Saving for Future College Costs

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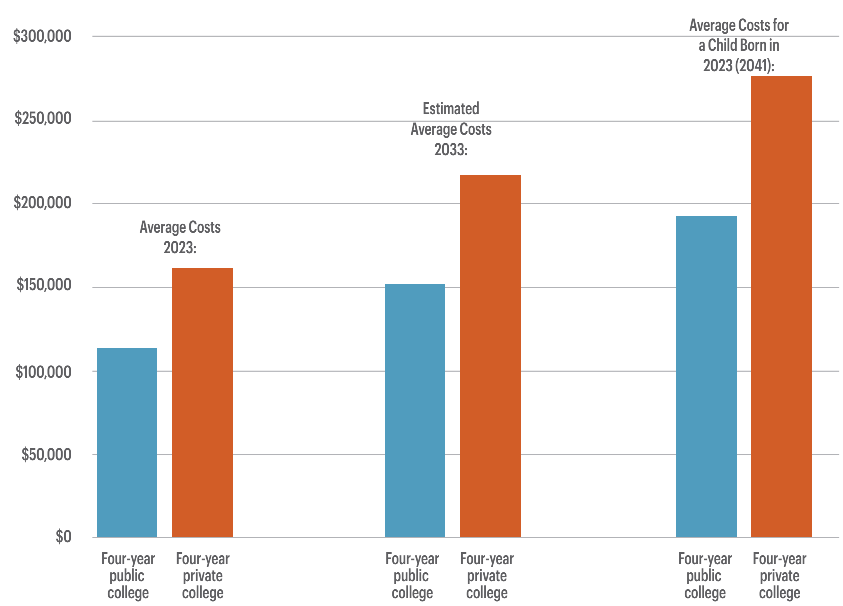
STUDENT LOAN AVAILABILITY HAS CHANGED over the last 20 years. Options for future generations are more limited. As well, costs continue to increase, an average of 3.11 percent annually from 2010 to 2020 for a four-year college.

For those with household incomes of $110,000 or more, the estimated net cost after grants and aid for a four-year public college is $113,338, $162,866 for a private school. The current limit on four years of federal loans, including subsidized and unsubsidized loans, for a dependent undergraduate is $27,000. As such, a student will need an additional $86,000 for a public college or $135,000 for a private college for their four years.

That's the estimate for a student starting in Fall 2023. It will only get more challenging. The estimated average net four-year cost in 10 years before federal loans will be $152,000 for a public college and $218,000 for a private school. In 18 years — that is, for 2023 newborns — costs will have risen to averages of $193,000 for a public college and $277,000 for a private college four-year education. Whatever is not funded by savings or cash flow will likely be funded by private student loans, which will require a co-signer unless the student has a qualifying credit history and an approved amount of earned income.

College Costs Keep Rising



Source: Pennsylvania College averages from 2020 used and calculated with a 3% inflation rate.

How does all that translate when it comes to paying back student loans? For a freshman entering college this fall borrowing the full amount, including the federal student loans, and assuming a best scenario 5 percent interest rate over 20 years, their loan payments will be an estimated $748 per month (public school) or $1,074 per month (private school). The number of financial institutions that consolidate loans has also dwindled over the last 20 years due to higher default rates, meaning there is not as much competition to work in a student's favor.

529 PLANS AND SAVINGS

529 plans are excellent tools for saving for college, especially if they are started early in the student's life. Ultimately they are after-tax dollars — and many states allow deductions for contributions — that grow tax deferred. If the gains are used for qualified education expenses, they are tax-free. In a scenario where $500 per month is saved for 18 years — a total of $108,000 — given a 6 percent annualized return, the account would be worth $193,676, including the gain of $85,676 that will not be taxed as long as the money is used for qualified education expenses.

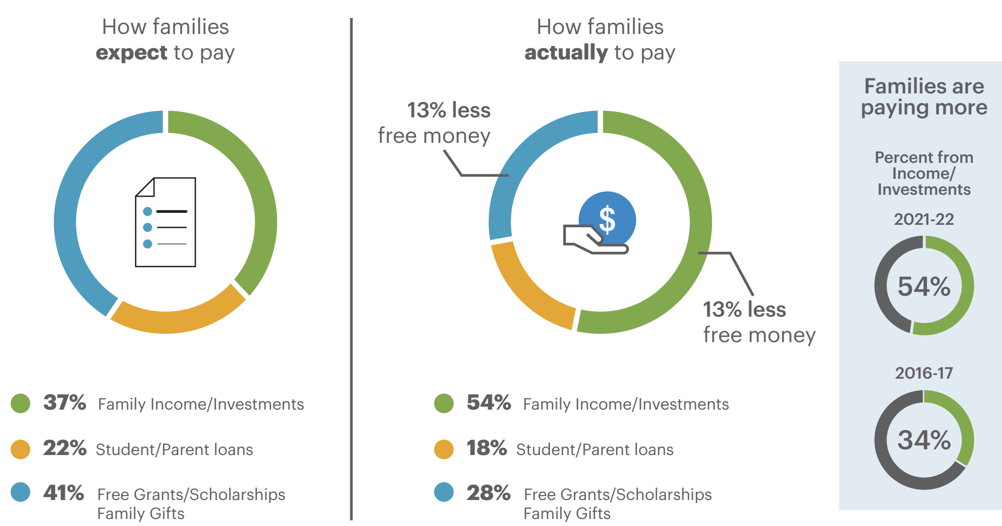
QUALIFIED COLLEGE EDUCATION EXPENSES INCLUDE:

- Tuition and fees (for all eligible institutions)
- Books and supplies
- Computers, software and Internet
- Room and board (must be enrolled and attending at least half 50 percent of the time)
- Special needs equipment
- Student loans (a lifetime limit of $10,000)

Paying for College: Expectations vs. Reality

The typical family pays more than expected for college from their own pocket.

Families need more for college than expected.
Breakdown of college funding sources.



Source: Sallie Mae, **How America Pays for College**, 2017 and 2022, and **Higher Ambitions: How American Plans for Post-Secondary Education**, 2020.

The student must attend a qualifying school, which includes colleges and universities, but also vocational and trade schools. Public, private, and parochial elementary and secondary schools also qualify for up to $10,000 per year of untaxed dollars used for expenses. As long as the institution you're enrolling in is eligible for Title IV federal student aid, you can also use a 529 plan to pay for online tuition and fees.

LEFTOVER FUNDS

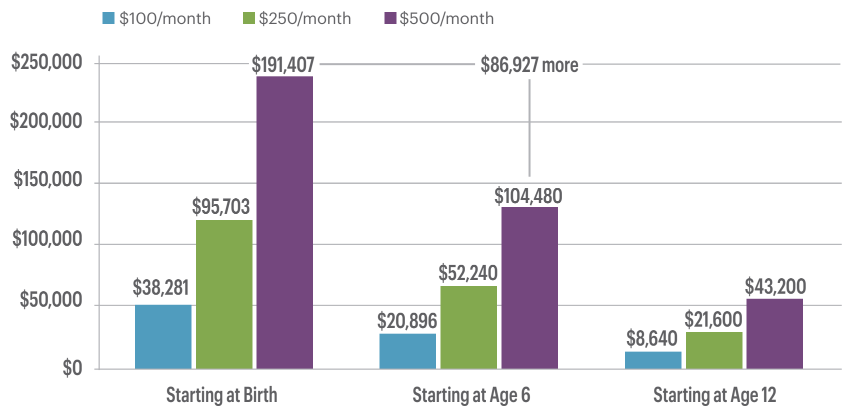
There are no time or age limits for using a 529 college savings plan. Money can be kept in a 529 plan indefinitely. If there are 529 funds left over after education expenses are paid, the money can be used in a variety of ways:

- For additional education, such as to pursue a master's or doctorate degree
- For another student, a qualified family member of the original beneficiary:
    - Spouse
    - Son, daughter, stepchild, foster child, adopted child or a descendant
    - Son-in-law, daughter-in-law
    - Siblings or steps-siblings
    - Brother-in-law, sister-in-law
    - Father-in-law, mother-in-law
    - Aunt, Uncle or their spouse
    - Niece, nephew or their spouse
    - First cousin or their spouse
- As tax-free 529 distributions to pay off student loan debt up to a lifetime limit of $10,000 (a provision of the SECURE Act)
- To be saved for the education of future generations (an opportunity to establish an educational legacy for your grandchildren)
- In some cases, as a non-qualified withdrawal with no penalty tax on the earnings, such as when the beneficiary dies, becomes disabled, or attends a U.S. military academy
- If your child gets a scholarship, up to the amount of the award to spend on anything you like (investment account gains taxed as income)
- As of 2024, to roll over into a Roth IRA for the account's beneficiary without incurring taxes or penalties (up to $35,000, subject to annual Roth IRA contribution limits [$6,500 in 2023]; a provision of SECURE 2.0 Act). Additional stipulations include:
    - You must have owned the 529 educational savings account for at least 15 years before you can roll over the money.
    - You can only roll over money that's been in the account for five or more years.
    - The account holder, typically a child's parent or guardian, can't roll over the money into their own Roth IRA. It must be an account established for the beneficiary of the 529 plan.

Start Early, Save More

The sooner you start investing the more time you have to grow your college fund through the power of long-term compounding.

Small monthly contributions add up over time. Total amounts accumulated at different starting ages[1].



Put college investing on autopilot.

Three-fourths of 529-plan users make automatic contributions from bank accounts or paychecks[2].

[1]J.P. Morgan Asset Management. This hypothetical example illustrated the future values at age 18 of different regular monthly investments for different time periods. Chart also assumes an annual investment return of 6%, compounded monthly. Investment losses could affect the relative tax-deferred investing advantage. This hypothetical illustration is not indicative of any specific investment and does not reflect the impact of fees or expenses. Such costs would lower performance Each investor should consider his or her current and anticipated investment horizon and income tax bracket when making an investment decision as the illustration may not reflect these factors. A plan of regular investment cannot ensure a profit or protect against a loss in a declining market. This chart is shown for illustrative purposes only. Past performance is no guarantee of future results.

[2]ISS Market intelligence, 529 Industry Analysis 2022.

As a wealth advisor, I do not advise my clients to rob from their retirement savings to fund their child's or grandchild's education. However, if the money is available, or you can make room in your budget to put aside an amount on a monthly schedule, 529 savings are an excellent way to reduce the financial burden of student loans your children might face in the future. Parents may be inclined to think, "My kids will borrow money to go to college like I did." However, be aware that loan access and options have changed significantly and the resulting burdens on graduating students have increased substantially.

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Brittany Taylor helps her clients achieve their financial goals by establishing and overseeing financial plans specific to their unique economic and life situations. She employs a holistic approach with investment and wealth protection plans that help them attain their objectives. Contact Brittany at 814-459-1116; or email her at btaylor@hbkswealth.com