THE COMPASS CHRONICLE

Highlighting important wealth management issues *Fall 2010*

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A client-focused wealth management firm dedicated to providing objective advice to individuals, families, and corporate retirement plans.

Our wealth management services include:

- Investment Management and Consulting
- Retirement Planning
- Education Funding
- Gift Planning

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Saving For College

An Overview for Parents and Grandparents

As we head into the colder months and high school juniors begin to narrow their college choices, many of their parents will begin to feel the pressure of the forthcoming school bills. Even if you have years yet to save before your children or grandchildren reach college age, the cost of a college education can be daunting.

For a baby born today, the cost of attending a four-year private university is projected to be $445,000 on average, excluding textbooks, supplies, and transportation, based on six percent inflation for today's college costs as provided by the College Board. In order to fully meet that cost, you would need to save over $900 each month from the child's birth until they reached eighteen, assuming an eight percent annual return in a tax-free investment vehicle.

While many children may receive loans, grants, scholarships, and work-related income to offset some of these projected costs, the monthly savings necessary can be meaningful. Based on a study recently released by Fidelity Investments, parents, on average, are projected to meet only sixteen percent of their children's college expenses from savings.

Fortunately, several savings vehicles exist to meet educational costs. They generally differ based on:

1. the extent to which the donor can control the assets in the account;
2. the tax status of the account; and
3. the impact each type of account has on receiving financial aid.

UTMAs

Long before the now popular Section 529-type plans became available, Uniform Gifts to Minors Act (UGMA) accounts tended to be the savings vehicle of choice for children. Ultimately, UGMAs were replaced by Uniform Transfers to Minors Act (UTMA) accounts, which allow an adult (custodian) to control the account for the benefit of the child (beneficiary).

However, once the child reaches the age of majority (21 for a Massachusetts UTMA) the assets in the account are owned by the child, who can then spend the assets as they wish. Another drawback of UTMAs is that they count as an asset of the child for federal financial aid purposes, which reduces possible aid relative to assets held in the parent's name. UTMAs do not have contribution limits and taxes may be incurred depending on the beneficiary's age and the investment income earned on the account.

Education Savings Accounts

Education Savings Accounts (ESAs) allow investments to grow and be withdrawn tax-free for qualified educational expenses at private primary and secondary schools, as well as colleges. ESAs have seen limited usage, however, due to eligibility requirements and annual contribution

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limits. To qualify to contribute to an ESA, a married couple filing jointly must have a modified adjusted gross income of less than $190,000. For those who are eligible, you are limited to a maximum annual contribution of only $2,000, restricting the benefit of this savings vehicle. ESAs are considered an asset of the parent (or whoever established the account) for federal financial aid purposes.

Section 529 Plans

Section 529 plans, named after a section of the Internal Revenue Code, are now the dominant savings vehicle for college expenses and are offered by all fifty states, the District of Columbia, and a private college consortium. No income limitations exist for contributors and lifetime contributions for some plans are in excess of $300,000 (and you may have more than one 529 account per beneficiary). Like ESAs, Section 529 accounts are considered the donor's asset and are tax-free vehicles as long as they are used for qualified educational expenses.

Section 529 plans come in two flavors: savings plans and prepaid tuition plans. With a savings plan, the donor selects from the available investment options, which are subject to the variability of the market's returns. A prepaid tuition plan is just that: it allows a donor to prepay a beneficiary's tuition at predetermined prices for use in the future. State-sponsored prepaid tuition plans are usually available to in-state residents only. They are usually best-suited for those who will attend one of the participating colleges.

In Massachusetts, the savings plan, the U.Fund, is managed by Fidelity Investments, whereas the U.Plan is the state's prepaid tuition plan. For parents or grandparents who are interested in establishing a college savings plan, we first review whether their home state plan offers a tax deduction or other tax benefit for contributions (Massachusetts, for example, does not offer any tax benefit for making contributions to the U.Fund or U.Plan). If no tax benefit is offered for the home plan, our counsel is to venture beyond the state's offerings and pick the best plan available nationwide.

Other savings vehicles can be used for educational expenses, such as U.S. savings bonds, trusts, and life insurance, each with different implications for control, taxation, and financial aid. However, we have focused on the most prevalent options used by parents and grandparents in this article.

COMPASS Wealth Management offers its advice and assistance in opening Section 529 and Education Savings Accounts to clients free of charge. If we may be of assistance, please contact our office.

Buffet On Gold

"You could take all the gold that's ever been mined, and it would fill a cube 67 feet in each direction. For what that's worth at current gold prices, you could buy all—not some—all of the farmland in the United States. Plus, you could buy 10 Exxon Mobils, plus have $1 trillion of walking-around money. Or you could have a big cube of metal. Which would you take? Which is going to produce more value?"

Warren Buffet

U.S. Competitiveness Slips

According to *Rising Above the Gathering Storm, Revisited,* the National Academies (the National Academy of Sciences, National Academy of Engineering, and Institute of Medicine) note that the competitiveness of the United States is under serious threat. Their assessment is that U.S. competitiveness has worsened in the five years since their inaugural report was issued.

Since our lead article this issue focuses on education funding, here we highlight a few of the education-related factoids from *Rising Above the Gathering Storm, Revisited:*

- The average U.S. K – 12 student spends four hours per day in front of a television.
- The United States ranks 48th in the quality of mathematics and science education, according to the World Economic Forum.
- Among industrialized countries, the U.S. ranks 20th in its high school completion rate and 16th in its college completion rate.
- For the first time in 2000, foreign students outnumbered U.S. students studying the physical sciences and engineering in United States graduate schools.
- Nearly one-half (49%) of U.S. adults do not know how long it takes for the earth to revolve around the sun.

"To buy when others are despondently selling and to sell when others are avidly buying requires the greatest fortitude and pays the greatest rewards." (aka buy low, sell high)

Sir John M. Templeton