Financial Experts Network

INSIGHTS, TRENDS & OPPORTUNITIES WITH 529 PLANS

HOSTED BY TOM DICKSON

FINANCIAL EXPERTS NETWORK

TOM@FINANCIALEXPERTSNETWORK.COM

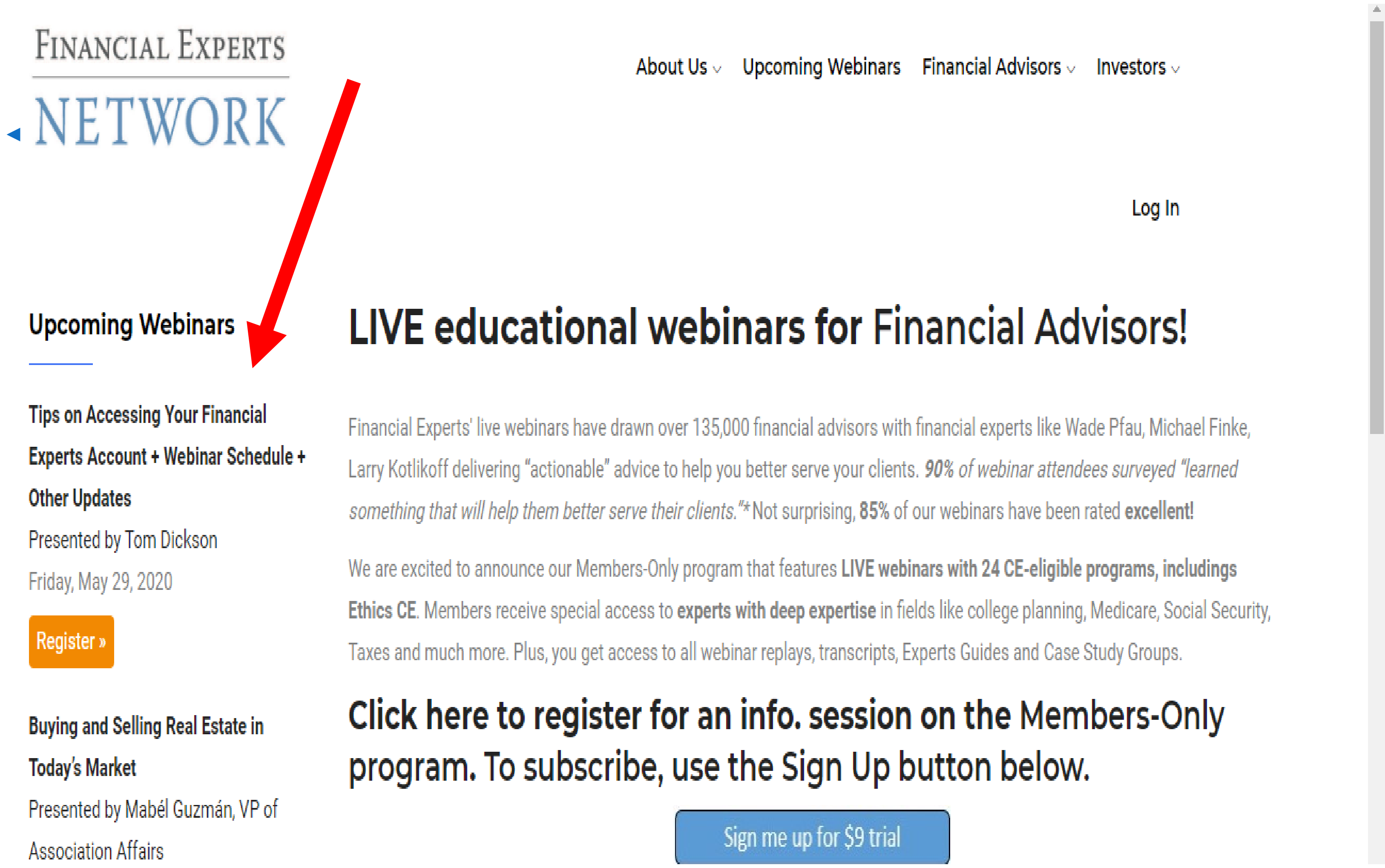
THANKS FOR BEING A MEMBER!

#1: Today's session is CE eligible

#2: Lots of Webinars

- **Buying/Selling Real Estate Today on June 4th**
- **Life Insurance Post SECURE Act on June 11th**
- **Ethics CE on June 25th**

Training this Friday at 11:00 EDT



FINANCIAL EXPERTS NETWORK

About Us | Upcoming Webinars | Financial Advisors | Investors

Log In

Upcoming Webinars

Tips on Accessing Your Financial Experts Account + Webinar Schedule + Other Updates

Presented by Tom Dickson

Friday, May 29, 2020

Register »

Buying and Selling Real Estate in Today's Market

Presented by Mabél Guzmán, VP of Association Affairs

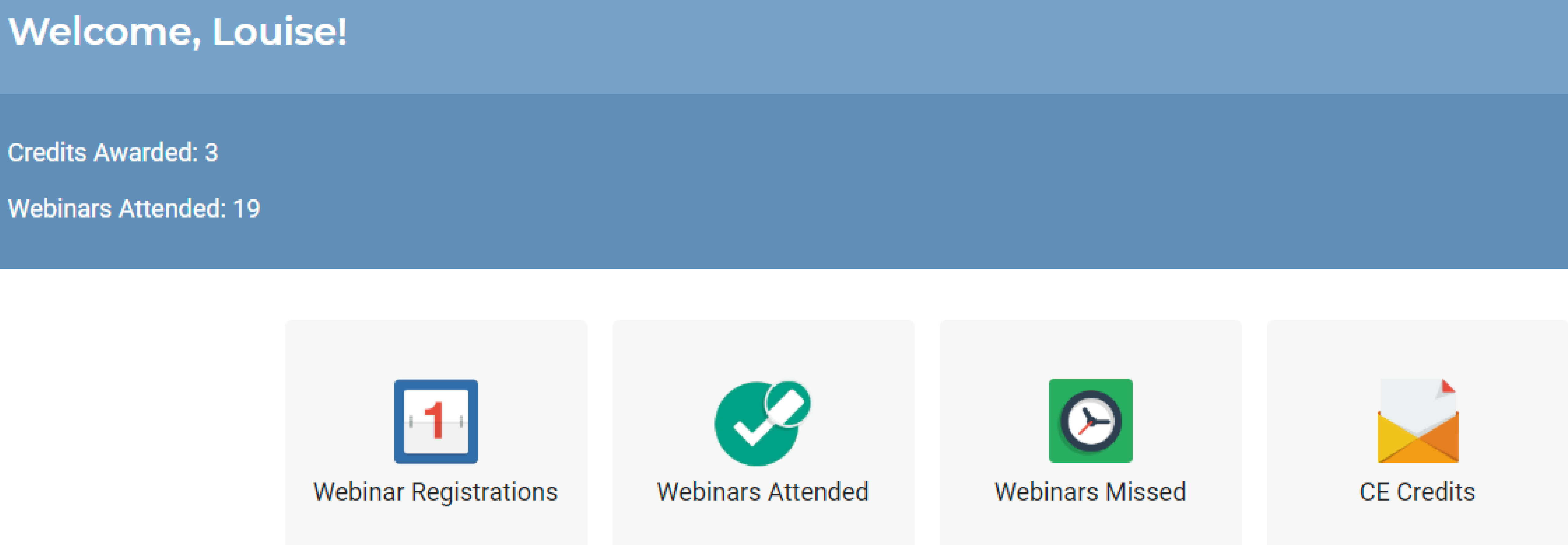
LIVE educational webinars for Financial Advisors!

Financial Experts' live webinars have drawn over 135,000 financial advisors with financial experts like Wade Pfau, Michael Finke, Larry Kotlikoff delivering "actionable" advice to help you better serve your clients. ***90% of webinar attendees surveyed "learned** something that will help them better serve their clients."** * Not surprising, **85%** of our webinars have been rated **excellent!**

We are excited to announce our Members-Only program that features **LIVE webinars with 24 CE-eligible programs, includings Ethics CE**. Members receive special access to **experts with deep expertise** in fields like college planning, Medicare, Social Security, Taxes and much more. Plus, you get access to all webinar replays, transcripts, Experts Guides and Case Study Groups.

Click here to register for an info. session on the Members-Only program. To subscribe, use the Sign Up button below.

Sign me up for $9 trial



Confirm your CE credits and more

Webinars You Attended

Webinar	Date ▼	Attendance	CE Credits	
"Sure Things" that may impact 2020 Market Returns Presented by Larry Swedroe, Chief Research Officer	May 14, 2020	78 minutes	1	view replay
Lawyerly Advice on Financial Advisor Obligations under The SECURE Act Presented by Stephen Wilkes, Esq., Roberta Casper Watson. Esq.	April 30, 2020	82 minutes	1	view replay
Expert Panel on 401(k), IRA and SBA Loans under the CARES Act Presented by Scott Graham, Esq. Scott Bishop, CFP®, CPA	April 24, 2020	66 minutes	1	view replay

Financial Experts
NETWORK

"Sure Things" that may impact 2020 Market Returns

View Edit Delete Revisions Devel

Presented by Larry Swedroe, Chief Research Officer

Thursday, May 14, 2020 at 12:30 PM ET

Listen to investment expert Larry Swedroe for a fascinating update on the "sure things" commonly assumed as factors will impact the markets in 2020. These sure things include assumptions for key factors such as GDP growth, corporate earnings and inflation. These sure things also include overweighting investments such as REITs, gold and large-cap stocks.

Helpful Resources and Documents

Click here for materials

Welcome Guests!

Want Quality Education?

- **Monthly subscription**: $9 for 3-4 CE-eligible webinars a month
- **CE Credits**: CFP, CLU, RICP, CLU, ChFC and CIMA
- **Speakers:** Ed Slott, Wade Pfau, Bob Keebler et al.
- Webinars have an **86% Excellent Rating**

35 of 47 Webinars were CE eligible
May, 2019 to April, 2020

Learn more or Sign Up:

www.financialexpertsnetwork.com/subscriptions

Meet the Expert:

Christopher Stack, Esq.
Managing Consultant,
SavingforCollege.com

FINANCIAL EXPERTS
NETWORK

Introduction/legal note

- SFC is a well known independent resource and authority on 529 plans.

- Chris Stack has been a member of the NYS Bar for over 30 years and leads SFC educational and training efforts. He has served as author of 529 state legislation for several states and is very familiar with relevant provisions of Section 529 and various state programs and opened his first two 529 accounts in 1997.

- SFC and its affiliates are not broker-dealers, not affiliated with Financial Experts Network, or any 529 program manager or distributor and are not in the business of selling or offering securities and do not make recommendations to buy or sell securities of any kind. We do, however, receive fees from many managers of these programs, for a variety of products and services that we furnish, including a fee from Columbia Threadneedle Investments for speaking before you today and others other times.

- IRS Circular 230 Notice: To ensure compliance with requirements imposed by the IRS, you are informed that any U.S. tax advice contained in this communication is not intended or written to be used, and cannot be used by any taxpayer, for the purpose of avoiding U.S. tax penalties.

- This presentation does not constitute tax advice and investors should consult their tax advisors prior to making contributions to a 529 plan.

Background on 529 Plans

- Congress enacted IRC §529 in 1996, reacting to an IRS dispute about tuition prepayment programs a dozen states had set up to for their residents.

- Saving/Investment plans were also included in the legislation at that time.

- States serve as plan trustees – most interested in plans directly offered.

- First advisor-sold 529 plans introduced in 2000 by Alliance & Putnam

Background on 529 Plans

- As of 2002, 68% of net 529 sales were through advisor-sold plans vs. 32% direct-sold 529 plans.
- As of 12/31/19, $346B was invested in 529 investment plans, with $201B in directly sold plans, led by NV/Vanguard $22B, vs. $145B in advisor-sold plans, led by VA/American Funds $71B.
- In reality, NV & UT are 2 plans very popular with RIAs – who either don't bill for related advice or manually invoice for such 529 aum.

Why Talk About Investing in 529 Plans?

- Investing in education for family members is important to clients & prospects.
- Financial aid is **NOT** available for every client.
- Most financial aid awards includes loans; with interest increasing costs.
- Clients/prospects are clearly doing this on their own.
- "All or none" – holistic planning component.
- Deepens relationship with client – expand relationship horizontally.
- Opportunity for multi-generational issue – expand relationship vertically.
- **= Need to help clients plan and prepare!**

1. Fidelity 2016 Study . 2. The College Board Trends Report November 2019

College costs are high now and still ↑ 2x CPI

2019-2020 cost of attendance	x 4 years	= Cost not <
Boston U	\$75,002	\$300,008
Carleton College	\$73,769	\$295,076
Colgate	\$75,000	\$300,000
U of Miami	\$70,906	\$283,624
New York U	\$76,614	\$306,546
Notre Dame	\$74,193	\$296,772
Santa Clara	\$77,829	\$311,316
U. Southern California	\$77,459	\$309,836
Southern Methodist	\$74,918	\$299,672
Villanova	\$69,328	\$277,312
Wake Forest	\$71,700	\$286,800

FINANCIAL EXPERTS NETWORK

Source: website of each respective university December 2019.

Why should we invest in 529 plans?

- "The Best Way To Save for College": SFC
- A leading reason for long term saving/investing[1]
  = "STICKY ASSETS"
- One of the biggest obstacles to the preservation and growth of individual and family wealth over time is:
  - ☒ Inflation
  - Improper asset allocation/bear markets
  - **Taxes!**
  - **1 – Source: Investment Company Institute, Profile of Mutual Fund Shareholders, 2019**

FINANCIAL EXPERTS NETWORK

Why may 529 plans be the solution?
Look at what it offers!

I. 529 accounts grow free of federal and state income taxes

II. Qualified withdrawals free of federal and all state taxes (except AL)

III. Most apprenticeship, tech, college and graduate school expenses are qualified

IV. Qualified w/ds include up to $10K for: 1) annual tuition (only) for K – 12 & 2) student loans

V. No age, time, or income limit on owner/account or # of accounts per owner

VI. Generous gift and unique estate tax treatment

VII. Federal/state creditor protection may be available

VIII. Beneficiary never has any rights or access to account

IX. **Owner always has daily access, liquidity and control**

Investors should be informed that depending upon the laws of their home state, favorable state tax treatment of funding a Section 529 plan may be limited to investments made into plan offered by their home state.

Federal income tax rules

- ✓ Qualified withdrawals from a 529 plan are excluded from federal income taxes:
  - – Hypothetical example:
    - If **$150,000** is contributed/invested today/at once gift tax-free
    - Assume 6% growth over 7 years = **<u>$225,545</u>**

    = $75,545 of earnings grown & spent for Qualified Expenses is Federal & State (49 states) tax-free !!!!!

What happens if not used for college?

If owner decides not to use for designated beneficiary's college expenses, they have three options:

1. Change beneficiary to a qualified member of beneficiary's family
2. Do nothing and continue to earn on tax-deferred basis
3. Withdraw funds for any other purpose and pay taxes and penalty, if applicable, on earnings withdrawn

Federal income tax rules

✓ Non-qualified withdrawal of <u>earnings</u> are taxable to ***"distributee"*** at ordinary federal tax rates plus 10% penalty

- **Hypothetical Example:**

- $150,000 grows to $225,545 over 7 years @ 6%
- A $50,000 withdrawal for <u>***non-qualified expenses only***</u> =

$150/226K x 50 = $33,253 ROP = no tax

$16,747 earnings @ 12% tax rate = $2,010

x 10% penalty <u>= $1,675</u>

Total federal tax and penalty = $3,685 (7% of W/D)

NEVER Net Investment Income Tax On Withdrawals!

FINANCIAL EXPERTS NETWORK

Federal income tax rules

✓ Note: Re **Disabled Beneficiaries** -Since 2017 Tax Law Changes through 2025:

First $15,000 annually required for disabled child (<26 y.o.) – Transfer from the 529 Account (tax-free) to 529A/ABLE account, then use tax-free for:

education	housing
transportation	employment training and support
assistive technology	personal support services
health prevention/wellness	financial management and admin. services
legal fees	oversight and monitoring
funeral & burial expenses	other expenses approved by the IRS

FINANCIAL EXPERTS NETWORK

What are the potential gift/estate tax benefits?

- Contributions to a 529 account are completed gifts to designated beneficiary
- Apply gift tax credits: $15,000 - single/$30,000- joint annual gift tax exclusion
- Apply five years' worth of annual exclusions (up to $75,000/$150,000 for joint filers) at once* (File IRS Form 709)
- Unified/Lifetime Gift Tax Credits per person are also available ***($11.58M[1]) = very generous gifting opportunities***

Funding each 529 account = Gifting to the D.B.

Gifting = removes the asset from the donor's taxable estate

17 States & DC have a separate estate and/or inheritance tax - ACTEC

$68T of wealth is to be transferred over next quarter century – Cerulli Associates Report Nov 2018

*The Donor must be alive on January 1 of the year for which they claim such annual exclusion or that portion of the contribution must be added back to the Donor's taxable estate. 1- expires 2025 & reverts back to 2017 level, as adjusted.

Maximum funding a 529 account

An example:

John and his wife consider funding one 529 account with their sole grandchild, ***baby wonderful***, as the Designated Beneficiary, in 2020:

Using their annual exclusion:

$15,000 x 5 (2020-2024) x 2 =	$150,000

Using a small % of their ULGTE:

$175,000 of $11.58M (leaves each $11.4M) x 2 =	<u>$350,000</u>
Just 1 529 account funded, at once, free of gift tax	**$500,000**

FINANCIAL EXPERTS
NETWORK

Maximum funding a 529 account

If they did invest in 2020 and died 7 years later in 2026*, their *heirs* (not ***baby wonderful***) inherit either:

With 529 accounts	Taxable account in taxable estate
$751,815 (full account) with **no** estate taxes due	**$396,910** after 40% federal estate tax* of $264,607

= **$354,905 more passed on** after 7 years on original $500,000 invested in just 1 account

* Hypothetical tax rate based on maximum federal estate tax of 40% as of 2020 but with no state estate tax

What about UGMA/UTMAs?

- Income > $2,200 is taxed at the parents' tax rate
  - Applies to students for up to age 24 for f/t students[1]
- ✓ **Solution**: Invest UGMA/UTMA (cash) in a 529 plan[2]
  - Tax on earnings = 0% rather than onerous trust rate
  - Already gifted: not subject to annual gifting amount

[1] Applies only to children whose earned income is not > one-half of the amount of their support.
[2] UGMA/UTMAs are irrevocable and one cannot change such beneficiary. 529 plans may only accept cash. In order to invest assets from an UGMA account into a 529 plan, the account owner may have to sell assets in the UGMA account, pay taxes on the gains, if any, and then transfer the proceeds to the 529 plan. Whereas the tax advantages of 529 plan earnings attach to withdrawals for higher education expenses, expenditures from an UGMA account may be less restricted.

How may a trust benefit?

- Many trusts are set up to fund educational expenses
- Trusts are subject to high federal and state income tax rates

37% federal rate & 3.8% on earnings > $12,950; some states > 10%

- ✓ Trusts may invest in and own a tax-free 529 account(s)
- ✓ Irrevocable trusts may max funding an account for each beneficiary
- ✓ Trusts may take qualified withdrawals or carve out new accounts

Funding the 529 account

A $5,000 investment ?

- or a -

$500,000 investment?

Why would a client <u>**not**</u> choose to fund the 529 account?

- The client requires all invested assets for income
- They have all of their assets in qualified plans
- They believe they can net a higher return elsewhere
- ***The client does not really care for their child or grandchild***
- They don’t understand that they always maintain complete control over the account and they are unaware that <u>the penalty is 10% on earnings withdrawn</u> – not the full withdrawal!

MANAGING THE 529 ACCOUNT

- Accounts are typically "tapped" before retirement account
  - There is a need to access funds in shorter time span = less time to "recover" losses/underperformance
- Investment reallocation is restricted
  - Investment changes to account only 2x per year
- Rollovers - similar to IRAs – new plan transfers assets @ no cost, penalty or taxes if within 60 days or Trustee to Trustee
- Rollovers are <u>not</u> included in annual change limit

SELECTING A 529 PLAN

- Are you familiar with the underlying funds?
- Are there multiple investment choices?
  - How is the age-based portfolio structured?
- Are there forms required to adjust account or withdraw?
- Are there hidden fees/restrictions?
- Is there investment flexibility?
- What is the plan's net performance?
- What is the cost/value trade-off?

FINANCIAL EXPERTS
NETWORK

WHERE IS THE 529 INDUSTRY TRENDING TO?

The future of 529 plans in the advisor world is **not** bright

- Many advisors have determined to forego doing 529 business
  - Perception as small ticket, still mostly “check & app” at most firms
  - Investment reallocation is restricted - only 2x per year per account per tax law
  - Investment choices limited
  - Not available in an advisory account
  - Higher compensation or lower, as advisor seek, not available in 529 plans
  - Too confusing with uneven state tax treatment and different plan features

WHERE IS THE 529 INDUSTRY TRENDING TO?

The future of 529 plans in the advisor world **IS** bright

- More advisors are embracing doing more 529 business
  - True cost of education is "big-ticket" as 529s cover K-grad school + loans
  - Planning is growing in importance to advisor-client relationship
  - Investment choices have greatly expanded – many plans offer 30+ choices
  - Compensation on accounts adjusted in response to regulators and advisors
  - Many state tax benefits for contributing treatment and different plan features
  - **May 27: Morgan Stanley announces the first 529 plan on an advisory platform**

The views expressed in this material are the views of Savingforcollege.com and are subject to change without notice at any time based upon market and other factors.

All information has been obtained from sources believed to be reliable, but its accuracy is not guaranteed. There is no representation or warranty as to the current accuracy, reliability or completeness of, nor liability for, decisions based on such information and it should not be relied on as such.

This information may contain certain statements that may be deemed forward-looking statements. Please note that any such statements are not guarantees of any future performance and actual results or developments may differ materially from those discussed. There is no guarantee that investment objectives will be achieved or that any particular investment will be profitable. Past performance does not guarantee future results.