

# Ways to Save for College

In accumulating funds for college, one of the first questions a family will face is, "Where do we invest the money?" Many financial professionals will recommend to their clients that money saved for college should be placed in relatively low-risk investments. If there is a long enough time frame, the savings may be placed initially in higher risk (and potentially higher return) investments. As the time for college gets closer, the accumulated funds can be shifted into more conservative choices.



The ultimate decision will depend on a range of factors such as the number of years until college begins, the amount of money available to invest, a family's income tax bracket, risk tolerance, and investment experience. A few of the more traditional approaches are:

- **Savings accounts:** Including certificates of deposit, money market deposit accounts and passbook savings accounts.
- **Tax-free municipal bonds:** Held either directly or through a mutual fund.
- **U.S. Treasury securities:** Such as treasury bills or treasury bonds.
- **Growth stocks/growth mutual funds:** For the long-term investor.

## Tax-Advantaged Strategies

There are a number of tax-advantaged<sup>1</sup> strategies available to accumulate funds for college expenses. The rules surrounding these strategies can be complicated and they should only be used after careful review with a tax or other financial professional.

- **IRC Sec. 529 Plans:** These plans allow an individual to either pre-pay a student's tuition, or contribute to a savings account established to pay the student's "qualified higher education expenses." Contributions are not tax deductible, but growth in an account is tax-deferred. If certain requirements are met, distributions to pay qualified higher expenses are excluded from income.<sup>2</sup>
- **Coverdell Education Savings Account (C-ESA):** Up to \$2,000 per year may be contributed to a C-ESA for an individual. Contributions are not tax-deductible, but growth is tax-deferred. Distributions are excluded from income if used for qualifying educational expenses. Other restrictions may apply.
- **U.S. savings bonds:** Interest on series EE savings bonds issued after 1989, or Series I savings bonds, may (certain limits apply) be excluded from income if qualified education expenses are paid in the year the bonds are redeemed.
- **Baccalaureate bonds:** A special form of state-issued, tax-exempt municipal bond. Interest on these bonds is generally tax free, at both the state and federal level.

<sup>1</sup> The rules described here concern federal income tax law. State or local income tax law may vary.

<sup>2</sup> The fees, expenses, and features of 529 plans can vary from state to state. 529 Plans involve investment risk, including the possible loss of funds. There is no guarantee a college-funding goal will be met. Under current federal tax law, the tax-free treatment of qualified 529 plan distributions ends December 31, 2010.