Never Too Affluent for 529 Plans: 529 Gifting and Estate Planning Strategies

Have you ruled out 529 plans because you expect to pay for college from current income?

Are you concerned with reducing estate taxes?

Are you seeking a way to make substantial tax-free gifts?

Would you like a simple way to leave a significant legacy for grandchildren?

A valuable resource — no matter what your net worth or income

If you have a high annual income or net worth, you may believe that 529 college savings plans are off limits to you, or — at the very least — they would offer you no or little benefit. You may be surprised to learn that, beyond being an education savings vehicle, a 529 plan can be a tool you can use to help reduce your estate taxes.[1] And while there are limits on how much you can give, there are even accelerated gifting provisions with a 529 plan that provide additional tax planning flexibility.

The potential benefits of a 529 plan

Establishing a 529 plan for your children or grandchildren may allow you to benefit from:

- Tax-free distributions for higher-education purposes
- Tax-free accumulation of income and capital gains — with no "kiddie taxes" that can complicate Uniform Transfers to Minors Act (UTMA) and Uniform Gifts to Minors Act (UGMA) approaches
- The ability to make contributions exceeding the annual gift exclusion in a single year without triggering gift taxes
- Uninterrupted control of your gift and plan assets — also unlike UTMA and UGMA accounts
- The exclusion of assets from your estate, lowering potential estate tax liability

Your financial advisor: Helping you make an informed decision

As you consider establishing a 529 plan, your financial advisor can help you consider several questions and possible issues:

- **What kind of tax benefits can you expect?** Contributions to a 529 plan are made with post-tax dollars, so there are no immediate tax benefits to establishing one. But the long-term tax benefits can be substantial. Earnings accumulate tax-deferred and distributions are tax-free if used for appropriate education expenses, such as tuition, room and board, books, and required supplies and equipment. (Distributions used for any other purpose may be subject to ordinary income taxes and an additional 10% penalty.)
- **Should you take advantage of special gifting flexibility?** 529 plans have a unique accelerated gifting rule that allows you to give up to five times the annual gift tax exclusion amount without incurring federal gift tax. To do so, you must elect to treat the contribution as five pro rata gifts over a five-year period by filing gift tax Form 709. That may allow you to contribute up to $65,000 in a single year ($13,000 x 5) and twice that amount for a couple. Be sure to consult with a qualified tax professional before electing this strategy. Accelerated

(continued)

[1] While federal gift tax still applies for 2010, as the law currently stands, estate and generation-skipping transfer taxes are repealed for 2010. They are scheduled to be reinstated on January 1, 2011, with a $1 million exemption and a 55% tax rate, unless the president enacts new legislation with alternative provisions.

gifting also removes the future growth from estate tax. If a donor elects to treat a donation as five separate, equal gifts to avoid gift tax, then the donation will be excludable from his or her estate on a pro rata basis. To fully avoid estate tax, the donor must survive to January 1 of the fifth calendar year.

- **Do you want to retain control of assets in the plan?**
  As donor, you can retain control of the assets in the 529 plan — unlike with an UGMA or UTMA account, where you must eventually turn over control to the beneficiary. You can also:
  - Change beneficiaries within the family (to a qualified family member) and still preserve tax benefits.
  - Change the beneficiary to future heirs and still avoid gift tax by managing the gift process.
  - Name a successor owner who will assume control of the account upon your death while avoiding probate.
- **Does the plan offer estate tax advantages?**
  Even though you retain control of the 529 plan, assets are excluded from your taxable estate (subject to certain time restrictions related to the accelerated gifting options).

A checklist

Your financial advisor can help you review your goals and discuss how a 529 plan may not only help your family cover college education expenses, but also serve as a potential estate planning tool. So, before you meet with your financial advisor, you should review some important information and documents:

- ☐ Your children's education plans
- ☐ Estate and/or legacy planning documents you've developed with your tax and/or legal advisor
- ☐ Your Expected Family Contribution toward college costs as determined by your Free Application for Federal Student Aid

Next steps

After reviewing your situation and goals, your financial advisor will be better able to explain the potential financial and estate planning benefits of establishing a 529 plan. Then, if you decide to move forward, you and your advisor can discuss the details of establishing the plan and selecting the investments.

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