

Education Funding

In accumulating funds for college, one of the first questions a family will face is, “Where do we get the money?” Many financial professionals will recommend to their clients that money saved for college should be placed in relatively low-risk investments. If there is a long enough time frame, the savings may be placed initially in higher risk (and potentially higher return) investments. As the time for college gets closer, the accumulated funds can be shifted into more conservative choices.

The ultimate decision will depend on a range of factors such as the number of years until college begins, the amount of money available to invest, a family’s income tax bracket, risk tolerance, and investment experience. A few of the more traditional approaches are:

- **Savings accounts:**Including certificates of deposit, money market deposit accounts and passbook savings accounts.
- **Tax-free municipal bonds¹:**Held either directly or through a mutual fund.
- **U.S. Treasury securities:**Such as treasury bills or treasury bonds.
- **Growth stocks/growth mutual funds¹:**For the long-term investor.

Tax-Advantaged Strategies

There are a number of tax-advantaged² strategies available to accumulate funds for college expenses. The rules surrounding these strategies can be complicated and they should only be used after careful review with a tax or other financial professional.

- **IRC Sec. 529 Plans:** These plans allow an individual to either pre-pay a student’s tuition, or contribute to a savings account established to pay the student’s “qualified higher education expenses.” Contributions are not tax deductible, but growth in an account is tax-deferred. If certain requirements are met, distributions to pay qualified higher expenses are excluded from income.³
- **Coverdell Education Savings Account (C-ESA):** Up to \$2,000 per year may be contributed to a C-ESA for an individual. Contributions are not tax-deductible, but growth is tax-deferred. Distributions are excluded from income if used for qualifying educational expenses. Other restrictions may apply.
- **U.S. savings bonds:** Interest on series EE savings bonds issued after 1989, or Series I savings bonds, may (certain limits apply) be excluded from income if qualified education expenses are paid in the year the bonds are redeemed.
- **Baccalaureate bonds:** A special form of state-issued, tax-exempt municipal bond. Interest on these bonds is generally **tax** free, at both the state and federal level.

Who Owns the Funds?

A second issue facing families planning for college is the question of “Who will own the funds?” The answer to this question involves issues of control, income and gift taxes, and may impact any future application for financial aid.

- **Parents:** Either in accounts specifically earmarked for college or as a part of a general family portfolio.
- **Child:** Often a custodial account is used, under either the Uniform Gifts to Minors Act (UGMA) or the Uniform Transfers to Minors Act (UTMA).
- **Trust:** In certain situations, usually involving wealthy families, specialized types of trusts may be used, such as a Crummey trust or charitable remainder trust.

Other Resources

There are a number of excellent references and guides to investments and college planning available in bookstores and public libraries. State and federal agencies involved in higher education also are excellent sources of information. In addition, there are a number of sites on the Internet which can provide information, including the following.

- [The College Board](#)
- [National Association of Student Financial Aid Administrators](#)
- [National Association of State Treasurers](#) - Links to state-run web pages on prepaid tuition or college savings plans
- [Consumer Information Catalogue](#)

Begin Early and Seek Professional Advice

Developing a plan to save for a child’s college education can be complicated. Questions can arise involving income, estate, and gift taxes, as well as investment issues. Individuals are strongly advised to begin a savings program as early as possible, and seek professional financial planning or tax advice before implementing a savings plan.

¹Mutual funds are offered by prospectus, which should be read carefully before investing or sending money.

²The rules described here concern federal income tax law. State or local income tax law may vary.

³The fees, expenses, and features of 529 plans can vary from state to state. 529 Plans involve investment risk, including the possible loss of funds. There is no guarantee a college-funding goal will be met. Under current federal tax law, the tax-free treatment of qualified 529 plan distributions ends December 31, 2010.