

529 Savings Plan



NEW FLEXIBILITY FOR 529 PLANS

In 2009, you can change your investment allocations twice.

The IRS has given owners of 529 plans the freedom to revise the asset allocations of their accounts twice during 2009.¹ You could only previously do this once per year.

Basically, the once-a-year rule was put in place to prevent people from day trading their college savings. In 2008, this rule had a downside: many parents and grandparents who had invested in stock-burdened mutual funds could only sit and watch as their 529 plans took big hits.

Decision Time for Parents. The new IRS ruling may prompt a big shift in asset allocations. Many 529 account holders who had the bulk of their assets in equities may be eager to move those assets into money market funds, CDs and other risk-averse investments. (529 plan owners are commonly urged to allocate assets more cautiously as account balances grow and children get closer to that first day of college.) Other account holders may do that and move their money into another state's plan.

The big decision is whether to move the money into investment vehicles with lower risks or to leave the funds alone and hope for a market rebound. The IRS will let you change your mind twice in 2009 – so if you change to a conservative allocation and you want to change back, you have permission to do so.

Options to Think About. If your 529 account doesn't yet contain assets to pay for the entirety of college expenses across four years, you could earmark the money for a child's last two or three years of college. That may buy time for your account as the markets recover.

Another option, if your income permits it and your child is ready to enter college: the Hope Credit. That's a federal tax credit of up to \$1,800 a year, and it can help you cover the cost of tuition and fees in your child's freshman and sophomore years. In 2009, a taxpayer's MAGI will determine the reduction in the amount of the Hope Credit. Reductions start at the \$50,000 level for individual filers, and the \$100,000 level for joint filers.²



By the way, things may change with the Hope Credit. The economic stimulus package recently proposed by House Democrats (which stands a real chance of being signed into law by President Obama) would simplify the Hope Credit and Lifetime Learning Credit into one \$2,500 education credit. The House Ways and Means Committee has proposed making this \$2,500 credit available

to more taxpayers by raising the income limits on eligibility; as planned, part of the \$2,500 credit would even be refundable.³

If your AGI is too high to claim a Hope Credit, you might be eligible to deduct up to \$4,000 of tuition expenses.⁴ And lastly, if your 529 plan is under water, you do have the option of cashing out without penalties or federal taxes (but you may have to pay state taxes) and possibly claiming the loss as a miscellaneous itemized deduction.⁵

Time to Talk 529? With the freedom to change your mind twice this year, you may be considering reallocating your 529 plan assets once or twice in response to the market. Consult with your financial advisor to determine if this is wise in 2009.

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Citations

¹ irs.gov/pub/irs-drop/n-09-01.pdf [1/13/09]

² money-zine.com/Financial-Planning/Tax-Shelter/Income-Tax-Changes-2009/ [12/29/08]

³ marketwatch.com/news/story/tax-breaks-aimed-home-buyers/story.aspx?guid={561E47C6-5528-4C5F-93C8-895F06BB47FB}&dist=msr_1 [1/15/09]

⁴ usatoday.com/money/perfi/columnist/block/2009-01-05-529-college-savings-plans_N.htm [1/5/09]

⁵ online.wsj.com/article/SB123068308029744121.html?mod=googlenews_wsj [12/31/08]