INVESTING IN POTENTIAL WITH A 529 SAVINGS PLAN

As tuition costs climb higher than ever, saving early for education opportunities is one of the most important decisions you can make.

RAYMOND JAMES®

Giving the gift of education – whether it's for a child, grandchild, family friend or even yourself – can have a lasting impact, perhaps for generations to come.

While covering the cost of tuition, fees, books, supplies and equipment can seem overwhelming, with consistent investing, sound financial advice and a 529 plan, funding higher education is an achievable goal. Plus, by working closely with your financial advisor, tapping into a 529's tax-free growth opportunities, estate planning incentives and state tax deductions is easier than ever.*

A new legacy of education begins with you. We're here to help you get started.

* Earnings in 529 plans are not subject to federal tax and in most cases state tax, as long as you use withdrawals for eligible college expenses, such as tuition and room and board. However, if you withdraw money from a 529 plan and do not use it on an eligible higher education expense, you generally will be subject to income tax and an additional 10% federal tax penalty on earnings. An investor should consider, before investing, whether the investor's or designated beneficiary's home state offers any state tax or other benefits that are only available for investments in such state's qualified tuition program.

For most parents, paying for their children's college education will be one of their greatest financial challenges. A 2016 Sallie Mae study, "How America Saves for College," revealed that 92% of parents believe college is an important investment in their child's future, but they find that saving for it can be challenging.

WHAT IS A 529 PLAN?

A 529 plan is a popular savings vehicle that can be established for anyone, but is most often used by parents and grandparents interested in providing education funding. In addition, a 529 can provide an easy wealth transfer and may work well for those wanting to reduce their estate.

529 plans generally offer a set of investment portfolios that are allocated among stocks, bonds, mutual funds, CDs and money market instruments. Typically, the program will offer at least one age-based or years-to-college portfolio and several static portfolios. This asset allocation will generally be more aggressive for younger beneficiaries and less aggressive for those nearing college age**. Many programs also offer individual fund portfolios.

Keep in mind that regulations allow no more than two investment strategy changes, which may include rebalancing on 529 plans each year. Therefore, some investors prefer plans that offer pre-constructed static or age-based portfolios. New contributions can always be directed as the owner wishes.

**Asset allocation does not guarantee a profit nor protect against loss.

ELIGIBLE EDUCATIONAL INSTITUTIONS

A 529 savings plan will pay for qualified expenses at any private or public college, university, or technical or vocational school in the country and abroad that qualifies for federal financial aid. You can look up eligible institutions by visiting the Department of Education website fafsa.ed.gov and clicking on "School Code Search."

QUALIFIED HIGHER EDUCATION EXPENSES

With limits set by the eligible educational institution in question, qualified expenses include tuition, fees, books, supplies, computers and equipment required for the enrollment or attendance of the beneficiary. Room and board is also often included if the student is enrolled at least half time – an allowance determined by the school in question.

FEES AND EXPENSES

Typically, 529s charge an enrollment fee, an annual fee or both. Also, most investments carry a load on the actual investment share. The program description will detail any other fees that may apply.

529s have gathered significant assets over the past few years, resulting in reduced expense ratios. All things being equal, a plan with lower fees and expenses should produce better returns over time***. However, actual performance is difficult to assess given the wide variations among plans. Your selection may be guided by the investments offered.

***There is no assurance that any investment strategy will be successful. Investing involves risk including the possible loss of principal.

THE BENEFITS OF 529s MAKE LIFE LESS TAXING

GIFT TAX AND ESTATE PLANNING BENEFITS

Contributions to a 529 are considered completed gifts for federal gift and estate tax purposes and may be excludable from your taxable estate. Most literature suggests a limit of $14,000 per year, the current federal gift tax exclusion limit. By staying under this limit, you do not tap into your gift and estate tax basic exclusion amount.

A unique feature of the 529 is a rule that allows for five years of contributions up front without gift-tax consequences. By filing IRS Form 709, up to $70,000 ($140,000 for married couples) can be contributed to a beneficiary in a single year without federal gift-tax consequences, provided you do not make any additional gifts to that beneficiary over a five-year period. The idea is that a large, early contribution has a chance for more tax-free growth than smaller contributions made annually.

Estate tax benefits can be significant. Once a 529 plan is funded, it is considered a completed gift to the beneficiary for federal estate tax purposes even though the owner has full control of the account. If opting for a five-year election, the contributor must outlive the election or it will be prorated back on a calendar year basis.

Before contributing to a 529, become familiar with your state's gift tax and inheritance tax rules. Contributions in excess of the amounts listed above can be made, but will incur gift taxation that is credited against a gift and estate tax basic exclusion amount ($5.45 million in 2016).

TAX-DEFERRED SAVINGS AND TAX-FREE WITHDRAWALS

All 529s provide tax-deferred savings and tax-free withdrawal of funds used for higher education. In essence, 529s are similar to Roth IRAs but have much higher contribution limits, no income limits and a low impact on financial aid eligibility. Like Roth IRAs, 529 savings plans allow for tax- and penalty-free withdrawals of principal at any time and for any purpose. The earnings

portion, however, must be spent toward qualified higher education expenses. Any leftover funds withdrawn will incur income tax and a 10% penalty.

POSSIBLE STATE TAX BENEFITS

Although the federal tax benefit is the same for all plans, state tax benefits vary. It's important to understand the tax deductions or tax credits that may be available to you – especially if you reside in a state with income tax.

States that offer a benefit tend to only do so for participants of the plan sponsored by their state, the in-state plan. However, some states allow a deduction for out-of-state plans. Your advisor can help you determine how much the deduction is worth.

In some cases, the state tax savings are relatively small, especially for large contribution amounts and for longer investment periods. In such cases, the significance of the tax consideration diminishes.

OWNERSHIP AND CONTRIBUTIONS

Each account has one account owner, a contributor and one named beneficiary. Although the beneficiary must always be a person, the owner may be an entity such as a trust, partnership or corporation. In most cases, the owner and the contributor are the same person.

Typically, the beneficiary is a child or grandchild, but can be an unrelated person – or the owner, contributor and beneficiary can all be the same person. The point of the legislation is to allow funds to be saved for educational purposes, not exclusively for traditional students.

Contributions may be made by the account owner or by another person; however, all contributions become the property of the account owner, and only the account owner can give instructions to distribute money from the account.

Many 529s allow for transfer of ownership, often with certain limitations. If a successor owner has been designated by the account owner prior to death or incapacitation, the successor owner takes on all of the rights of the original account owner.

CONTRIBUTING TO A 529 PLAN

Anyone can contribute to a 529 regardless of age or income. This includes an individual, corporation, partnership, trust, guardian, committee, trustee, executor, administrator or any person acting in a fiduciary capacity. Local governments and some nonprofit organizations may also participate.

CONTRIBUTION LIMITS

The maximum amount that can be contributed to a 529 account is established by the relevant state program's rules and may be changed each year to reflect the increasing costs of higher education. Once this limit – by contribution or appreciation – is reached, no additional contributions are permitted. Currently, the maximum in the marketplace is more than $500,000 and growing. Of course, there is no limit on the amount the account can grow.

Contributions and investment returns are not insured nor guaranteed by the FDIC, the plan provider, or any state or federal government agency.

CONTROL OF THE 529s ACCOUNT

A popular aspect of the 529 is that the owner controls the account and the money in it. While the contributions are considered a completed gift to the beneficiary, legal rights to the money usually stay with the owner indefinitely.

For example, grandparents can set up a 529 for each grandchild, reducing their estates while retaining control of the money. They can even take back the funds if they so choose, although they may trigger taxes and a 10% penalty on the earnings portion if the funds were used for something other than education. Nevertheless, 529 funds remain the owner's property.

BENEFICIARY AND OWNERSHIP DESIGNATION RULES

With discretion over the account beneficiary and control of the account, the owner determines who becomes the beneficiary and at what time, rather than the account transferring at a preset age or date. The owner can also change the account beneficiary at his or her discretion, an especially important feature when comparing a 529 to a UTMA/UGMA account.

If the new beneficiary is a family member from a younger generation than the original beneficiary, the original beneficiary may be subject to generation-skipping transfer taxes. If they are of the same generation, then there are no tax implications. The beneficiary also may be changed to a non-family member (although this would not be a tax-free transaction), or the owner could even opt to use the account for educational purposes for him or herself.

While not specifically designed for education funding, UGMA/UTMA Custodial Accounts allow you to transfer ownership of assets to your child and accumulate funds in your child's name.

529s AND FINANCIAL AID

The Free Application for Federal Student Aid (FAFSA) uses the Expected Family Contribution (EFC) formula to determine how much of a child's college expenses a family is expected to cover. The EFC formula assumes that a large percentage of family income is available to pay for college and considers only about 5% of a parent's savings and 20% of the child's assets in the equation.

A 529 is considered to be the parent's asset rather than the child's. Thus, it allows the child to receive more financial aid when using a 529 compared to some other savings vehicles. If the 529 is owned by a grandparent, none of the assets are included, as grandparents' assets are not considered in the formula (but the withdrawal from a grandparent-owned 529 may affect the formula). While some private schools use this formula when dispersing federal financial aid, they may have different guidelines when using their own financial aid pools.

Prepaid 529 plans allow contributors to purchase future tuition credits for in-state, public colleges at today's prices. These plans have limited transferability, and assets are generally used to pay only for tuition, not other expenses such as books or supplies.

COMPOUNDING AND CREDITOR PROTECTION

THE EFFECT OF COMPOUND INTEREST

Compounding has a dramatic effect on savings and investments. If in 10 years you'll need $100,000 for education, it's important to look at the effect compounding can have when you either earn or pay a 6% interest rate (for this example, disregard any tax implications).

By saving the money you could reach $100,000 by making monthly payments of $610.21 over 10 years, a total of $73,225.20. In contrast, if you borrow the funds you would make monthly payments of $1,110.21 for 10 years to pay off the loan – a total of $133,224.60. By planning ahead, you can tap into $60,000 in savings.*

PROTECTION FROM CREDITORS

Many 529s provide asset protection against creditors. Although the level varies among the plans, look for plans that explicitly offer statutory protection from creditors. State laws differ, so you should seek legal advice.

Federal bankruptcy law protects 529s that meet certain time requirements. Assets held in the account less than one year have no protection. Up to $5,000 of account assets held one to two years and the entire amount that has been held for more than two years are protected.

*Future interest rates are unknown and the assumptions above may not prove realistic. This is a hypothetical example for illustrative purposes only. It is not intended to reflect the actual performance of any security. Investments involve risk and you may incur a profit or a loss.

CONTRIBUTING TO OTHER PLANS SIMULTANEOUSLY

When contributing to a 529, contributions may be made to both an education savings account (ESA) and a 529 savings plan for the same beneficiary in the same tax year. Keep in mind that the total annual gift-tax exclusion applies.

You can also contribute to both a 529 savings plan and a 529 prepaid plan for the same beneficiary, however, you will need to pay attention to the gifting rules and the maximum contribution limits set by each state's 529 plan.

In contributing to both a savings and a prepaid plan, it holds true that a total of up to $70,000 ($140,000 for married couples) can be contributed for a beneficiary in a single year without federal gift-tax consequences, provided you do not make any additional gifts to that beneficiary over a five-year period.

Contributions in excess of these amounts can be made but will incur gift taxation, which is credited against an owner's gift and estate tax basic exclusion amount. When purchasing a plan in the same state, many 529 programs prohibit additional contributions once the account plus all other 529s for that beneficiary reach the program's maximum account limit. This means that if a beneficiary is named on one or more 529 savings plans and/or one or more 529 prepaid plans, no more contributions may be made to any of the accounts once the total balance of all accounts reaches the highest maximum account limit of any of the beneficiary's 529s.

A single contributor can give up to $70,000 within a five-year period

A couple contributing can give up to $140,000 in a five-year period

The current annual federal gift tax exclusion limit is … $14,000

Coverdell Education Savings Accounts (ESAs) are used for education expenses and can be funded in the same year as a 529 savings plan. Raymond James does not offer Coverdell accounts as a custodian, but is contracted to offer them through certain mutual fund companies.

529 savings plans can be a valuable tool for funding a college education – whether it's for a child, grandchild or even yourself.

Speak to your advisor to learn more about the tax-free growth opportunities, estate planning incentives and state tax deductions available to you through a 529.

Investors should consult a tax advisor about any state tax consequences of an investment in a 529 plan.

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