THE BASICS OF COLLEGE SAVINGS PLANNING

BAILEY WEALTH SERVICES

THE BASICS OF COLLEGE SAVINGS PLANNING

If you're planning on your children getting a college degree, there are several things to think about. Where to go, what to study — and how to pay for it — are all likely top of mind. When it comes to the question of why they are attending college, today's high school students seek higher-pay, more job opportunities and purpose-driven careers after college.

WHY ARE YOU CONSIDERING APPLYING TO COLLEGE?

"Set myself up for a higher paying job"	*50%*
"Give myself more employment opportunities"	*44%*
"Gain in-depth knowledge in a specific field before pursuing a career in that field"	*35%*

Source: Fidelity 2023 College Savings & Student Debt Study

GETTING YOUR HEAD AROUND THE COST

It's rare to scan the daily news without seeing an article about the increasing cost of going to college. When you add up tuition, room and board, books and other expenses, the total cost of a year at a public or private college may seem impossible to reach.

The College Board is a not-for-profit organization whose mission is to connect students to college opportunity and success. This organization has been serving for more than 100 years and is a key source for college costs. In its 2022 report, "Trends in College Pricing and Student Aid," it reports that a moderate college budget for an in-state student attending a four-year public college in 2022-2023 averages $27,940. For out-of-state students at public colleges, the average budget comes to $45,240. And for students attending private colleges, the average is $57,570. For some historical perspective, the College Board reports that over the past 10 years, tuition, fees and room and board has gone up 2% a year for public four-year universities. If you're a parent with a baby, that means by the time your child is 18, it could cost nearly $40,000 a year for them to attend an in-state public university.

LPL IS HERE TO HELP

This brochure will provide you with practical information about the resources available to help you save for college. In addition, it will cover some basic information regarding financial aid as well as student loans. Your financial professional at LPL Financial is always available to provide guidance, educate you on your savings options and help your family create a solid plan to achieve this important financial goal.

COLLEGE SAVINGS RESOURCES

529 PLANS

A 529 Plan is an education savings plan operated by a state designed to help families set aside funds for future college costs. It is named after Section 529 of the Internal Revenue Code which created these types of savings plans. 529 accounts can be used for college and trade schools and up to $10,000 of K-12 education costs including tuition, room and board at school and a computer if required for your student's classes. 529 accounts can also help pay down $10,000 of student loans per student.

Source: https://www.savingforcollege.com/article/what-you-can-pay-for-with-a-529-plan

529 Plans are established by states. Except for Wyoming, all states offer at least one 529 Plan. In addition, anyone can open a 529 Plan account: a parent, grandparent or friend. And you can invest in a 529 of another state. The beneficiary can be anyone, even you. The only requirement is that the account owner be a U.S. citizen.

There are two types of 529 plans:

Savings Plans work much like a 401k or IRA by investing your contributions in mutual funds or similar investments. Your account will go up or down in value based on performance.

Prepaid Plans let you prepay all or part of the costs of an in-state public college education. This lets you lock in the tuition rate by purchasing units or credits. These plans are offered in only nine states as of 2023, and the credits can only be used for tuition. Read the plan details carefully, as some allow transfer to other schools, but your options can be limited.

The person who opens the 529 account or purchases the prepaid plan, owns the account, not the beneficiary, and always retains control. They decide how to invest the money contributed, how withdrawals are used and can change the beneficiary.

Contributions to a 529 Plan

529 Plans have no income limits, age limits or annual contribution limits. Initial minimum contributions often start as low as $25, and then monthly contributions can be as low as $15 in some states. Most plans allow you to "set it and forget it" with automatic investments that link to your bank account or payroll deduction plans. There are lifetime contribution limits, which vary by plan, ranging from $235,000 - $550,000 (as of June 2023).

In 2023, contributions up to $17,000 per beneficiary per account owner qualify for the federal annual gift tax exclusion. You can combine five years of annual exclusion gifts to a 529 plan. You'll need to file IRS Form 709 and check the box to treat the gift as spread over 5 years. It's always smart to check with your tax advisor about estate or gift tax consequences of contributing to a 529 Plan if this could be an issue for you.

Source: www.savingforcollege.com

529 Plan Income Tax Benefits

Contributions to 529 plans are made with after-tax dollars. Although contributions are not deductible, earnings in a 529 plan grow tax-free and will not be taxed when the money is taken out for qualified education expenses. Additionally, over 30 states and the District of Columbia currently offer a full or partial tax deduction or a tax credit for 529 plan contributions. Check with your state to see if your contributions qualify.

If a withdrawal is taken for a non-qualified expense, the earnings portion will be subject to federal, and possibly state, income tax. Also, the earnings portion of withdrawals taken for non-qualified expenses may be subject to a federal tax penalty of 10%. There may also be state income tax penalties.

ROLLOVERS OF 529 PLANS TO ROTH IRAS

For a number of reasons, your plans can change, and your 529 plan savings may end up not being used for the original beneficiary or there may be leftover funds in the account. The 2022 Secure 2.0 Act made it possible, as of 2024, to roll 529 funds over to a Roth IRA for the beneficiary without incurring penalties or taxes. The lifetime rollover limit is $35,000, but the contributions for 2023 are subject to annual IRA limits ($6,500 and $7,500 for those over age 50). The 529 must also have been open for more than 15 years.

COVERDELL ACCOUNTS

A Coverdell Education Savings Account (ESA) is a tax-preferred savings and investment account to encourage people to save for future education costs. Compared to 529 accounts, they are considered a lower-cost account option and have a wider range of investment options, such as individual stocks, bonds, exchange-traded funds, mutual funds and real estate investments.

There are some items to be aware of, including:

- The beneficiary of the Coverdell ESA must be under the age of 18 at the time the account is established.
- The contribution limit is $2,000 per beneficiary. When accounts are established by different family members for the same child total contributions cannot exceed $2,000 in a year for that beneficiary.
- There is an income limit of $110,000 for individuals and $220,000 for taxpayers filing married filing jointly above which you cannot contribute to ESA accounts.
- The low contribution limit means even a small annual maintenance fee charged by the financial institution could significantly affect your ESA investment return.
- Your contribution goes into an account that will be distributed to your child at 30 years old if not used for college, unless the beneficiary has special needs. The earnings in the account will be income taxable and subject to a 10% penalty. You can change the beneficiary on the account or transfer the balance to another Coverdell or 529 plan, subject to certain rules.

Sources: www.savingforcollege.com,
https://www.irs.gov/pub/irs-news/at-03-38.pdf

Coverdell Account Income Tax Benefits

Earnings in ESA accounts are tax-deferred, just like 529 plans. Similarly, if withdrawals are used for qualified education expenses, as defined by the Internal Revenue Service, they are exempt from federal income taxes. If a withdrawal is used for non-qualified expenses, then the earnings portion of the withdrawal is subject to federal, and perhaps state, income tax. Also, in most cases, the earnings portion of withdrawals taken for non-qualified expenses is subject to a federal tax penalty of 10%, though there are some exceptions.

Source: Bankrate.com Guide to Coverdell Education Savings Accounts

U.S. SAVINGS BONDS

Some or all the interest earned on U.S. Savings Bonds may be excluded from income if used for higher education. The bonds must be Series EE bonds issued after 1989, or Series I bonds. Bonds must be issued in the name of the taxpayer 24 years or older. Qualified expenses include tuition and fees, and contributions to Coverdell and 529 accounts, but do not include textbooks or room and board. It’s important to remember to pay the education expenses the same year you cash the savings bond, and you must claim the credit on that year’s tax return.

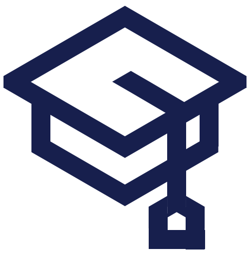
Sources: TreasuryDirect.gov Using Bonds for Higher Education
IRS.gov Exclusion of Interest from US Savings Bonds Form 8815

UTMA AND UGMA ACCOUNTS

Accounts set up under the Uniform Gifts to Minors Act (“UGMA”) and the Uniform Transfers to Minors Act (“UTMA”) have been used for many years to pay for college education. One advantage is that a portion of the earnings in these accounts may be either tax-free or taxed at the child’s tax rate. ($1,050 is tax-free, and the next $1,050 is taxed at the child’s rate). Earnings above this initial $2,100 is taxed at the parent’s tax rate until the child reaches the age of majority. The disadvantage is that earnings are taxed at all (unlike 529 accounts). Another disadvantage is once the child is no longer a minor, they control the account and how the money is spent. Depending on the state, one is no longer a minor between the ages of 18 and 25.

UGMAs and UTMAs can be rolled over into Section 529 Plans, but account control remains with the beneficiary once they are no longer a minor. Some financial planners suggest spending down the account for the benefit of the minor first. When the UGMA or UTMA balance is zero, then use the 529 plan for their remaining education expenses.

Please note these savings vehicles can be complicated, from both an estate planning and education funding standpoint. Please consult your financial planner, tax consultant and estate attorney for more details.



Source: www.savingforcollege.com

FINANCIAL AID OPPORTUNITIES

Once accepted to a college, you will receive a financial aid offer letter, that may include assistance from a variety of programs. Federal Financial aid is available in the form of grants, work-study programs, and loans. Some of the loans do not have to be paid back if certain conditions are met. To check your child's eligibility, always submit a Free Application for Federal Student Aid (FAFSA) at studentaid.gov.

RECENT CHANGES TO FAFSA APPLICATION PROCESS: WHAT TO KNOW

Typically, the FAFSA application process opens on October 1 for students and families starting college the following year. But in 2023, the FAFSA application will open sometime in December (to apply for the 2024-25 school year). The reason has to do with "FAFSA simplification" and how financial need is calculated. The Department of Education needed extra time to get the application launched. Here are a few of the key changes:

Streamlined application process. The FAFSA has been greatly simplified and reduced from 108 questions down to just 36, making it much easier and faster for families to apply for funding.

Discount eliminated for multiple children in college. Previously, financial aid eligibility increased for families with more than one child enrolled in college at the same time. Under the new legislation, the FAFSA no longer provides this discount.

Expected Family Contribution (EFC) replaced by Student Aid Index (SAI). The method of calculating how much aid you are eligible for has changed significantly. Expected Family Contribution (EFC) is no longer the metric used to calculate need-based aid. Instead, a new metric, Student Aid Index (SAI), is used. To help determine what you qualify for, review the Student Aid Index Chart and Calculator to see how your family will score. Or go to: https://tinyurl.com/3ejh26ef.

Determining which parent completes the form in the case of a divorce or separation. Previously, in a two-parent household, either parent could complete the FAFSA. However, if the parents were divorced or separated, the custodial parent was required to fill out the FAFSA and that parent's income and assets were counted for financial aid purposes. The income used was for the prior-prior year, meaning if you were submitting the FAFSA in 2022, you used your 2020 tax return, instead of the most recent return.

The new legislation requires the divorced parent who provided the most financial support in the "prior-prior" tax year to complete the FAFSA, instead of the custodial parent. The parent who provided the most support in 2021 must complete the 2023 FAFSA for the 2024-25 award year. In cases in which the support provided is 50/50, it may default to the parent or household with the highest AGI. It's important to note that even if the parents were never married, these same rules apply.

529 Accounts may now be reported on the FAFSA. About the first $10,000 will fall under the Asset Protection Allowance (the exact amount depends on the older parent's age). Any parental assets over that could reduce the aid package by up to 5.64% of the asset's value.

Source: Aug 10, 2023, https://www.savingforcollege.com/article/yes-your-529-plan-will-affect-financial-aid#:~:text=The%20value%20of%20a%20529,on%20the%20older%20parent's%20age).

No financial consequences for contributions made by others. Previously, families were required to report "money received or paid" from others on the student's behalf on the FAFSA. This means that if grandparents, other relatives, friends, or others outside the immediate family provided financial support to help pay for college costs, it had to be reported. Under the new legislation, this form of untaxed income will no longer be considered in the SAI and cannot affect a student's chances for need-based financial aid.

Many advisors still recommend waiting until the student's senior year or until graduation, to ensure their contributions do not adversely affect non-FAFSA based awards. Some schools may have their own scholarships and grants based on merit or need, not necessarily on FAFSA.

https://www.lendingtree.com/student/colleges-no-student-loans-policy/.

For more comprehensive information on the changes to the FAFSA application process, read "Seven Major FAFSA Changes: What Families Need to Know" (Kiplinger Personal Finance, February 16, 2023). Or go to: https://tinyurl.com/bdfykxcn.

U.S. DEPARTMENT OF EDUCATION LOAN PROGRAMS

The U.S. Department of Education offers the following loan programs (check out studentaid.gov for current interest rates). It's important to note that a key component of how much the student must repay is when interest starts accruing. In addition, "subsidized" loans mean the government pays the interest while the child is in school.

- **Direct Subsidized Loans** are loans made to eligible undergraduate students who demonstrate financial need to help cover the costs of higher education at a college or career school. Repayment typically must start within six months of graduation, leaving school, or going below half-time attendance.
- **Direct Unsubsidized Loans** are loans made to eligible undergraduate, graduate, and professional students (for example medical school), but in this case, the student does not have to demonstrate financial need to be eligible for the loan. Interest on the loan begins accruing immediately. The same repayment rules as subsidized loans apply.
- **Direct PLUS Loans** are loans made to graduate or professional students and parents of dependent undergraduate students to help pay for education expenses not covered by other financial aid. The same repayment rules as subsidized loans apply.
- A **Pell Grant** and other types of federal student aid grants are available as direct aid (grants do not need to be repaid) based on exceptional financial need and the cost of attending college. Check out U.S. Dept. of Education Federal Pell Grant Program details.

Source: www.savingforcollege.com

STATE FINANCIAL AID PROGRAMS

Students can also benefit from state financial aid programs. General information about these programs is available from the National Association of State Student Grant and Aid Programs. In addition, corporations, foundations, and communities offer scholarships, grants and endowments to students, many of which are not primarily based on financial need or academic achievement. Many colleges will also offer additional financial aid based on merit or need. Be sure to contact the school's financial aid office to see what other forms of aid may be available.

FEDERAL TAX CREDITS AVAILABLE

There are two federal tax credits available to help with paying for college expenses. The American Opportunity Tax Credit provides a tax credit of up to $2,500 per year per student. It is for qualified higher education expenses for students in their first four years of post-secondary schooling. However, there are income limits to be able to take advantage of this credit.

The Lifetime Learning credit allows for a tax credit of up to $2,000 per year per tax return. The credit is for qualified higher education expenses for students at any stage of their post-secondary education. Like the American Opportunity credit, there are income limits in order to use the credit.

Be sure to check the Internal Revenue Service's Publication 970, "Tax Benefits for Education," for more information on these tax credits, including current income limits.

STUDENT LOANS

Taking out a student loan is always an option. However, you've likely seen many news reports and articles about the loan debt that many students are accumulating to attend college. Here are some facts:

- 43.5 million borrowers with outstanding student loans
- Estimated $1.7 trillion in total student loan debt in the U.S.
- Student loan delinquency rate of 11% (default within the first year of repayment)
- Each borrower has an average of $37,787 in student loan debt

Student loan debt doesn't just affect recent graduates. It continues to significantly impact people's financial lives even into their older years.

Age Group	Amount Owed
24 and younger	$104 billion
25 to 34	$497 billion
35 to 49	$634 billion
50 to 61	$293 billion
62 and older	$107 billion

Source: www.credit.com (3/22/2023)

STUDENT LOAN REPAYMENT OPTIONS

If you find yourself struggling to make loan payments, temporary solutions include asking the lender for a suspension of payments for a specific period, a reduction in the amount of the payment for a time, or an extension of the time to repay. If there are multiple loans, consider either student loan refinancing or a loan consolidation.

REFINANCING

To pay for college, you may have used a mix of loans from private lenders and loans from the federal government. The interest rates, balances, and terms for each of those loans may vary. Some of your loans may have variable rates while others have fixed rates. Student loan refinancing, which can only be done with a private lender (including banks and credit unions) is designed to help you combine all your student loans — federal and private — into a single, more affordable loan. That new refinanced loan will have a brand-new interest rate which, if your credit is in good shape, could be lower and at a fixed rate. There are pros and cons to refinancing. For more details go to https://studentaid.gov/understand-aid/types/loans/federal-vs-private.

CONSOLIDATION

If you have federal loans and want to maintain the protection and other benefits that come with them, you have another option — student loan consolidation. Federal loan consolidation involves combining all your existing federal student loans into a single loan with the federal government. Unlike refinancing into a private loan, which allows you to refinance both federal and private loans, the federal government will only consolidate government loans. There's another key difference with consolidation: the interest rate, which will be a fixed rate, won't be lower. Rather, it'll be a weighted average of all the interest rates on your current federal loans rounded up to the nearest 1/8%. The U.S. Department of Education offers Direct Consolidation Loans, which require no application fee.

FEDERAL STUDENT LOAN REPAYMENT PLANS

- You can pick from repayment plans that determine your monthly payment based on your income or plans that give you a fixed monthly payment.
- Repayment plans based on your income are a smart choice to lower your payment. For example, payments on the Saving on a Valuable Education (SAVE) Plan are no more than 10% of your discretionary income. The lower your income — or the larger your family size — the less you'll pay each month.

FIXED PAYMENT REPAYMENT PLANS

The fixed payment repayment plans include the Standard Repayment Plan, the Graduated Repayment Plan, and the Extended Repayment Plan. These plans base your monthly payment amount on how much you owe, your interest rate, and a fixed repayment time period.

INCOME-DRIVEN REPAYMENT (IDR) PLANS

IDR plans base your monthly payment on how much money you make and your family size. There are four IDR plans: Saving on a Valuable Education (SAVE) Plan; Pay as you Earn (PAYE), Income-Base Repayment Plan (IBR); and Income-Contingent Repayment (ICR) Plan. Each of these has important differences such as term of the loan and percentage of your income your payment will be based on so analyze them carefully or consult your financial planner. Check out Repayment Plans | Federal Student Aid for more details.

Source: Citizen's Bank (https://www.citizensbank.com/learning/student-loan-consolidation-vs-refinancing.aspx).

STUDENT LOANS: A FINAL THOUGHT

For many individuals, borrowing for college is the only path to earning a degree that can spark a fulfilling career and possibly a lifetime of financial security. However, with all the talk of a student loan crisis, six-figure student loan debt, and unsustainable student borrowing, it's easy to wonder if borrowing for college is a good idea.

You owe it to yourself to do some in-depth research to see which careers offer you the most personal reward and long-term opportunities, then decide if taking on the amount of student debt you're considering is worth it. The federal government's Bureau of Labor Statistics publishes an annual Occupational Outlook Handbook that shows the median pay and projected demand for workers in almost any occupation over the next 10 years at various levels of education. Check out https://www.bls.gov/ooh/.

This information is not meant to be comprehensive. These programs are complex and include many different income restrictions. Consult with your financial advisor and tax professional for advice appropriate to your individual situation.

Bailey Wealth Services
A. Sean Bailey, CFP®
Wealth Advisor
1604 Hewitt Ave
Suite 704
Everett, 98201
(425)252-4032 Phone
sean.bailey@baileywealth.org
www.baileywealth.org

RP-874-1023 Tracking #502369 (Exp. 10/25)