



PENSINGER
FINANCIAL, INC.

529 Plan: Questions and Answers

There are two types of 529 plans: 1) college savings plan and 2) pre-paid tuition plan. We strongly prefer the college savings plan over the pre-paid tuition plans, therefore this document focuses on the college savings plan.

Q. What is a 529 plan?

A 529 plan is a qualified tuition plan operated by a state or educational institution. It offers you tax advantages when saving for college and other post-secondary training for a designated beneficiary, such as a child or grandchild. They have been around since 1996.

Q. What is the main advantage of a 529 plan?

529 plan distributions (a distribution is when you take money out of the plan) are tax-free as long as they are used to pay qualified higher education expenses for the designated beneficiary*.

Qualified expenses include: tuition & fees, books, supplies, room & board (for at least half-time students), and possibly computer related equipment & software and Internet access if used for educational purposes.

Higher education is defined by the IRS as any college, university, vocational school, or other postsecondary educational institution eligible to participate in the student aid programs administered by the U.S. Department of Education. It includes virtually all accredited, public, nonprofit, and proprietary (privately owned profit-making) postsecondary institutions. The educational institution should be able to tell you if it is an eligible educational institution.

*Non-qualified education expenses will result in your paying taxes on earnings (but not on contributions as they were made with after tax dollars) and an additional 10% federal tax. Also any amount of deduction previously taken for Illinois income tax purposes is subject to recapture.

Q. As far as Illinois Plans go I've seen Bright Start and Bright Directions, what is the difference?

Bright Start is a direct sold 529 plan by the State of Illinois. Bright Directions is a third-party advisor sold plan, this means Bright Directions acts as a middle man between you and the State of Illinois; therefore you will pay a higher overall fee for a Bright Directions 529 plan because you are also paying an advisor's commission. Bright Start offers better and lower cost investment options compared to Bright Directions, therefore we steer our clients to the Bright Start 529 Plans. However, we can set up either plan for you.

Q. Are contributions to a 529 plan tax deductible?

No, contributions to 529 plans are not tax deductible.

Q. Can anyone set up a 529 plan?

Yes. You can set one up and name anyone as a beneficiary — a relative, a friend, even yourself. The plan owner, called the custodian, controls the funds until withdrawal; the beneficiary does not control the account. There are no income restrictions on either you, as the contributor, or the beneficiary. There is also no limit to the number of plans you may set up. Keep in mind you can only have one plan per beneficiary, in other words, you cannot have one plan and list your two kids as 50 / 50 beneficiaries.

However, you can change the beneficiary of a plan if the new beneficiary is in the same family. For example, you can have one 529 plan with your oldest child named as the

beneficiary then when he finishes college you can name your next oldest child as the beneficiary of that same plan.

Q. Are there contribution limits?

Yes. Contributions cannot exceed the amount necessary to provide for the qualified education expenses of the beneficiary, generally not more \$350,000 can be contributed to a 529 plan. If you contribute to a 529 plan, however, be aware that there may be gift tax consequences if your contributions, plus any other gifts, to a particular beneficiary exceed the gift tax exclusion amount during the year.

As of 2016 one can give \$14,000 per student per year (or a married couple can give \$28,000). Also, 529 plans allow for a once per 5 year lump sum contribution where by a person can contribute \$70,000 (\$14,000 limit * 5) or (\$140,000 for a married couple) without incurring a gift tax.

Q. Can anyone contribute to my 529 plan?

Yes, anyone can make contributions to your 529 plan; a 529 plan in your name does not mean only you can contribute to it. This is great for grandparents who want to give money to a young child other than directly giving cash to that child for example.

Q. Am I restricted to my own state's 529 plans?

No. You are not limited to your state's plan, you can choose any state's plan. Keep in mind, your home state may offer special tax advantages when choosing your state's plan*. Your child does not have to attend a school in your plan's home state. For example, if you choose Florida's plan your child does not have to go to school in Florida in order for you to use the funds, you will still be able to use the funds to pay for qualified higher education expenses.

*If you live in Illinois and use the Illinois Bright Start College Savings Plan – your contributions are state tax deductible up to \$10,000 per parent, per year (\$20,000 for a married couple).

Q. Who controls the funds in a 529 plan?

The custodian of the 529 plan controls the funds. The custodian is the person responsible for the plan (typically the parent). Note: your financial advisor is not the custodian of your plan. Also, the custodian controls the funds until they are withdrawn.

Q. Does owning a 529 plan affect financial aid, scholarships, or government tax credits (such as American Opportunity, Hope, or Lifetime Learning Credit)?

No, it does not. And actually if the parent is the account owner, the 529 plan is factored less heavily into the financial aid calculation than if it was in the student's name. Also, grandparent owned 529 plan assets are not considered in the financial aid calculation formula.

Q. Each 529 plan account has one designated beneficiary. What does that mean?

A designated beneficiary is usually the student or future student for whom the plan is intended to provide benefits. Only one beneficiary is allowed per plan. Again, the owner / custodian of the plan is allowed to be the beneficiary of the plan, too.

Q. Can I change the beneficiary of a 529 plan I have set up?

Yes. There are no tax consequences if you change the designated beneficiary to another member of your family. Also, any funds distributed from a 529 plan are not taxable if rolled over to another plan for the benefit of the same beneficiary or for the benefit of a member of the beneficiary's family. For example, you can roll funds from the 529 plan for one of your children into a sibling's plan without penalty. You are only allowed to change the plan's beneficiary once per calendar year.

Q. What is an eligible educational institution?

An eligible educational institution is any institution defined as offering a higher education. The definition of higher education was discussed in the above question "What is the main advantage of a 529 plan?"

Q. What investment options are available?

Fortunately, 529 plans offer plenty of sensible and low-cost investment options including stocks and bonds. You are only allowed to change your investment allocation once per year.

As with any investment you are at risk to lose some or all of your investment.

Q. How do I fund the plan and make additional contributions?

Many methods are available to initially and continually fund the plan. You can write a check, do an electronic transfer from your bank account, set up an automatic investment plan, set up a payroll deduction plan, or rollover an existing qualified education savings plan (like another 529, a Coverdell Education Savings Account, or U.S. Series EE education savings bonds).

Q. Is setting up a 529 plan for my child right for me?

Only you can figure that out, but we'll help you get to the point. 529 plans are not for everyone, and are also not the only option available for paying for college. Setting up a 529 plan is an investment decision, which means both the benefits and drawbacks must be considered, along with alternative ways of accomplishing funding college.