

## Investing for Education

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This publication provides an initial look at investing for future educational expenses. To find out more about investing, see *Before You Invest* (NebGuide G1925), *Investment Alternatives* (Extension Circular EC481), and *Investing for Retirement*, NebGuide G2097.

- How much to invest for education
- Tax-advantaged investments for education
- Paying for higher education

After retirement, one of the most frequently reported investment goals is funding college or post-secondary education. Saving for a child’s education is one of the largest expenses a family may have. To help prepare, first determine how much you wish to invest for college. Then, use the interactive calculator at the College Savings Plan Network website, [www.collegesavings.org](http://www.collegesavings.org), to get an estimate of the savings required based on the child’s age, type of college, number of years until the child attends college, and specific expenses being covered.

### Where to Invest for Education

Next, decide where to invest money being saved for a child’s education. There are several tax-advantaged investment products to make the savings process easier. Available options include:

- **529 plans.** Every state offers at least one type of 529 plan. Specific details about each state’s plans can be found at the College Savings Plan Network website (listed above). Withdrawals from 529 accounts for qualified educational expenses are tax-free. Earnings grow tax-deferred, allowing investors to maximize the power of compound interest. Look for plan features such as state income tax benefits, low investment expenses, high contribution caps, affordable minimum contributions, and “age-based tracks” where the asset allocation becomes more conservative as the beneficiary gets older. One of the best websites for comparing 529 plans is [www.savingforcollege.com](http://www.savingforcollege.com).

- **Coverdell Education Savings Accounts.** The maximum annual contribution limit of \$2,000 grows tax-deferred and is tax-free if used for qualified education expenses including tuition, room, board, supplies, and fees. Coverdell accounts allow a wide choice of investment choices. While there are no tax deductions for contributions, withdrawals are also allowed for elementary and secondary school expenses as well as post-secondary education. Balances in a Coverdell must be spent by the time the beneficiary reaches age 30, or they may be gifted to another family member under 30.
- **Prepaid tuition plans** are offered by about one-third of all states, as well as by individual colleges and universities. An advantage is that investors can lock in current tuition and fees when the plan is opened (as long as residency is established for the parent or child).
- **Custodial accounts.** The Uniform Gift to Minors Act (UGMA) and Uniform Transfer to Minors Act (UTMA) provide for tax-advantaged custodial accounts for college savings. An adult acts as the custodian for the account and makes all the investment decisions until the beneficiary reaches the age of majority. UGMA accounts are limited to holding money and securities. UTMA accounts can also hold real estate, fine art, and patents and royalties. A possible disadvantage with custodial accounts is that the money is technically owned by the child at age of majority (depending on state law) and could be used for expenses other than college. Also, since these funds belong to the child, they could reduce available financial aid. Changes in tax laws have extended the “kiddie tax” on college students’ investment earnings to age 24. Under this tax, specified unearned income of a child such as earnings on investments is taxed at the parent’s marginal tax rate no matter whether the child is claimed as a dependent on the parent’s return.

- **Savings bonds** may be a way to accumulate funds for education expenses because the interest earned over the life of the bonds usually is tax-free if planned according to income and other restrictions. For additional information, see IRS Form 8815 at [www.irs.gov/pub/irs-pdf/f8815.pdf](http://www.irs.gov/pub/irs-pdf/f8815.pdf).

#### **Tips on Paying for Higher Education**

- Always investigate the availability of financial aid. An objective information source for financial aid is The College Board at [www.collegeboard.com/pay](http://www.collegeboard.com/pay).
- For most situations, use earmarked education sources such as Coverdell and 529 plans first.
- Consult a tax professional before using a home equity line of credit, pension plan, or IRAs for paying educational expenses.

#### **Resource**

eXtension Personal Finance website: [www.extension.org/personal\\_finance](http://www.extension.org/personal_finance)

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