Building Your Child's College Savings Portfolio

[subhead] As college tuition continues to rise, planning your child's education today can save you from future financial anxiety

Here's an unsurprising statement – raising kids is really expensive. According to the most recent estimate, the cost to raise them to through the age of 17 (not including college expenses) is an estimated $233,610 for a child born in 2015, according to a report released by the Department of Agriculture.[1]

College education isn't far behind, with costs steadily rising. The College Board — a nonprofit educational association — reports that for 2017-2018, the average tuition, fees, room and board, books and supplies for a four-year private college is $46,950 per year ($20,770 for a public in-state institution).[2]

The good news is that there are steps you can take today to ensure that you're prepared to pay those expenses when the time comes. Understanding how to utilize the 529 college savings plan is a great starting point.

Named after Section 529 of the Internal Revenue Code, a 529 plan is a tax-advantaged way to save, or even pay in advance, for college expenses.

By establishing a 529 plan now you're not only taking advantage of potential end-of-year tax benefits, you're giving a child a helping hand toward the skyrocketing cost of higher education.

Understanding the Two 529 Varieties

A 529 comes in two varieties: a pre-paid plan and a savings plan. A pre-paid 529 plan allows the account holder to pre-pay all or part of the tuition and fees of an in-state college education. Pre-paid plans may also be converted for use at out-of-state colleges.

This 529 savings plan works similarly to a Roth IRA and offers investment options similar to mutual funds. Its value can rise and fall based on the performance of the investment option chosen.

Earnings in a 529 plan can be tax-deferred, with withdrawals being exempt from federal and state income taxes if you use the funds for qualified expenses such as tuition, fees, room and board and supplies. Many states also offer state tax deductions or tax credits on top of that.

Broad Flexibility

Another key benefit of 529 plans is their flexibility. Some investments that are used for education funding (such as a Coverdell ESA) require that the assets be given to the beneficiary when they reach a certain age. With a 529 plan, the owner of the account continues to make all of the decisions. For example, if the beneficiary decides not to go to college, you can choose a different beneficiary or use the plan for your own education needs.

529 savings can also be used for any accredited in-state, out-of-state or international educational institution. And while some education investment vehicles have age restrictions, a 529 plan has none, so anyone can benefit from one.

Additionally, you can usually cover full college costs because the contribution limits per beneficiary generally exceed $300,000. However, contribution limits vary by state.

Doing Even More with Your 529 Plan

With Congress recently passing the Tax Cuts and Jobs Act, 529 plan benefits have significantly been expanded to cover K-12 education expenses as well. Families will be able to withdraw up to $10,000 per year tax-free for elementary, high school or homeschool expenses. Previously, the only vehicle that offered tax-free savings for K-12 were Coverdell ESA's, but that financial tool is severely limited in comparison to a 529 plan.

It is advised that if you utilize a 529 plan to save for college and would like to also establish one for K-12 to consider opening separate accounts for each. This will help you keep better track of each goal, and select the appropriate investments based on your withdrawal schedule.

[1] Source: It Costs $233,610 to Raise a Child – CNN Money, http://money.cnn.com/2017/01/09/pf/cost-of-raising-a-child-2015/index.html

[2] Source: Trends in College Pricing – The College Board, https://trends.collegeboard.org/college-pricing