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Bush Makes Big Changes To College Savings Plans

By Carl Hampton

Saving money for our children's higher education is a little like walking through a mine field, which plan best suites our needs. President Bush has just signed the Pension Protection Act, the act outlines strengthening the financing rules for defined benefit plans. The main problem I found with this act is that the Pension Protection Act eliminates the 2010 sunset provision for tax-free withdrawals from the Section 529 tuition savings plan.

This plan was created in 1996 and it allows after-tax income (which means it will not be taxed there after) to be invested in state-sponsored plans and to grow free of federal and state taxes. Fortunately, the Economic Growth and Reconciliation Act of 2001 states that as long as the 529 money is used for college expenses that income earned can be withdrawn free of federal and state taxes. But the tax-free withdrawals are set to expire at the end of the year 2010. If and when that happens the distributions from the plan are taxable, albeit at the student rate.

Most experts are now saying that more 529 options only represent more ways to make the same mistake of investing in these plans. Your investments are locked into specific rules just for a tax benefit and the plan is completely lacking in flexibility. The Coverdell Education Savings Account is another alternative to Section 529. Both plans are similar in that they allow money to grow tax deferred. The Coverdell Education Savings Account may also be put towards primary and secondary education.

If your children qualify for financial aid and you want to use the 529 plans then put it in your name. You really don't want the plan to be considered your child's assets when financial aid calculates an aid package. For those high-income parents who probably won't qualify for financial aid, it would make sense to place the Section 529 under you child's name to take advantage of the lower tax rate.

Experts recommend purchasing a Series I United States savings bond with the child's name on it. It can be used for higher education and the interest income is exempt from federal income taxes. Another option for a high-income family is custodial accounts - Uniform Transfers to Minors Account (U.T.M.A.) or Uniform Gifts to Minors' Accounts (U.G.M.A.). These accounts are a way to shift assets to your children. You could also set up a complex trust which would include restrictions so that once the child turns 18 they would not be able to spend all the money on a car or sound system.

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College Savings Plans - are they the best choice for my child?

By Vanessa McHooley

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College Savings Plans, also called Section 529 plans, are one of the best ways to save for college because they offer:

- Tax advantages
- A variety of investment options
- Flexible contribution options
- Parental control
- Little impact on eligibility for need-based financial aid

Tax advantages

Investments in 529 plans are usually exempt from federal taxes. Earnings are tax-deferred and are not subject to capital gains taxes. Redemptions are also exempt from federal income tax if they are used to pay for tuition, room and board, fees, books, supplies, or equipment.

Most states also offer tax advantages, at least if you enroll in the plan for your own state. In addition, contributions may be deductible on your state income tax.

In addition to these income tax benefits, College Savings plans can be a valuable estate planning tool. The accelerated gift option allows you to average gifts over \$11,000 per beneficiary over a five year period with no federal gift tax. This means you can contribute up to \$55,000 per beneficiary in one year with no gift tax. Contributions are immediately removed from the donor's gross taxable estate (and included in the estate of the beneficiary).

Investment options

Most states offer three or more investment options ranging from conservative to aggressive. One is usually an age-based portfolio that invests mainly in stocks while a child is young, then shifts to bonds and money-market funds as college years come closer. 529 plans are managed by experienced investment companies, such as Vanguard, Fidelity, and TIAA-CREF.

Contribution options

Anyone can contribute money on behalf of a beneficiary, allowing friends and relatives to give the gift of education. In addition, the minimum investment amount required to open an account is usually lower than mutual funds require, making section 529 plans affordable for lower income families.

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States set their own contribution limits for college savings plans. Most states base their limit on an estimate of the amount of money needed for seven years of post-secondary education. Limits range from \$146,000 to \$305,000.

In addition, most states allow you to regularly transfer funds from your checking or savings account to your 529 plans. Some states even let you set up payroll deductions.

Parental control

The money in a College Savings Plan is controlled by the account owner, not the child. So if the child decides to not go to college, they do not have access to the funds. Instead, the account owner can get his or her money back (with income taxes and a 10% penalty owed on earnings) or transfer the funds to another family member.

Impact on eligibility for need-based financial aid

College savings plans have a low impact on financial aid eligibility because they are considered an asset of the account owner (usually the parent), rather than the student.

Choosing a plan

Most states have their own College Savings Plans, but you do not have to enroll in the plan in your state. Look first at the plans in your own state, especially if they offer tax advantages. Other factors to consider as you compare state plans are expenses and investing options.

Prepaid tuition plans

Another type of Section 529 plan are the prepaid tuition plans. Prepaid tuition plans are guaranteed to increase in value at the same rate as college tuition. So, if you purchase shares worth one semester of tuition at a state college, those shares will always be worth one semester of tuition, even 10 years later when tuition rates have doubled. These plans offer basically the same tax and contribution benefits as College Saving plans, and they are guaranteed by the government. However, because prepaid tuition plans are considered a resource, they reduce need-based financial aid dollar for dollar. Therefore, families that expect to qualify for need-based financial aid should avoid prepaid tuition plans and invest in college savings plans instead. Another alternative is to roll prepaid tuition plan funds over into the state's 529 college savings plan before college begins.

There are many advantages to college savings plans; however, there are many ways a parent can help a student pay for a college education. Make sure to research as many avenues as possible to make the most informed decision on how to pay for school, and you could end up with the optimal college funding solution.

This article is distributed by NextStudent. At NextStudent, we believe that getting an education is the best investment you can make, and we're dedicated to helping you pursue your education dreams by making college funding as easy as possible. We invite you to learn more about how to get College Savings Plans at <http://www.NextStudent.com> .

My goal is to help every student succeed – education is one of the most important things a person can have, so I have made it my personal mission to help every student pay for their education. Aside from that, I am just a pretty average girl from SD.



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