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# Choosing a College Savings Plan

**May 28, 2016**

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# Choosing a College Savings Plan

With so many 529 plans to choose from, you'll need to ask a lot of questions in order to select the best plan for you.

## Compare the plans offered by different states

If you're interested in joining a college savings plan, you should consider all of your options. Compare the plans offered by different states in terms of flexibility, tax considerations, investment selection, contribution rules, and costs and fees. Any state that offers a 529 plan can provide you with a free packet of information that describes the program and its rules. You can also check out a plan's website.

Keep in mind that some states allow nonresidents to join their plans, and others don't. The vast majority of states that offer college savings plans allow nonresidents to participate.

## Consider the plan's account ownership and beneficiary designation rules

When comparing college savings plans, keep plan flexibility in mind, particularly with respect to account ownership and beneficiary designation rules. These rules may vary from state to state. A college savings plan can be an expensive undertaking. And your child's education is certainly important to you. As an account owner, you'll want to make sure the account works the way you want it to work.

Generally, the account owner retains ownership and a certain amount of control over the college savings plan account. For example, he or she can change the beneficiary of the account or terminate the account and receive a refund of contributions. However, keep in mind that if you terminate the account, you'll typically receive back only a portion of your earnings, if any, and a penalty will generally apply, unless you terminate the account because the beneficiary has died or is disabled. Here are some questions to ask when researching various plans:

- Can I own the account jointly with my spouse or another person?
- Can a trust or other entity be an account owner?
- Can I name a successor owner when I open the account? If not, what happens to the account when I die?
- Must the account owner be a state resident? Must the beneficiary be a state resident?
- What happens if the account owner or beneficiary later moves out of state?
- Are account statements issued only to the account owner or also to the beneficiary?
- Can I view the account on-line?
- If I terminate the account, how much of my contributions and earnings will I get back, and will I pay a penalty?

## Tax considerations

Some individuals favor 529 college savings plans over other college savings vehicles because of the federal (and sometimes state) tax advantages associated with 529 plans. Let's face it--we all want to keep our taxes to a minimum. No matter which college savings plan you join, all qualified withdrawals will be free of federal income tax. But things differ at the state level.

Some states exempt a college savings plan's earnings from income tax if used to pay qualified higher education expenses. Some states may also let you deduct on your state income tax return some or all of your plan contributions in a given year. Other states offer no such income tax benefits. Since state tax benefits can vary widely, compare the tax benefits. But remember--you're entitled only to the state tax benefits (if any) offered by the state in which you reside. So, look at your own state's plan first and research the state tax benefits available, especially if you're thinking about moving to another state in the near future. Also, keep in mind that states may limit their tax benefits to individuals who participate in the in-state 529 plan only.

Consider, also, any state gift tax issues regarding contributions, and whether there are state penalties for withdrawals that are not used for permitted education expenses. The following questions can help you determine what tax advantages each state offers:

- Can I claim a deduction on my state income tax return for my contributions to the college savings plan?

- Is my deduction recaptured into income if later withdrawals are not used for qualified education purposes?
- Is there a limitation or cap placed on the amount of my state income tax deduction? If so, what is it?
- If a withdrawal from the college savings plan is used to pay qualified education expenses, are the plan's earnings exempt from state income tax? Must I join my own state's 529 plan to get its tax benefits?

## Number and type of investment vehicles offered

If you're interested in opening a college savings plan account, you should consider the number and type of investment vehicles offered by each plan. Since some investors are more comfortable with risk than others, investment choice is important. For example, if you're a conservative investor with very limited funds, you might want to choose a plan that offers one or more conservative investment options. Investment choice may also be important if you're a sophisticated investor who wants to maximize return. However, keep in mind that all investing involves risk, including the possible loss of principal, and there can be no assurance that any investment strategy will be successful.

College savings plans typically offer several different investment portfolios that you can pick from to invest your contributions. If you want to change your investment option, you can generally do so twice per calendar year for your existing contributions, anytime for your future contributions, or anytime you change the beneficiary of the account.

You may want to look at the past investment performance of a particular portfolio and compare it with other portfolios in different plans. You should also think about the reputation of the plan manager. Here are some investment-related questions to ask:

- How many investment options does the college savings plan provide?
- Is an age-based asset allocation approach offered? If so, can I select a portfolio other than one designed to match the age of my designated beneficiary?
- If the college savings plan offers more than one investment option, can I spread a contribution among the options without opening multiple accounts?
- Can I choose one investment portfolio with today's contribution, and a different portfolio with future contributions?
- Under what circumstances will the plan let me switch my existing contributions (and earnings) from one portfolio to another portfolio?
- Can I make changes to my investment selections online or over the phone, or do I need to send in a written request?
- Who manages the plan's investments, and how solid is that company's reputation?
- When does the investment manager's contract with the plan end? What happens to my account if the state changes investment managers?

## Contribution rules

Although we all have different financial situations, money is important to each of us. So, to ensure that you select a college savings plan that best matches your financial means, you should investigate the contribution rules of each plan. For example, if you have plenty of funds to invest, you might be interested in the college savings plan that allows you to accumulate the most funds (the maximum contribution limit). Most plans have maximum contribution limits of \$300,000 and up. But if money is tight for you, you might want to avoid plans that require a high annual plan contribution. Find out the answers to the following questions:

- What's the maximum contribution limit for the plan?
- What's the minimum amount I must contribute to establish the college savings plan?
- Are annual contributions required? If so, how much?
- Can someone other than the account owner make plan contributions?
- Are the contribution limits different if I am a resident of the state or a nonresident?

## Costs and fees

Since plan costs and fees can really add up and take a sizable bite out of your funds, you should consider the expenses associated with each plan. Sometimes, nonresidents joining a plan must pay higher broker's fees or higher annual account fees. Investigate whether a break is given to residents, and compare the overall costs of different plans. Consider the following questions:

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- Are residents and nonresidents treated differently in terms of plan costs and fees?
  - Is there an application fee, beneficiary substitution fee, or account owner substitution fee?
  - What other fees and costs are charged, and what are the amounts?
  - Will my fees be less if I contribute through payroll deduction or automatic deduction from my checking account?
  - Is there a fee to do a rollover to another state's plan?
  - Will I be penalized if I move my account out of the plan within a short time after I open the account? How short a time?
  - Is there a fee if I terminate the account?
  - Do I pay the fees separately, or is the fee deducted from my account?

**Note:** *Investors should consider the investment objectives, risks, charges, and expenses associated with 529 plans before investing. More information about 529 plans is available in the issuer's official statement, which should be read carefully before investing. Also, before investing, consider whether your state offers a 529 plan that provides residents with favorable state tax benefits. As with other investments, there are generally fees and expenses associated with participation in a 529 savings plan. There is also the risk that the investments may lose money or not perform well enough to cover college costs as anticipated.*

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