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YOUR WEALTH JOURNEY — NAVIGATING LIFE'S FINANCIAL MILESTONES

Financing a College Education: Options to Consider

Tips for developing the best strategy while keeping your financial goals intact

Among its many benefits, a college education can have a significant impact on future earning potential. It is an important investment. It is also becoming a more expensive one as increases in college costs continue to outpace inflation. Fortunately, if you want to help pay for your child's or grandchild's education expenses, numerous financing options are available.

Savings Vehicles

The cost of college education has risen faster than inflation nearly every year over the past four decades. And while colleges costs have risen more slowly over the past 10 years, they continue to increase. According to the College Board Trends in College Pricing 2023, the published inflation-adjusted (real) costs of tuition, fees, and room and board have risen on average about 0.5% over this time frame, reaching nearly $56,000 a year at private schools by 2023 and nearly $40,000 at public schools.

Whether you need to build up assets to finance your children's or grandchildren's education or you expect to pay their education costs out-of-pocket, you may benefit from using one or more savings vehicles. The earlier you begin, the greater the potential benefits.

529 College Savings Plan

A 529 savings plan allows parents and grandparents to set aside money for a child's college education, offering tax-deferred growth and tax-free distributions for qualified education expenses such as tuition, fees, books, room and board. Since 529s are state-sponsored saving plans, some states will offer an income tax deduction or tax credit. Contributions are not federally tax deductible.

You can contribute only cash, not securities, to any state plan you select. Each state sets the contribution limits and offers investment options, varying in type, risk, and time frame. You have the ability to reallocate assets twice a year. You retain control of the investment account and name the beneficiary. Additional restrictions and limits may apply.

A 529 plan also comes in the form of a prepaid tuition plan, allowing you to pay for future tuition at today's prices. However, if the beneficiary chooses a school not included in the plan, there may be uncertainty about how the value of the prepaid tuition plan will be determined. Additionally, if the selected school is private, the value may fall well short of tuition costs.

Among the advantages of a 529 plan is the ability to front-load the plan by using up to five years of your gift tax annual exclusion ($18,000 for 2024). That adds up to an $90,000 immediate contribution—$180,000 for a married couple splitting the gift. The contribution is removed from your taxable estate, yet you keep control over the 529 plan. Be mindful that there could be estate tax consequences if you accelerate your annual exclusions and die before the five years have passed. Also, any distributions attributable to growth that are not used for qualified education expenses will be subject to income taxes and a 10% penalty.

Contributions beyond the annual exclusion will be applied toward your lifetime gift and estate tax exclusion of $13.6 million for 2024.

You are able to change the beneficiary to certain family members in the same generation, such as a sibling or first cousin of the beneficiary or yourself if you are considering going back to school. This will allow you to avoid taxes and penalties if the initial beneficiary decides not to pursue a college education or does not use all the plan funds on qualified expenses. Keep in mind that changing the beneficiary to someone in a lower generation than

the current beneficiary, such as his or her child, could trigger gift and generation-skipping transfer (GST) tax consequences.

Note: *Federally tax-free withdrawals are allowed to pay for up to $10,000 of K-12 tuition. State tax benefits are available for expenses that the state deems as "qualified," which may or may not include K-12 tuition.*

Uniform Transfers to Minors Accounts (UTMAs)

An UTMA allows you to transfer assets to a minor by opening a custodial account for them. The assets can be used not only for education expenses, but for any purpose that will benefit the child with the exception of basic support expenses such as food and clothing.

Assets transferred are removed from your taxable estate, yet you maintain control over how the assets are invested and distributed until the beneficiary reaches the age of majority (18 or 21, depending on the state).

There is no limit on how much you can transfer to an UTMA. Transfers are eligible for the annual gift tax exclusion ($18,000, or $36,000 for married couples splitting gifts in 2024). Those in excess of your exclusion will use up part of your lifetime gift tax exemption or be subject to gift taxes. If the beneficiary is your grandchild or someone else more than one generation below you, a transfer beyond your annual exclusion generally will also use up some of your GST tax exemption or be subject to GST tax.

The minor is subject to income tax on a UTMA account. If income is above $2,600 (for 2024) the "*kiddie tax*" applies.

Trusts

Creating a trust is a way to transfer an unlimited amount of assets that can be used to fund a child's or grandchild's college education while maintaining some control over investments and distributions. A wide variety of options are able, each offering various advantages and disadvantages.

With an irrevocable trust, for example, assets transferred to the trust are removed from your taxable estate. The trustee, named by you, maintains control over how the assets are invested and when they are distributed to the beneficiary. Since the annual gift tax exclusion does not apply to gifts made to irrevocable trusts, often a "Crummey" provision is added, thus allowing the gift tax exclusion.

Trust income (in non-grantor trusts) that is not distributed is subject to income taxes — based on special tax brackets for trusts, where the rates climb much more rapidly than for individuals. Trust income distributed to the beneficiary could be subject to the kiddie tax.

Coverdell Education Savings Accounts (ESAs)

Similar to IRAs, Coverdell Education Savings Accounts allow you nearly unlimited investment options and the ability to reallocate assets at almost any time. Similar to 529 plans, distributions used for qualified education expenses are tax free.

Unfortunately, the annual contribution limit is just $2,000, and that limit is gradually phased out down to $0 based on relatively low income-based limitations. So, an ESA likely will not be sufficient to finance all of your child's or grandchild's education expenses. However, it can supplement other saving vehicles.

Direct Tuition Payments

If you would like to avoid the various limitations that apply to 529s, UTMAs, trusts, and ESAs but still want to help finance your child's or grandchild's education, another option is making tuition payments directly to the school, rather than giving money to the child to pay the tuition.

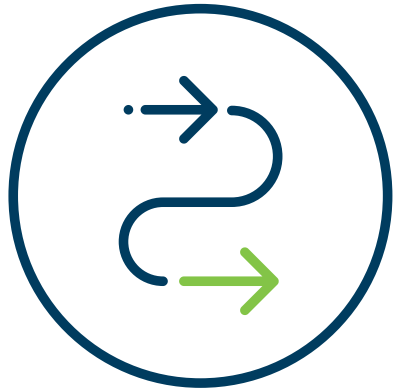
Direct tuition payments are not subject to gift or GST taxes and therefore do not use up any of your annual gift tax exclusion, lifetime gift tax exemption, or GST tax exemption.

Direct tuition payment is also available for elementary and high school tuition.

Education Financing Options at a Glance

	Advantages	Disadvantages	Other Considerations
529 Savings Plan	• Tax-free earnings and distributions • No income limits for making contributions • Contributions may be deductible for state income tax • Assets generally excluded from owner's estate • Beneficiary can be changed to another family member • Varying levels of control of investments	• Benefit not guaranteed; investment risk • May only be used for qualified education expenses • 10% penalty and ordinary income tax on the earnings portion of non-qualified distributions	• Need to evaluate different states' plans • Can front-load the plan by contributing up to 5 years of your gift tax annual exclusion • Year-round enrollment • Cash contributions only
UTMA (Custodial Account)	• Flexibility—may be used for expenses other than education • No income or contribution limits • Assets excluded from donor's estate • Control of investments	• Beneficiary gains control of assets at age 18 or 21 • No income-tax benefits and may trigger "kiddie tax"	• May trigger gift tax • Assets owned by the beneficiary
Trust	• Flexibility—may be used for expenses other than education • Control over distributions • No income or contribution limits • Control of investments • If irrevocable, removes assets from donor's estate	• No income-tax benefits • Legal fees to establish	• Attorney creates trust document • May require Crummey provisions to avoid triggering gift tax • May be subject to trust tax rates
Coverdell Education Savings Account (ESA)	• Tax-free earnings and distributions • Kindergarten through graduate expenses eligible • Control of investments • Can be rolled over to ESA for another family member	• Benefit not guaranteed; investment risk • Contributions limited to $2,000 per year, phasing out at relatively low income levels • 10% penalty and ordinary income tax on the earnings portion of nonqualified distributions	• All assets must be distributed within 30 days of when the beneficiary turns age 30
Direct Payment	• Not subject to gift tax (without using up any annual exclusion or lifetime exemption) • Kindergarten through graduate expense eligible	• Gift-tax-free treatment applies only to payments of tuition and certain fees	• Payments must be made directly to the educational institution

Note: Savings and payment options affect financial aid in different ways. Contact your tax advisor for details.



Alternative Sources of Funding

It is wonderful to save to help a child with his or her education costs but you should not sacrifice saving for your own retirement. Alternative education-funding sources are available, whereas there are fewer options for funding retirement expenses.

Financial aid comes in a variety of ways, from grants and scholarships to work-study and loans. Often aid is needs-based, but a multitude of merit-based scholarships are available as well as student loans regardless of financial need.

If you have a child in college or graduate school now, your family may be able to benefit from one of the various tax credits and deductions available for certain education expenses or student-loan interest. These breaks generally phase out based on income. If your income is too high to qualify, your child might be eligible. A deduction for student loan interest is also available.

Begin Planning Today

Wherever you are on the timeline, begin planning for education expenses today. You will want to compare your options, fees, and tax implications of the various education savings plans available.

William Blair has extensive experience with comprehensive financial planning. We can help you determine how education financing should fit in with your overall financial plan and how to best achieve your goals. If you are interested in learning more, contact your William Blair wealth advisor.

Contact Us:

Please contact your William Blair wealth advisor or contact us at *pwm@williamblair.com*.