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Early college planning for a growing family

With the excitement of building your family comes the important task of updating your financial planning goals. Disciplined saving now means having options later.

"Having children brings new beginnings and a whole new set of goals for the future. It's important to work with a financial advisor to craft a comprehensive plan that considers all of life's possibilities."

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Raising a family can lead to some complex financial planning challenges. At the same time, saving for the cost of education has never been more important.

The good news is that it's never too early to start planning. Saving as much as possible early on can help investors benefit from the power of compounding over time. How to save — choosing among various types of accounts and investments — also affects outcome, and families should consider seeking professional advice on college planning.

Infants and preschool

Some parents start saving even before a baby is born. With a 529 savings plan, for example, parents may establish an account using their own Social Security number and name their child as the beneficiary at a later date.

Starting early allows the account to invest through multiple market cycles. Parents may want to begin with a more growth-focused investment strategy to take advantage of a far-off horizon. Saving with a 529 plan, even when a child is very young, will give you the flexibility to use funds to pay for K-12 tuition (up to $10,000 per student annually), or a qualified apprenticeship, as well as college costs.

This may also be the time to get documents in order:

- Establish a will or trust and a health care proxy.
- Make necessary changes or additions for beneficiaries to your insurance, medical plans, and other benefits.
- Review your retirement plans and other accounts to see if changes are needed.

Elementary and middle school (ages 5–13)

As the family grows, establish additional savings accounts that focus on the age and goal of the child. If more than one child will be in college at the same time, be sure to include this factor in your planning.

- In addition to saving for education, continue to pay off debt, maintain emergency savings, and save for retirement.
- Consider and revisit the time horizon and investment options for your short-term and long-term goals.
- Explore some college savings calculators to get a sense of how much to save.
- Ask grandparents and other family members to consider contributions to the college account for gift-giving/ milestone occasions.
- Consider utilizing a variety of savings vehicles to help you meet your objectives. Explore prepaid tuition plans that lock in tuition rates at in-state public colleges. A Roth IRA may be used to save for both education and retirement.

Know your options for saving on behalf of your child(ren)

Guidance from a professional financial advisor can be a key resource for identifying the investment choices and savings strategies that are appropriate for your goals.

	529 PLAN	CUSTODIAL ACCOUNT (UGMA/UTMA)	ROTH IRA
Control of assets	Owner of account, who may change beneficiary at any time	Beneficiary becomes owner at age of majority	Owner of account
Federal tax benefits	After-tax contributions grow and distribute tax free for qualified college expenses (or up to $10,000 per student per year in K–12 tuition)*	After-tax contributions. First $1,250 in unearned income not taxed. The next $1,250 taxed at child's tax bracket, and excess earnings are taxed at the parent's marginal tax bracket	Contributions withdrawn without tax and penalty for any reason. Withdrawal of account earnings for higher education expenses not subject to an early withdrawal penalty§
Annual contributions	May front-load up to five years' worth of gifts at one time ($85,000 for individuals/ $170,000 for married couples)	$17,000 for individuals/ $34,000 for married couples	$6,500 ($7,500 for taxpayers age 50 and over). Must have taxable compensation, and the limit is phased out based on income
Federal financial aid treatment†	Parent asset (favorable)	Student asset (less favorable)	Not counted as asset
Allowed use of funds‡	Tuition, room and board, qualified apprenticeship programs, and other qualified expenses at any accredited college. Up to $10,000 annually per student for K–12 tuition, and $10,000 in total to pay back student loans	Funds must be used on behalf of the minor	Can be used for retirement, education, and up to $10,000 for first-time home purchase

* Federal tax-free distributions (taken after December 31, 2017). Earnings may be subject to state income taxes in certain states.
† Other types of financial aid calculations may differ from FAFSA.
‡ Withdrawn earnings subject to federal tax and 10% penalty if not used for qualified expenses.
§ Roth distributions are free from taxes and penalty if the account is held for 5 years and there has been a qualifying event such as the account owner turning age 59½.

Planning considerations

- Consider a two-bucket strategy. Establish a 529 savings plan and contribute to an age-based investment option for college costs, and select another investment option within the plan that is more liquid for elementary or high school tuition.
- For 2023, the gifting limit is $17,000 annually for individuals and $34,000 for married couples.
- A special provision of 529 plans allows contributions equal to five years' worth of gifts to a single beneficiary in a single year without triggering the federal gift tax.
- While taking distributions for early education is now an option for 529 plans, savings benefit most from the compounding of earnings over time.

Eighty-five percent of high school students plan to work while in college and 62% plan to cut costs by living at home. According to a recent survey from the College Savings Foundation, 51% of all high school students are currently working to earn money for their higher education.

Read Putnam's investor education piece, "Four-year action plan to prepare for college," to learn about the key college preparation activities for parents and students throughout high school.

Helping children understand saving

Teaching children about saving and other finance basics can begin at an early age.

Preschool (ages 3–5)

Consider talking with young children about the financial value of items. If they break a toy, explain the difference between simply buying a new one or fixing the toy and putting the replacement cost toward something else.

Elementary and middle school (ages 5–13)

Introduce the concept of long-term savings goals. Consider setting up a piggy bank with separate sections for saving, spending, and donating to people in need.

Establish a "matching program." Encourage your children to save at least half of the money they receive for gifts, and then match those contributions. Take your children to the bank to open a savings account, and keep them updated as their savings grow.

Learn more about college savings at putnamwealthmanagement.com

Resources can help you get started

It's never too early to develop a comprehensive financial plan to fund an education. College costs have risen consistently over decades, and saving is not always easy, particularly with competing financial priorities, such as daily expenses, mortgages, and retirement savings. Guidance from a professional financial advisor can be a key resource for identifying the investment choices and savings strategies that are appropriate for your goals.

Putnam resources

putnam.com/individual/college-savings/support

- "Four-year action plan to prepare for college"
- Putnam college savings calculator
- "Strategies to make the most of college savings"
- "Why a college student needs a health-care proxy"

Additional information

- *Raising Financially Fit Kids*, by Joline Godfrey
- Federal Student Aid (studentaid.gov)
- *U.S. News & World Report* best colleges list
- Scholly — information on scholarships (myscholly.com and mobile app)
- College Board (collegeboard.org)
- IRS publication 970, "Tax Benefits for Education" — information on college savings accounts, tax credits, and tax deductions (irs.gov/publications/p970)

Chris Hennessey is Professor Emeritus of Law at Babson College and member of the Putnam Investments Business Advisory Group. His opinions do not necessarily reflect those of Putnam Investments. This information is not meant to be tax and/or legal advice.

Please consult with the appropriate tax or legal professional regarding your particular circumstances before making any investment decisions. Putnam does not provide tax or legal advice.

Putnam 529 for America is sponsored by the State of Nevada, acting through the Trustees of the College Savings Plans of Nevada and the Nevada College Savings Trust Fund. Anyone may invest in the plan and use the proceeds to attend school in any state. ***Before investing, consider whether your state's plan or that of your beneficiary offers state tax or other state benefits such as financial aid, scholarship funds, and protection from creditors that may not be available through Putnam 529 for America.*** *If you withdraw money for something other than qualified higher education expenses, you will owe federal income tax and may face a 10% federal tax penalty on earnings. Consult a tax advisor.*

You should carefully consider the investment objectives, risks, charges, and expenses of the plan before investing. For an offering statement containing this and other information about Putnam 529 for America, call Putnam's dedicated 529 hotline at 1-877-PUTNAM529. You should read the offering statement carefully before investing. Putnam Retail Management, principal underwriter and distributor. Putnam Investment Management, investment manager.