

529 plans

An education-savings vehicle with multiple benefits

The first-year college tuition bill in 2021 is projected to be \$33,766* for an in-state average public education institution and \$67,197* for an average private institution.

Building the assets you'll need to fund a child's or grandchild's education is a challenge, but you may be able to meet it by contributing to a 529 plan.

529 plans were made possible by federal legislation but are implemented at the state or institution level. Nearly all states have approved and adopted these qualified tuition-assistance programs. Most states let nonresidents participate in their plans, although the tax benefits may be greater for residents than for nonresidents.

Under current legislation you may contribute to both a Coverdell Education Savings Account (ESA) and a 529 plan in the same year for the same beneficiary through the end of 2012.

The beneficiary can use 529 plan account balances at any participating accredited postsecondary school in the United States or certain schools abroad for tuition, room and board, books, equipment, and supplies. You (the owner) retain control of the assets and can change beneficiaries within the designated beneficiary's family at any time without penalty. Other key advantages of these plans are:

- **Federal-income-tax-free qualified distributions.** The beneficiary may be able to take qualified distributions federal-income-tax-free.
- **No income limitations for participation.** There is no income limit for contributing to a 529 plan, which is a benefit for higher-income families.
- **Substantial contribution amounts.** Contribution limits are significantly higher than those allowed for an ESA (see next bullet point). Maximum account balance limits vary from state to state.
- **Significant estate-planning benefits.** A single person can contribute up to \$65,000 in one year per beneficiary; a married couple can contribute up to \$130,000 in one year per beneficiary with no gift-tax consequences. Such a contribution will be considered a five-year accelerated annual-exclusion gift, so no additional gifts can be made for that beneficiary for the next four years without incurring gift-tax implications unless the annual gift exclusion increases. The gift amount and subsequent appreciation, however, are removed from your taxable estate. (A portion of the contribution amount may be included in the donor's taxable-estate calculation if the donor should die within the five-year period.)

*Total yearly costs for in-state tuition, fees, books, room and board, transportation, and miscellaneous expenses. Base is 2010-2011 school year. Costs for 2021 projected by Wells Fargo Advisors in October 2010 assuming a 5.2% increase per year. Source: Trends in College Pricing. ©2010 collegeboard.com, Inc. Reprinted with permission. collegeboard.com. All rights reserved.

-
- **No burden of investment decisions.** The plan's chosen investment manager will be responsible for portfolio management of all contributions. Initially, some plans may let you select from several asset-allocation-model alternatives, which generally you may change once every calendar year and/or with a beneficiary change.

An investment in a 529 plan will fluctuate such that the shares when redeemed may be worth more or less than the original investment. There are no guarantees that an investment in a 529 plan will cover higher-education expenses. Investors should consult the plan's offering document for the fees and expenses associated with that plan. You should consider a 529 plan's investment objectives, risks, charges and expenses carefully before investing. The plan's official statement, which contains this and other important information, should be read carefully before investing.

Frequently asked questions

How will my contributions be invested?

Typically your contribution is invested in a predetermined portfolio of stocks, bonds and cash. These portfolios are managed by the plan's chosen investment firm. In general, owners designate a certain allocation model at the time of the original contribution and can change this investment model once every calendar year and/or when they change the beneficiary.

What happens if the account balance is not used for qualified higher-education expenses?

Every withdrawal from a 529 plan is separated into two components: an "earnings" portion and a "return of your investment" portion.

The return of your investment in the 529 plan is never subject to federal income tax. On the other hand, if a withdrawal is not used for qualified higher-education expenses, the earnings portion of the withdrawal is subject to income tax and potentially a 10% IRS penalty.

If the beneficiary dies, becomes disabled or receives a tax-free scholarship, you may take penalty-free nonqualified distributions from the 529 balance within that same calendar year.

Can I change the beneficiary after I've made a contribution?

You may change your 529 savings plan account beneficiary to another qualified family member of the designated beneficiary without triggering a penalty. A qualified family member generally includes siblings, descendants, ancestors, aunts, uncles and first cousins. If you change the beneficiary to a descendant of the designated beneficiary, you will trigger a gift equal to the value transferred from the 529 account. If the value is more than the annual exclusion (or five-year accelerated annual exclusion), you must report it as a "taxable gift."

How will 529 plan investment balances affect eligibility for financial aid?

Assets in a 529 account may limit federal financial aid eligibility as follows:

- If a parent owns the 529 account, up to 5.64% of the value is included in Expected Family Contribution (EFC) as a parental asset. Any 529 accounts owned by a dependent student or by a custodian for the student are reported on the Free Application for Federal Student Aid (FAFSA) as a parental asset. Any qualified withdrawals from these accounts are not included as income to the student.
- If a 529 account is owned by a grandparent (or someone other than a parent or the student), the account's value is not reportable as an asset on the FAFSA financial aid application. However, any distributions from these third-party accounts are considered financial support to the student and are reportable on the following year's FAFSA as student income. Student income is assessed at the student's 50% rate.

The above information pertains to the federal FAFSA calculation. Some schools may use an institutional formula, which may assess assets differently and produce a different aid determination.

How does a 529 plan compare with more traditional college-savings vehicles, such as custodial accounts, ESAs, etc.?

The table on page 4 briefly describes the features of various college-savings vehicles. For a more complete discussion and comparison of these types of vehicles, ask your Financial Advisor for a copy of our education-planning brochure.

Can I transfer existing Uniform Gift to Minors Act/Uniform Transfer to Minors Act (UGMA/UTMA) balances into a 529 plan?

Yes, but 529 plan contributions must be made in cash, so if you choose to use UGMA/UTMA funds, your UGMA/UTMA assets must be liquidated (possibly triggering tax consequences) before making your 529 contribution.

You should be aware that you are not allowed to change the beneficiary on these accounts. The UGMA/UTMA assets you transfer into the 529 plan will continue to be governed by the control rules involving UGMA/UTMA assets. That is, the beneficiary may gain control of those assets when attaining the age upon which custodianship ends.

You should also be aware that assets in a non-529 plan custodial account can be used for a variety of purposes without penalty. Nonqualified withdrawals (those not used to pay higher education expenses) from a 529 plan may trigger ordinary income taxes and a 10% penalty.

A better strategy may be to maintain your UGMA/UTMA assets and direct new education savings into a 529 plan.

Can I make a gift to a custodial account and a 529 plan in the same year?

Yes, within certain limitations. A gift to a custodial account is limited to the annual gift-exclusion amount (\$13,000 for individuals, \$26,000 for married couples) without affecting your lifetime gift-tax-exclusion amount (\$5 million in 2011). However, a gift to a 529 plan that is in excess of the annual gift-exclusion amount may be considered a five-year accelerated annual-exclusion gift if properly elected as such on a gift tax return.

Comparing education savings vehicles

	529 plan	Custodial account (UGMA/UTMA)	Coverdell Education Savings Account (ESA)	Parent's taxable account
Ownership/control of account	Participant (owner).	Custodian controls for the minor until termination age.	Generally, parent or guardian controls for the beneficiary.	Registered owner.
Guidelines for use	Qualified higher-education expenses at accredited post-secondary schools anywhere in the United States and certain schools abroad.	If used before the age of termination, must be used for the minor's benefit. No restrictions on use when under the beneficiary's control.	Must use for qualified elementary-, secondary- or higher-education expenses before the beneficiary turns 30. Can also be used for tutoring, computer equipment, room and board, uniforms, and extended-day program costs.*	None.
Adjusted gross income (AGI) limit	None.	None.	Single filers: \$95,000-\$110,000 Joint filers: \$190,000-\$220,000*	None.
Annual contribution limit	\$13,000 contribution per donor, per beneficiary. Can elect a five-year lump-sum gift of \$65,000 per donor, per beneficiary. Lifetime contribution cap of the plan applies. Amount varies by state.	\$13,000 contribution per donor, per beneficiary to a child's UGMA/UTMA account without being subject to federal gift-tax treatment.	\$2,000* per designated beneficiary under age 18.* Contributions to the same account can be made by any taxpayer who meets AGI limits, subject to the annual overall limitation.	None.
Taxation of earnings	Qualified distributions may be federal-income-tax-free. State tax treatment may vary.	If child is under age 19, or for a full-time student under age 24 (in 2011), the "kiddie tax" applies: First \$950 of investment earnings is exempt from federal income tax if child has no earned income. Second \$950 taxed at the child's rate if child has no earned income. Above \$1,900 taxed at parent's highest marginal rate.†	Qualified distributions may be free from federal income tax. State treatment may vary.	Earnings taxed in the year realized.
Taxation/penalty upon early withdrawal	Earnings portion of nonqualified withdrawals taxed as ordinary income and subject to a 10% penalty (earnings only). Penalty-free nonqualified withdrawals permitted in the event of tax-free scholarship or death/disability of the beneficiary.	N/A	Income tax plus 10% penalty on earnings portion that exceeds or is not used for qualified education expenses. Penalty-free nonqualified withdrawals permitted in the event of tax-free scholarship or death/disability of the beneficiary.	N/A
Change of beneficiary	Can transfer account to benefit a qualified member of the designated beneficiary's family (including cousins) penalty-free. (Gift-tax consequences may apply if changing to a lower-generation beneficiary.)	Not permitted. Contributions are irrevocable gifts to the child.	Can transfer account to benefit a qualified member of the designated beneficiary's family (including cousins) penalty-free. (Gift tax consequences may apply if changing to a lower-generation beneficiary.)	N/A

*Subject to the sunset provision in the Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001. These temporary changes were extended through the end of 2012 with the enactment of the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010.

†This assumes the child has unearned income only.

College savings plans offered by each state differ significantly in features and benefits. The optimal plan for each investor depends on his or her individual objectives and circumstances. In comparing plans, each investor should consider each plan's investment alternatives, fees and state tax implications.

You can count on us

529 plans can help parents, grandparents, aunts and uncles, and others provide significant benefits to their beneficiaries to help secure the type of education they deserve.

There are many 529 plan choices, and your Financial Advisor can help you choose the one that best fits your needs.

Whether college is years away or right around the corner, put time on your side. Discuss college-funding alternatives with your Financial Advisor today.

For example, if you made a \$35,000 contribution in one year to a 529 savings plan and elected the five-year accelerated annual exclusion gift on the gift tax return, your contribution would be treated as a \$7,000 gift in the current year and each of the next four years. In that same year, you may gift an additional \$6,000 to the same beneficiary in a custodial account (reaching your one-year total of \$13,000, the annual gift-exclusion limit for 2011). If each spouse of a married couple gifted \$35,000, the couple would be able to double these gifts.*

How can I maximize the 529 plan's estate-planning benefits?

Affluent families may want to contribute as much as possible into a 529 plan, both to fund college expenses for beneficiaries and to move assets out of a taxable estate. The obvious solution appears to be to make the maximum annual exclusion gift contribution (\$65,000 for an individual or \$130,000 for a married couple using the five-year lump-sum election) in a single year.

Think twice if this is your goal and you are close to the end of the year. By maximizing that contribution this year, you use your annual-exclusion gift amount for that beneficiary for the next four years. That means four more years must pass before you can again contribute to that 529 plan account for that beneficiary without gift-tax consequences. If, instead, you make one year's annual exclusion gift for a beneficiary before year end, (\$13,000 for an individual or \$26,000 for a married couple) and then maximize your 529 plan contribution in the new year, you can contribute up to \$78,000 (individuals) or \$156,000 (married couples) within a matter of months rather than over six years, as illustrated below.*

Maximizing the estate-planning benefits of a 529 plan

For a married couple



**This hypothetical example is designed to illustrate the effect of certain planning strategies based on stated assumptions. The strategy described may or may not be suitable for your particular situation. Before implementing any strategy, you should seek the advice of your tax and legal advisors. No guarantee of specific results is made; past performance is no guarantee of future results.*

This publication is designed to provide accurate and authoritative information regarding the subject matter covered. It is made available with the understanding that Wells Fargo Advisors is not engaged in rendering legal, accounting or tax-preparation services. If tax or legal advice is required, the services of a competent professional should be sought. Wells Fargo Advisors' view is that investment decisions should be based on investment merit, not solely on tax considerations. However, the effects of taxes are a critical factor in achieving a desired after-tax return on your investment.

The information provided is based on internal and external sources that are considered reliable; however, the accuracy of the information is not guaranteed. Specific questions on taxes as they relate to your situation should be directed to your tax advisor.

Investment and Insurance Products: ► NOT FDIC Insured ► NO Bank Guarantee ► MAY Lose Value

Wells Fargo Advisors is the trade name used by two separate registered broker-dealers: Wells Fargo Advisors, LLC and Wells Fargo Advisors Financial Network, LLC, Members SIPC, non-bank affiliates of Wells Fargo & Company. ©2009 Wells Fargo Advisors, LLC. All rights reserved.