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Trusts & Estates Law Alert

Grandparents, Moms and Dads
Tax Relief for College Savings
529 Plan

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Is there someone in your life who will be going to a college or university for an undergraduate or graduate degree? Could it be your grandchild? Your child? Your niece or nephew? Yourself? Are you looking for ways to help your family while getting a tax break? If so, read on.

The news media is full of warnings that college tuition is rapidly rising. Many parents have had to dip into retirement savings to fund their child's college education. Currently, the average cost of a private college in the metro Washington, D.C. area is approximately $26,000 per year. This is a conservative figure as many of the top colleges are already charging $35,000 plus per year.

BENEFITS

If you are one of those people named above, the 529 Plan may be for you. The 529 Plan is a state-approved investment plan, to help individuals and their families save for future college expenses, including room and board, books, fees, supplies and equipment. Amounts saved in a 529 Plan may be used at any accredited college or university in the United States and even some foreign institutions.

Generally, everyone is eligible to participate since there are no income limitations. Amounts that individuals may deposit are substantial—many state plans permit over $200,000 per beneficiary and there are no rules against participating in several plans at once. Best of all, beneficiaries may be changed if a beneficiary does not attend college.

The investment in a 529 Plan grows tax-free and distributions from it are tax-free federally if they are used to pay qualified higher education expenses for distributions in years 2002 to 2010.

If Congress does not extend the tax break, the earnings portion of distributions will be taxable to the beneficiary after 2010.

Some states offer a deduction for state income tax purposes for contributions while others offer an income exemption upon withdrawal.

TAX RAMIFICATIONS

For individuals who are concerned with estate taxes, any amounts contributed to a plan are removed from the donor's estate. Up to $11,000 ($22,000 per couple), otherwise known as the annual exclusion amount, may be transferred per person without a gift tax consequence. Also, an individual may transfer up to $55,000 (five times the current year's annual exclusion amount) in one year and elect to treat the contribution as made over five calendar years, providing the donor survives the five years. This allows not only the $55,000, but the growth on it, to be excluded from the individual's estate sooner. As long as the contributed amount is within the annual exclusion amount, the transfer is not subject to the generation-skipping tax.

In the past, in order to qualify for the annual exclusion, a gift had to be a "completed" gift—the donor relinquished all control over the funds. With a 529 Plan, however, the donor maintains control over a 529 Plan account. The donor decides when to withdraw and for what purpose. He or she may change a beneficiary or revoke the gift and have it revert to himself or herself. If the gift is revoked and returned to the donor, however, the amount is considered part of his or her estate again.

CONCLUSION

In addition to the 529 Plan, there are several other ways to plan for educational expenses. A member of our estate planning team would be happy to discuss them as well as any other estate planning questions that you may have.

Do you know of others who should receive the Trusts & Estates Law Alert? If so, please complete the form below and fax to: 202-457-1678, attn: Candace Brosowsky, or visit our on-line library at www.jackscamp.com.

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