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529 COLLEGE SAVINGS: THE GOOD, THE BAD, & THE UGLY

Is a 529 College Savings Plan Right for You?

Eligibility

Pros

Anyone can set up a 529 plan for the benefit of someone under 30. This can even be yourself if it is done for a child.

Considerations

If the beneficiary of the 529 is over 30, it will trigger a withdrawal, penalty and a taxable event. However, **it is portable** and can be transferred to another person under 30, so if your child skips college, you can transfer it to your grandchild.

contributions

Pros

Unlike an IRA, which has a \$6,500 annual contribution limit, a 529 has **no such restriction**. However, contributions must stay within gift/transfer tax limits of \$14,000 per year.

Considerations

There is a 5-year election where one can drop in \$70,000 at once, **avoiding the gift tax**. Nothing more can be contributed during the next four years, however. Under federal law, 529 plan balances **cannot exceed the expected cost** of the beneficiary's qualified higher education expenses. Limits vary by state, ranging from \$235,000 to \$425,000. California's is \$371,000. Virginia's is \$350,000.

Fees

Pros

Investment costs are higher, at 0.21% more per year than a comparable mutual fund, but these **costs have decreased** over the years. The slightly higher costs **may be covered by tax savings**, if properly distributed. Many 529 vehicles have program maintenance fees of about \$20, as well. In addition, there are fund load fees, advisor fees and state fees.

Considerations

Though fees exist, it is important not to get into the habit of **pinching pennies to burn dollars**. American Funds is #1 in the market with investment performances that exceed the competition. Even with all the fees, **effective account growth outpaces** even the low-fee 529s. At the end of the day, you will have **grown more** than you would have with a no-fee account.

The Advantage Growth

Pros

529 college savings plans are **tax free** as long as funds are distributed and used for educational expenses. These include tuition, mandatory fees, books, supplies and, for students enrolled more than half time, **room and board**. Certain states also have **tax credits**. The State of New York, for example, encourages residents to contribute to their 529s by giving a \$10,000 credit each year. No such credit exists for California residents.

Considerations

If funds are withdrawn early, there is a 10% federal penalty. Certain states will also impose a state penalty. There will also be a taxable event and gains will be taxed as income.

Other Features

Pros

529 plans have **low minimums**, some as low as \$15. In contrast, many mutual funds have high minimums, such as \$1,000. Also, there is **little-to-no impact** on financial aid.

Considerations

The 529 college plan loses its attractive features if you do not use it for educational purposes, so it is **inflexible**. If flexibility is needed, options such as a variable life insurance policy or a Roth IRA may achieve the same objectives.