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Funding College: 529 Plans vs. Alternatives

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529 plans can be a great way to save for college, but what are your other options?

By Jason Fannon

529 plans are a great way to save for college. On average, students are shelling out more than $11,600 per year to attend public, in-state institutions, according to a recent report from Bankrate. For students attending school out of state, that cost skyrockets to more than $30,700 per year. While savings programs like 529 plans can provide tax advantages and benefits, they are state specific. They can also come with various fees and strict rules when it comes to using the funds. Therefore, it’s important to understand all of your options to find the best financial fit for you or your college student.

The Limitations of a 529 Plan

Not all 529 plans look the same. These accounts are usually sponsored by the state and may come with different tax advantages or a lack thereof. For example, in Michigan, contributions made to the Michigan Education Savings Program are eligible for state income tax deductions. Contribution limits are $5,000 for individual filers and $10,000 for joint filers.

Aside from taxes, it’s also important to note that opening and maintaining these accounts may come with a fee. Some plans may charge an enrollment fee, an annual maintenance fee, or an administration fee to manage the account. These costs vary by state and plan. So don’t be afraid to shop around, or work with a financial adviser.

It’s also important to note that the money contributed to a 529 plan must be used for qualified educational expenses. Therefore, if your child decides not to attend college, or their tuition is fully covered by the institution due to household income or scholarships, it may become more difficult to utilize these funds. Qualified expenses include tuition and fees, room and board, textbooks and other education materials. If these funds are used for unrelated expenses, you could face a penalty.

A 529 plan can also count against you when it comes to receiving federal aid. The funds in these accounts are factored into the calculations that determine how much aid you qualify for. The impact it could have on the amount of aid you receive depends on who owns the 529 plan account.

Alternative Funding Options

Various tax advantages are one of the attractive features of a 529 plan, but this isn’t the only option with tax benefits.

Custodial Accounts

Custodial accounts, such as UGMA or UTMAs, are used to financially benefit a minor. These accounts must be managed by an adult until the child is no longer considered a minor, which differs by state. A custodial account can provide various tax benefits for the minor and the funds don’t have to be used for educational purposes. There are also more investment options with these accounts and the account fees may be lower.

For families looking for more flexibility, a Coverdell Education Savings Account might be a good fit. This account allows you to contribute up to $2,000 per child each year. These funds can be used to cover elementary and secondary education expenses. They also offer more investment options for account holders.

Grants

Grants are another great option for funding college. Grants such as Pell Grants, Federal Supplemental Educational Opportunity Grants and Teacher Education Assistance for College and Higher Education Grants are available at the federal level. These grants have different eligibility rules and requirements but are worth checking into.

Scholarships

Scholarships are another great way to pay for college. These may be offered through your state, your county, your prospective college and more. There are academic and athletic scholarships available and some may also have low-income eligibility. Be sure to do your research to see what you qualify for.

Federal Work-Study

The Federal Work-Study program is also an option. Through this program, you can earn money to pay for school by working part-time. You’ll earn the federal minimum wage and your total award amount will depend on when you apply, your financial need and your school’s funding level.

The price tag of a college degree isn’t cheap, but there are resources out there to help ease the financial burden. Research grant and scholarship opportunities you may qualify for and check into various savings and investing programs to find the right match. You can also compare in-state tuition versus out-of-state tuition, or consider trade and community college programs to help lower costs, especially if your child is still figuring out their path. If you’re concerned about the cost of tuition, consider working with a financial adviser who can help you review your options and make a choice that is best for you and your student.

About the author: Jason Fannon

Jason Fannon is the newest partner to the CFS team, but brings 24 years of season experience in the financial services industry. Previously, Jason served as a senior financial consultant at Charles Schwab, where he oversaw operations responsible for managing over $1 billion in client assets. Jason is an honors graduate of Arizona State University (BS Management/Real Estate), received his MBA in Management from Wayne State University and is an accredited CFP® practitioner (certified through Florida State University). He has been licensed in the securities industry for more than two decades and currently holds his Series 7, 63, 65 and 66 registrations.