The Wealth Counselor

A monthly newsletter for wealth planning professionals

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A law firm that focus our practice on Estate Planning and Administration, Business Planning and Elder Law. We help families and businesses preserve and protect assets and values.

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529 Plan Benefits Made Permanent by the Pension Protection Act

Whether your client is a parent with future educational obligations for young ones, or perhaps a loving aunt, uncle, grandparent, or stepparent, now more than ever 529 plans are an attractive tool for the escalating costs of education, as well as for income and estate planning purposes. This is because one of the hidden gems of the new Pension Protection Act of 2006 (signed into law on August 17, 2006) is a provision that makes permanent the income tax-free growth of Section 529 plans used for qualified higher education expenses. Prior to this new law, these provisions would have expired December 31, 2010.

> **Planning Tip: The new Pension Protection Act makes permanent the income tax-free growth of 529 plans, but only for withdrawals used for qualified higher education expenses. Funds used for other expenses are tax deferred (like an IRA) and subject to a 10% penalty.**

Most wealth planning professionals (and clients for that matter) understand the value of investing in 529 plans. 529 plans are by far the most popular college savings vehicle, but they've just become even more popular. According to a recent survey, 54% of parents with young children who do not currently own a 529 account are more likely to open one now, due to the new law, and 36% who already own a 529 plan say they are now more likely to increase the amount they contribute to existing plans. And another recent survey confirmed that older clients may want to learn more about college savings.

Income Tax Benefits

While many clients understand the educational savings benefits, many do not understand the benefits of investing in 529 plans for income tax purposes. Just like with an IRA, the power of tax-deferred growth makes 529 plans worthwhile even if not used for educational expenses. The ability to frontload up to five years of annual exclusion gifts, or $60,000 per beneficiary ($120,000 per beneficiary for married couples), without paying gift tax creates the ability to grow a significant amount of money tax free. In addition, many states offer residents a state income tax deduction for an investment in their state's 529 plan.

> **Planning Tip:** Clients should consider an investment in a 529 plan even if it is not anticipated that the funds will be used for educational purposes. The income tax benefits alone of 529 plans make these very worthwhile investments.

Estate Planning Tax Benefits

529 plans are unique in that you can invest in a 529 plan, retain absolute control over the assets, and yet remove those assets from your estate for estate tax purposes. This type of control typically means that the asset would be subject to estate tax at a 46% rate (in 2006) at death, but not with a 529 plan. Thus, clients can invest up to $60,000 per beneficiary ($120,000 per beneficiary for married couples) without paying gift tax and, if the client lives for at least five years, all of these assets will not be subject to estate tax. More importantly for many clients, a 529 plan allows them to use the 529 plan assets in a financial emergency.

> **Planning Tip:** Clients should also consider 529 plans for estate planning purposes to remove significant wealth from the estate tax while retaining the ability to use the assets in a financial emergency.

Educational Trusts

Many 529 plans permit a trust to be the owner and beneficiary of accounts set up under that states plan. A 529 plan combined with an Educational Trust may provide more flexibility to ensure that the 529 meets the client's objectives by, for example, moving assets between siblings or providing a smooth transition should the client become incapacitated or die.

This combination of 529 plans and specially designed trusts can also provide divorce and creditor protections, even for those states' 529 plans that do not provide their own asset protection; for example, to ensure that the 529 plan's assets do not end up in the hands of a former son-in-law or daughter-in-law. And the client still retains the ability to use the funds in a financial emergency.

> **Planning Tip:** Consider combining 529 plans with Educational Trusts to provide the greatest flexibility and to ensure that the 529 plan assets meet each client's particular planning objectives.

Conclusion

Now more than ever, clients should consider 529 plans for educational savings, income tax benefits and estate tax benefits; and when combined with a carefully-crafted Educational Trust, they will provide added flexibility to control this asset and to ensure that it meets the client's planning objectives.

You have received this newsletter because I believe you will find its content valuable, and I hope that it will help you to provide better service to your clients. Please feel free to contact me if you have any questions about this or any matters relating to estate planning.

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