paying for a child's education is often the second most expensive thing for which parents will pay. And, if you have ever wondered what the cost would be to put a child through college, go to one of the many website calculators that are available (e.g. www.savingforcollege.com). Based on information you submit, these calculators estimate the total projected cost of sending your child to college and, give you an idea about how much you will need to save in order to finance that education.

Start Saving When They Are Very Young. Let us assume that your child is currently one year old, and your alma mater is charging \$15,000 per year, including all expenses, tuition, housing, meals etc. Let us also assume that each year college costs will increase at the current level of inflation of 3% (a huge assumption since college costs increased around 6% from 2006 to 2007), and projected average annual returns on your investments of 8%. Using those figures, you will need upwards of \$103,723 to pay for four years of school. That means you will need to save \$212 per month for the next 17 years. If, on the other hand, your child is currently 10 years old, and you have not yet begun to save, the money you will need to save drops to \$79,495, but your required monthly savings requirement shoots up to \$549!

As investment advisors, one of our jobs is to counsel our clients on the best means for providing funding for their children's college education. And, in the same way that you might save for retirement through a 401 (k) plan or an IRA, there are a variety of savings tools specifically geared towards paying for a college education. One such tool is the "college savings plan" popularly known as a 529 Plan.

... 529 Plans Help With College Savings

What Are 529 Plans? A 529 plan is a tax-advantaged savings plan designed to encourage saving for future college costs. Legally known as “qualified tuition programs”, they are called “529 plans” after the section of the Internal Revenue Service Code that deals with the tax implications of the program. 529 plans are sponsored by states, state agencies, or educational institutions and are usually offered through private sector fund managers. Every state and the District of Columbia sponsor at least one type of plan. There are two types of 529 plans: pre-paid tuition plans and college savings plans.

First You’ve Got Your Pre-paid Tuition Plans . . . As an investment, pre-paid tuition plans have a variety of restrictions that may make them less appealing to investors than college savings plans among them certain residency requirements.

. . . And Then You’ve Got Your College Savings Plans. Typically, a 529 plan is owned by a child’s parents with the child noted as beneficiary. Owners contribute money into the plan and have control over how the funds are invested, even after the child reaches his or her majority. Non-owners can also make contributions into 529 plans although they are held to the same contribution limits that apply to owners (see below). Following is a table comparing prepaid tuition plans with college savings plans:

“An empty nest shouldn’t mean an empty wallet”

| Prepaid Tuition Plan | College Savings Plan |
|---|--|
| Locks in tuition prices at eligible public & private colleges & universities. | No lock on college costs. |
| All plans cover tuition and mandatory fees only. Some plans allow you to purchase a room & board option or use excess tuition credits for other qualified expenses. | Covers all "qualified higher education expenses," including: <ul style="list-style-type: none"> • Tuition • Room & board • Books, computers (if required) • Mandatory fees |
| Most plans set lump sum & installment payments prior to purchase based on age of beneficiary & number of years of college tuition purchased. | Many plans have contribution limits in excess of \$200,000. |
| Many state plans guaranteed or backed by state. | No state guarantee. Most investment options are subject to market risk. Your investment may make no profit or even decline in value. |
| Most plans have age/grade limit for beneficiary. | No age limits. Open to adults and children. |
| Most state plans require either owner or beneficiary of plan to be a state resident. | No residency requirement. However, nonresidents may only be able to purchase some plans through financial advisers or brokers. |
| Most plans have limited enrollment period. | Enrollment open all year. |

Source: *Smart Saving for College*, FINRA®

The benefits of 529 plans are realized when funds are used to pay for qualified higher education expenses (QHEEs). QHEEs are expenses that are incurred at a qualifying academic institution to defray certain eligible education expenses (go to <http://www.fafsa.ed.gov/FOTWebApp/FSLookupServlet> for a list of qualifying schools). There is no penalty for attending an out-of-state school. Withdrawals are tax-exempt when used to pay for QHEEs. In the event funds are withdrawn and used for purposes other than QHEEs, those funds will be taxed as ordinary income together with a 10% penalty. Among the various allowable expenses are such things as: tuition, room and board, text books and supplies.

It is important to note that because funds held in 529 plans are treated by colleges as parental assets when calculating expected family contributions towards college costs, setting up a 529 plan may impact a student's ability to obtain other financial aid.

Some of The Benefits of a 529 Plan. Like anything else that involves the Internal Revenue Service, there are certain things one must consider before setting up a 529 plan.

- **Federal & State Tax Exemptions**

The earnings and appreciation on 529 investments are not subject to federal or state (with some exceptions) taxation so long as the proceeds are used for qualified expenses. This is perhaps the greatest benefit of the 529 plan program.

- **State Tax Deductions**

Some states allow deductions from state income tax for contributions to 529 plans. Typically, deductions can only be taken for contributions made into in-state plans. For example, Virginia residents may take certain state income tax deductions if they contribute to the Virginia College Savings Plan. Every state has different rules regarding state income tax deductions. Louisiana, Maine, Michigan, Minnesota, and Rhode Island offer matching contributions to participants in their 529 plan. The matching amount is based on a variety of factors including the amount being contributed and, the contributor's income. However, not every state allows state income tax deductions for contributions to a plan.

- **No "Home State" Restrictions**

Parents are not limited to investing in their home state's 529 plan. As a result, parents have a wide variety of options from which to choose. This is especially important if your home state does not offer any state income tax benefit for investing with the in-state plan. Currently, there are 22 such states. Although some states waive certain fees associated with setting up a 529 plan, award rebates and match contributions for in-state 529 plan contributions, the benefits of using an out-of-state plan may outweigh the opportunity cost of using your in-state plan. Three states (Alabama, Illinois, and Pennsylvania) require account owners to include earnings on out-of-state plan withdrawals on their state income taxes, even if the withdrawals are used for QHEEs.

- **Rollovers and Transfers**

529 plans are open to transfers from certain other investment plans including rollovers from other out-of-state 529 plans. However, restrictions may apply and residents in certain states may face adverse tax consequences as a result of transfers and rollovers. For example, UTMA/UGMA custodial accounts can be transferred into 529 plans but, with some restrictions. One of the more notable restrictions is the fact that the owner of the custodial account will be required to sell the positions held in the custodial account (a taxable event) and the owner of the custodial account must be the beneficiary of the 529 account. So, while this may be a great way to maximize returns on your investments, enabling you to shop around for the best performing plan, there are also some drawbacks. Colorado, Georgia,



12010 Sunset Hills Road
 Suite 875
 Reston, Virginia 21090
 Phone: 703-689-4001
 Fax: 703-689-4016
 Web: www.fulcrumsecurities.com
 E-mail: info@fulcrumsecurities.com

Founded in 2003, Fulcrum Securities is an NASD registered full service investment firm offering brokerage and money management services to individual and institutional investors. Fulcrum Advisory Services is an SEC registered investment advisory firm providing asset management and consulting services.

With many years experience overseeing assets for a diversified client base, we are uniquely suited to offer unparalleled personalized attention and advice to our clients.

For further information about Fulcrum and our services, please give us a call.

“Investment Solutions for Today’s Investors”

Iowa, Utah, Nebraska, New York, and Virginia require people who transfer their 529 plans out-of-state to add back to their taxable state income any deductions received as a consequence of contribution made to the in-state 529 plan. Three states, Alabama, New York, and Pennsylvania, require residents to add to their taxable state income, the earnings on any rolled-over 529 plan. The regulations governing these “add backs” are known as “*Recapture Rules*.”

- **No Income Restrictions**

Regardless of your income, maximum contributions into a child’s 529 plan are currently set at \$12,000 for individuals and \$24,000 for married couples - Federal gift tax provision apply to any contributions above these amounts. Maximums are calculated on a *per child* basis and anyone can contribute to a child’s 529 plan including non-family members who face the same contribution restrictions. One also has the option of making a lump sum contribution of \$60,000 (\$120,000 for couples), with the understanding that no additional contributions be made for five years - a great way to get the money working sooner.

Over the course of a child’s lifetime, a college education could mean a difference of millions of dollars in income and parents should not have to “bust the bank” in order to afford future college costs. An investment plan is as necessary for your child’s education as it is for your own retirement and as your financial advisor, Fulcrum Securities is here to provide both advice and solutions to help you achieve your investment goals. Speak to your investment advisor and tax professional before investing in a 529 plan.

**For further information,
 please contact your Fulcrum Securities Investment Advisor**

September 2007

Copyright 2007. Fulcrum Securities Inc./Fulcrum Advisory Services Inc. 12010 Sunset Hills Road, Suite 875, Reston, Virginia 20190, tel. 703-689-4001, fax 703-689-4016. All Rights Reserved. Information contained herein is based on data obtained from recognized services, issuer reports or communications, or other sources believed to be reliable. However, such information has not been verified by us, and we do not make any representations as to its accuracy or completeness and we are not responsible for typographic errors. Any statements nonfactual in nature constitute only current opinions which are subject to change without notice. Neither the information nor any opinion expressed shall constitute an offer to sell or a solicitation of an offer to buy any securities or commodities mentioned herein. No bank guarantee, not FDIC insured, may lose value.