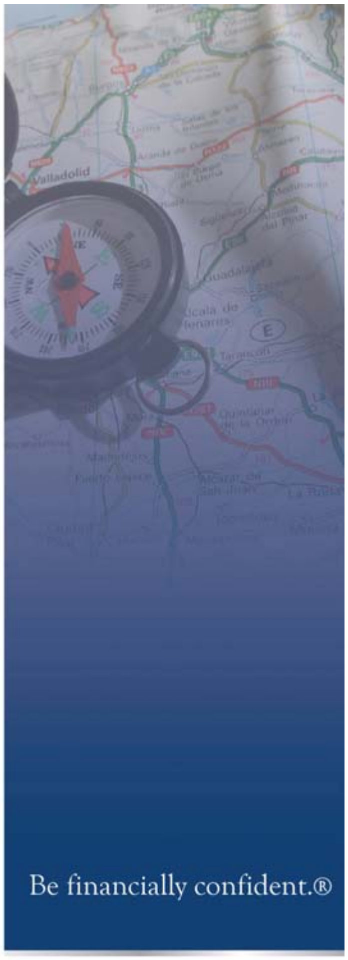
529 Plans: The Estate Planning Triple Play

by Clarissa R. Hobson, CFP®



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Much has been made of the ability to use 529 plans to implement effective estate planning strategies. First, it is important to understand that there are two types of 529 plans; prepaid tuition plans[i], and the more popular college savings plans, in which plan contributions are invested and grow to pay for a variety of future qualified college expenses. All states offer one or both of these plan types, and the account owner selects which state's 529 plan to use. This article will specifically focus on the benefits of 529 college savings plans.

There many tax and other benefits associated with 529 college savings plans. Contributions to these plans, though not federal income-tax deductible, grow tax-deferred, and qualified distributions for a beneficiary's college costs are withdrawn tax-free. In addition to the federal income tax benefits, many states offer additional tax benefits such as an up-front state income tax deduction on contributions or an income exemption on withdrawals. In general, contributions to plans sponsored by one's home state may offer more tax benefits than contributing to a plan offered by another state.

One of the primary estate planning benefits of 529 plans is the ability of the account owner to remove assets from their gross taxable estate while still retaining control of the assets. There is no other estate planning vehicle that allows for this type of flexibility**.** What this means is that the account owner can change designated beneficiaries and asset allocations, and can even reclaim the assets in the account for any time or any reason.

Married couples can contribute up to $26,000 per beneficiary per year in 2010 ($13,000 for individuals) without incurring gift tax consequences, and if desired, 5 years of contributions can be accelerated into a single year for a contribution of $130,000 ($65,000 for individuals). This may be desirable if the donor is interested in removing significant assets from an estate all at one time and may be implemented for an unlimited number of beneficiaries.   Contributions that qualify for the gift tax exclusion also qualify for the generation-skipping transfer tax exclusion. As an additional benefit, if a grand parent is the account owner for a grandchild's 529 plan, the assets in the account may not impact the grandchild's eligibility for financial aid.

As demonstrated in below, a married couple could remove $1,560,000 from their taxable estate over the course of ten years without any gift or generation-skipping transfer tax consequences:

	2010	2015	2020
Beneficiary 1	$130,000	$130,000	$130,000
Beneficiary 2	$130,000	$130,000	$130,000
Beneficiary 3	$130,000	$130,000	$130,000
Beneficiary 4	$130,000	$130,000	$130,000
Total Assets Removed from Estate	**$520,000**	**$1,040,000**	**$1,560,000**

In summary, 529 plans offer three key estate planning benefits: the ability to remove assets from the taxable estate, the opportunity to retain control of those assets, and the avoidance of gift and generation-skipping transfer taxes if contributions are kept within gift tax exclusion limits. Contributing to 529 plans provides for your beneficiaries' future education needs in a tax-advantaged manner while simultaneously improving your estate plan and tax circumstances!

Benefits specific to Colorado's 529 College Savings and Prepaid Tuition Plans: Contributions are allowed for each beneficiary up to $280,000 and are fully deductible in computing Colorado taxable income; qualified distributions are exempted from state income taxation. Colorado also provides protection from creditors' claims.

About The Author

Clarissa Hobson, CFP®, *has assisted clients in meeting their financial planning needs for a decade now. Prior to joining our firm, Clarissa served as the national Education Trainer for the Principal Financial Group, where she trained the firm's financial planning employees. She was initially employed by the Principal in 2006 as a Senior Employee Benefits Specialist, and during that time worked with the firm's clients to achieve their financial, investment and retirement goals. Before coming to the Principal, Clarissa was a member of the retirement services group at AmSouth Bank, where she served as a Senior Education Specialist and Trust Officer. She specialized in educating employees on how to meet their financial goals in retirement. Clarissa is a 2001 Magna Cum Laude graduate of the University of the South in Sewanee, TN.*

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