Money Matters
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Question of the Month: What are the Top Five Myths of 529 Higher Education Savings Plans?

By Aaron Skloff

Q: What are the top five myths of 529 higher education savings plans?

The Problem – Understanding 529s
Like many sections of the Internal Revenue Code, section 529 involves more than meets the eye. Misunderstanding or underutilizing its capabilities can present problems or forego opportunities.

The Solution — Debunking Key 529 Myths
In debunking the top five 529 myths you will gain a clear understanding of how powerful the multi-purpose 529 can be.

Basics on 529
Based on The College Board 2011-12 report, a child born today can expect to pay over $267,000 for a four-year undergraduate education at a state institution and over $440,000 for a private institution. Congress established section 529 of the tax code so savings used for qualified higher education expenses at an accredited education institution would be free from taxes. These plans are often called 529s, 529 college plans or 529 higher education savings plans. The plans offer tremendous estate tax planning tax shelter benefits. With a 2013 federal estate tax exemption of $1 million (55% tax rate) and a N.J. state exemption of a mere $675,000 (16% top tax rate), the 529 can save you and your heirs millions in taxes.

1. **Money contributed to a 529 must be used for my children's college education. Myth.** The money can be used for any purpose for anyone. If it is not used by the beneficiary for higher education expenses, only the gains will be assessed a 10% penalty and taxed as income. The penalty and taxes may be worthwhile if you can defer taxes over many years, for example 20 or 150 years.
2. **Contributions are still limited to $12,000 per year. Myth.** The annual contribution for 2012 is $13,000. This limit is per contributor, per beneficiary. A married couple could contribute $26,000 each year to each of their four children's 529 plans. If the couple utilizes the accelerated gift method, they could contribute $130,000 every five years to each of four kids' 529 plans.
3. **Beneficiaries cannot be changed. Myth.** You can change the beneficiary at any time. To avoid federal income tax and a 10% federal tax penalty on earnings, the new beneficiary must be a member of the family of the previous beneficiary (i.e.: sibling, spouse, parent, etc.).
4. **Investments cannot be changed. Myth.** Changes can be made once every year. An often overlooked solution to this limit is the ability to change the investments when the beneficiary is changed. For example, if you make a change in February and want to make another change in April you could simply change the beneficiary on the account and the investment change limit is reset.
5. **There are no estate planning benefits. Myth.** 529s are one of the most powerful, lowest cost estate planning vehicles. Contributions made to a 529 are removed from your estate. Unlike most solutions that remove assets from estates and leave little control over investments and beneficiaries, the 529 allows owners to change investments and beneficiaries every year.

Because 529 owners can name a successor to the account when they pass away, a 529 can be used for multiple generations.

Just imagine a grandmother and grandfather who strongly believe in education. Each makes $65,000 contributions as follows: four children, 16 grandchildren, 64 great-grandchildren and even their gardener's three children. In total, they contribute over $5.6 million and instantly remove the same amount from their estate.

Action Step — Open 529s
Contributing to a 529 immediately stops the taxation of any profits if the money is used for higher education, provides a disciplined way to save for higher education and could be a powerful estate planning tool. Like most investments, the earlier you begin contributing the more wealth you can create in the end.

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