

# Money 2000

University of Wisconsin-Extension

Family Living Programs

*and Beyond*

## Saving for college — Which plan to choose?

New tax laws encourage saving for college.

All 50 states now offer a 529 State College Savings Plan. Recent tax law changes make these plans even more attractive — funds used for qualified higher education expenses are exempt from federal taxes.

In addition, 23 states also offer state tax incentives. Wisconsin provides residents a state income tax deduction for up to \$3,000 per dependent for annual contributions to its plan.

You don't have to contribute to the plan in your state. Anyone may contribute to a 529 plan — you could live in New Mexico and contribute to a plan based in Maine for your grandchild in Oregon who wants to go to school at Michigan State.

And if you are planning on going back to school, most plans will even allow you to set up a 529 plan for yourself.

**EdVest** is Wisconsin's official 529 plan. With EdVest, your money grows free of Wisconsin state and federal taxes, and withdrawals for qualified expenses are also tax-free.\* Plus, Wisconsin residents receive a state tax deduction of up to \$3,000 per dependent per year.

You can choose from a number of investment options professionally managed by Strong in partnership with the State Treasurer's Office.

### 529 plan advantages:

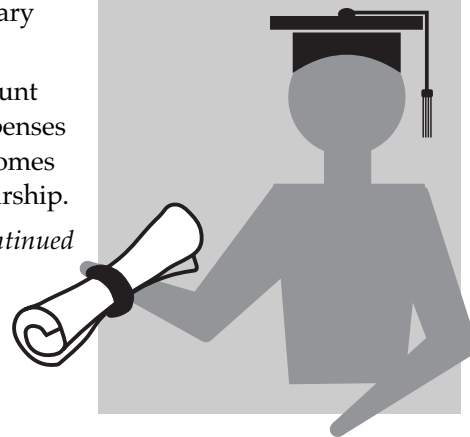
- High contribution limits — up to \$246,000 per account in Wisconsin
- Tax-deferred growth, tax-free withdrawal for qualified expenses
- Most plans have no age or income limitations for participation.
- The assets remain in your control as account owner. You decide when distributions are made and what the funds will be used for.
- Most plans allow you to change beneficiaries. You can change the beneficiary to a cousin, in-law or other individual directly related to the beneficiary.
- Funds may be used at any accredited college or university in the country and some foreign schools.
- You can rollover funds from one state's 529 plan to another:
  - once every 12 months, and
  - upon a change in the beneficiary for an account.
- No penalty is charged if the account cannot be used for education expenses because the beneficiary dies, becomes disabled, or gets a tax-free scholarship.

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# NEWS

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**To learn more  
about Wisconsin's  
529 plan, visit the  
Web site  
[www.edvest.com](http://www.edvest.com)  
or call toll-free  
(888) 338-3789  
to speak with one  
of EdVest's  
College Planning  
Specialists.**



\* As signed into law, the recent federal tax law changes are set to expire after December 31, 2010. Future legislation may extend or repeal these changes.

**Withdrawals from Education Savings plans are tax-free when used for education expenses.**

**Saving for college, *continued***

### **529 plan disadvantages:**

- Funds used for non-approved educational expenses are taxed as well as being subject to a 10 percent penalty on the earnings, not the principal.
- Inflexibility — All plans offer a limited number of investment options, which you can change once per year. (This may be viewed as an advantage by those who prefer not to make investment decisions.)
- Programs differ substantially from state to state. And rules continue to change, which can be confusing.

### **Choosing a 529 plan that best fits your needs**

Here are some questions to answer (use the resources below).

Does the plan offer good investment options?

How much is required for initial contribution? For subsequent investments?

What is the return on your investment? (Some plan funds are too new to have much of a track record.)

What are the expenses/fees involved?

How have others rated the plans?

How does the state treat tax breaks?

**For more information** on 529 plans, call the College Savings Plans Network toll-free: (877) 277-6496

**[www.collegesavings.org](http://www.collegesavings.org)**

BusinessWeek Guide to College Savings Plans

**[www.businessweek.com/magazine/content/02\\_10/b3773602.htm](http://www.businessweek.com/magazine/content/02_10/b3773602.htm)**

Internet Guide to 529 Plans

**[www.savingforcollege.com](http://www.savingforcollege.com)**

Internet access is available at many public libraries or other public places in your community.

### **Education Savings Accounts (ESAs)**

Coverdell Education Savings Accounts (previously Education IRAs) are the other option for saving for children's educational expenses.

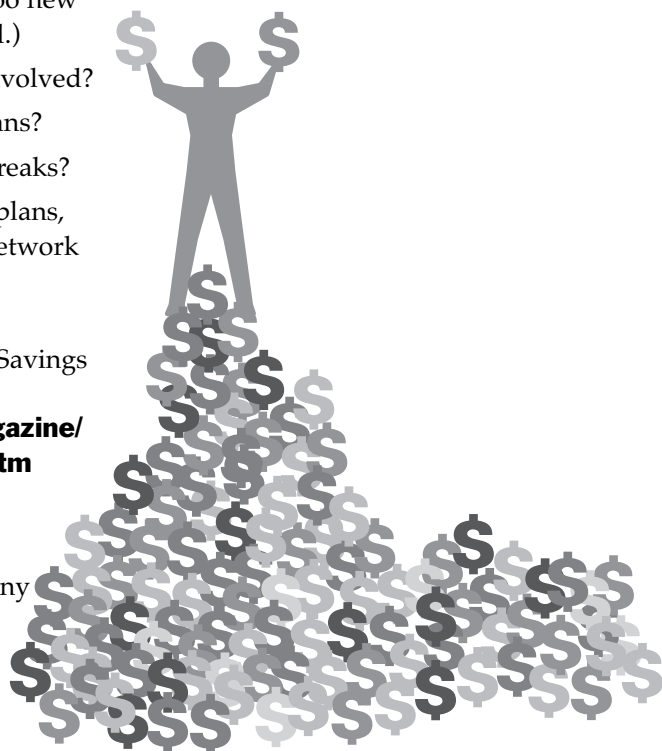
The annual contribution limit is now \$2,000 per child, up from the previous \$500 limit. Like 529 plans, withdrawals are tax-free when used for qualified education expenses.

#### **ESAs offer some benefits not available with 529 plans:**

- Unrestricted investment choices — You can decide how to invest the money, rather than being limited to the age-based asset allocation of most 529 plans.
- Funds can also be used for primary and secondary education expenses.

For more information, see the Guide to Coverdell Education Savings Accounts:

**[www.savingforcollege.com/coverdell](http://www.savingforcollege.com/coverdell)**



# Consumer debt is rising, bankruptcies increasing

Research by the Federal Reserve indicates that household debt is at a record high relative to disposable income. In 2001, total consumer debt rose to a record 16.3 percent of disposable personal income.

Some analysts are concerned that this unprecedented level of debt might pose a risk to the financial health of U.S. households. A high level of indebtedness among households could lead to increased household delinquencies and bankruptcies. And that could threaten the health of lenders if loan losses are greater than anticipated.

In fact, bankruptcy filings for the 12-month period ending in March 2002 hit a record of more than 1.5 million.

The total number of new bankruptcies filed during the first quarter of calendar year 2002 (Jan. 1 to March 31) rose 3.3 percent, increasing from 366,841 to 379,012 over the same period a year ago. The new mark is the highest first quarter ever, and the second highest 3-month figure in history.

In Wisconsin, there was one bankruptcy filing for every 90 households, ranking the state 35th nationally. Perhaps most alarming is the increase in state filings for the 3-month period ending March 31, 2002, compared to the identical period in 2001. The Western District of Wisconsin ranked fifth highest in the country with an increase of 16.3 percent.

## Bankruptcy definitions

**Chapter 7** of the Bankruptcy Code is available to both individual and business debtors. Its purpose is to achieve a fair distribution to creditors of the debtor's available non-exempt property. Unsecured debts not reaffirmed are discharged, providing a fresh financial start.

**Chapter 11** of the Bankruptcy Code is available for both business and consumer debtors. Its purpose is to:

- rehabilitate a business as a going concern, or
- reorganize an individual's finances through a court-approved reorganization plan.

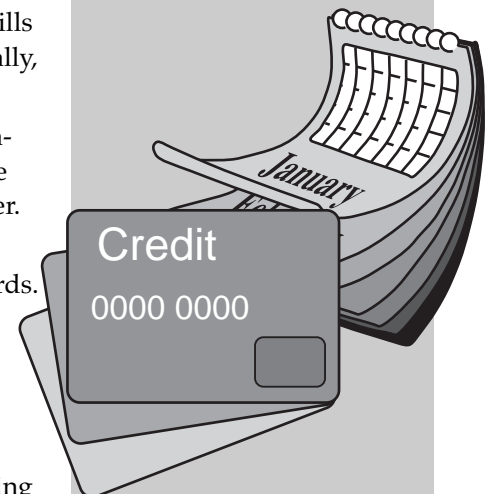
**Chapter 12** of the Bankruptcy Code is designed to give special debt relief to a family farmer with regular income from farming.

**Chapter 13** of the Bankruptcy Code is available for an individual with regular income whose debts do not exceed specific amounts. This is typically used to budget some of the debtor's future earnings under a plan through which creditors are paid in whole or in part.

## General budgeting tips

- Make impulse buying difficult — leave checkbooks, credit cards home.
- Automate your savings — set up deposits from your paycheck.
- Use a calendar to show when regular bills are due.
- Set aside money each month for bills that are due quarterly, semi-annually, or yearly.
- Budget for fun items, such as vacations and recreation. Provide some fun money for each family member.
- Create an expense item in your spending plan to pay off credit cards.
- Pay off the highest-interest rate credit cards first.
- Don't use credit cards until the balance is paid off.
- Remember, just the act of identifying your expenses is extremely valuable.

**Time to reduce your debt? Contact your county UW-Extension Office for a PowerPay Analysis to learn how you can pay down your debt faster and save hundreds.**





**Now might be a good time to refinance your student loans.**

# Student loan rates drop

Interest rates on many federal education loans are now at all-time lows. Since July 1, the new rate for student Stafford loans is 4.06 percent, and 4.86 percent for parent PLUS loans — down nearly 2 percent from last year.

If you have a variable rate loan, you will automatically owe less this next year. But you could save even more by consolidating to a new fixed rate loan to lock in these new lower rates.

For more information, check with the U.S. Department of Education's Direct Consolidation Loan Calculator: [www.ed.gov/DirectLoan/ConsolCalc/dlentry3.html](http://www.ed.gov/DirectLoan/ConsolCalc/dlentry3.html) or call toll-free: (800) 557-7392

Other useful Web sites: [loanconsolidation.ed.gov](http://loanconsolidation.ed.gov) [www.salliemae.com/apply/borrowing/smartloan.html](http://www.salliemae.com/apply/borrowing/smartloan.html)

*Money 2000 and Beyond:* [www.uwex.edu/ces/money2000](http://www.uwex.edu/ces/money2000)

## What about financial aid?

Concerned that contributing to a 529 plan could mean your child wouldn't be eligible to receive aid? It's still not clear how schools are going to handle 529 plan money. In most cases, it appears schools will treat this money as the parent's investment, not the child's.

The following formula is often used to determine parents' assets for calculating financial aid:



$$\begin{aligned} & \text{Net worth of parents' investments* - (minus) Protection Allowance**} \\ & = \text{(equals) Discretionary net worth x 12\%} \\ & = \text{(equals) Parents' expected contribution} \end{aligned}$$

\* **Investments** include real estate, trusts, money market and mutual funds, certificates of deposit (CDs), stocks, options, education savings accounts and 529 plans — all at the market value as of the day completing financial aid forms.

Investments not included: home, cash savings, checking account, cash value of life insurance, and retirement plans such as 401(k) plans and IRAs

### \*\* Protection allowance

Based on age of older parent

Age	Allowance for 2 parents	Allowance for 1 parent
45	\$42,400	\$24,400
50	\$48,300	\$27,200
55	\$55,300	\$30,800
60	\$64,100	\$35,000
65+	\$75,100	\$40,400

**Note:** *EdVest funds are not included when calculating Wisconsin state financial aid eligibility for Wisconsin residents.*

**University of Wisconsin-Extension** provides equal opportunities and affirmative action in employment and programming, including Title IX and ADA requirements. *Money 2000 and Beyond News* is written and compiled by Linda Boelter, CFP, family financial management specialist, UW-Extension. Thanks to Mary Fran Lepeska, Jane Hojan-Clark and Marty Olle for helping prepare this issue.

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