

BEST PRACTICES IN Compensation & Benefits

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How a 529 Plan Helps Employees Save Money

Since the early 1980s, college education costs have been rising at double the rate of inflation. It is no wonder that almost 50 percent of parents with children under age 18 indicate their number one financial goal is to ensure their children go to college.

A 529 plan is a state-sponsored college savings program that can help your employees save in many ways:

- **Tax-free earnings:** Although contributions are made on an after-tax basis, the interest your employees earn grows on a tax-free basis.
- **Tax-deductions:** Depending on the state plan your employee chooses, contributions may be partially or fully deductible from state income taxes.
- **Tax-free withdrawals:** Qualified withdrawals from 529 plans are free from federal income tax if used for eligible educational expenses, which include tuition, books, and room and board. In many cases, these qualified withdrawals are also state tax-free.
- **Savings discipline:** When 529 plan contributions are made via payroll deduction, it is "forced savings." Payroll deductions allow employees to save money for important financial goals each pay period instead of trying to save after paying for the rest of their monthly expenses.
- **No "use it or lose it" provision:** If the employee's child or grandchild does not go to college, they can change the beneficiary to another family member, use the money for their own educational expenses, or take a nonqualified withdrawal, which is subject to income taxes on contributions and a 10 percent penalty on earnings.

- **No income limits:** Anyone can participate.
- **Professionally managed assets:** Employees benefit from investing money in professionally managed accounts, possibly resulting in a higher yield than if the employee tried to manage the money on their own.
- **Dollar-cost averaging:** By purchasing investments regularly over the course of a year, employees are able to buy fewer shares when the price is high and more shares when the price is low, often resulting in a lower average cost per share.

A 529 plan can be a great way to help your employees save money. It is also recommended that you provide employees with unbiased investment education and guidance on how to coordinate investing in their retirement plans and the 529 plan. Vendor presentations many times focus solely on the benefits of participation and do not provide your employees with education so they can choose the right investments based on their time horizon and risk tolerance.

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