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PRIVATE WEALTH

Education Funding 101: Common Questions and Funding Strategies

College education costs are at record levels, and private primary and secondary school tuitions are not far behind. Finding the funding strategy that secures your children's education and supports your tax and estate planning objectives can be daunting. Whether you are a grandparent, parent or other family member, here are answers to some common questions about funding education expenses.

When is the best time to start?

It is never too early to start funding for a child's education. Identifying education goals and determining the best funding options for your family are part of a comprehensive Goals-based Wealth Review. Your Glenmede Relationship Team can help you get started.

Who can contribute?

Anyone can contribute to a child's education costs. Contributors should discuss their desire to help with the parents to coordinate the most effective way to make a gift and avoid adverse tax consequences for themselves, the parents or the child. What types of funding strategies are available? There are many ways to fund education expenses. In our experience, the most common approaches include:

Pay as you go

For parents with adequate means, paying education expenses directly to the school from current cash flow is a simple approach that leaves savings, investment and retirement accounts intact. It requires a reliable source of future cash flow sufficient to cover the rising cost of education for all children at every stage of the educational lifecycle. Parents who want to pay as they go should start planning early and work closely with their Glenmede Relationship Team to align time horizons with funding goals, project future costs and revisit assumptions whenever their circumstances change.

A few states allow residents to pay future college tuition costs at today's rates through a 529 prepaid tuition plan. The number of eligible colleges in those states is limited. If your state offers a 529 prepaid tuition plan and you are sure your child will attend a qualified college there, this type of plan can deliver significant savings.

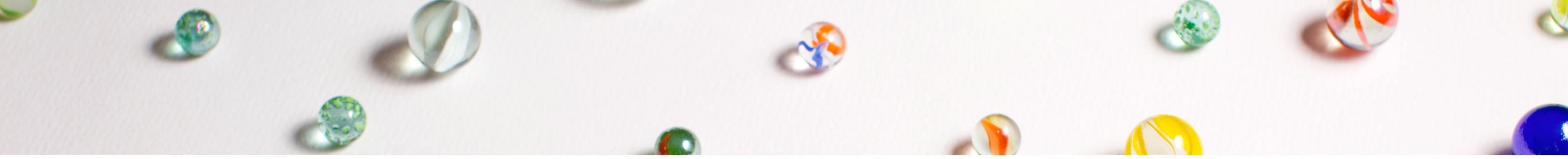
Preplanned savings

In today's low-interest-rate environment, interest bearing savings and investment accounts have given way to tax-advantaged state-sponsored tuition plans. The key to a successful savings strategy remains the same: Start early to reap the benefits of accumulated earnings.

529 qualified tuition plans

529 plans are readily accessible tax-advantaged savings plans designed exclusively for education expenses. Available in every state, anyone can establish an account for a named beneficiary, and the account can be rolled over tax-free to another family member if the beneficiary dies or does not use all the funds. Contributions qualify for the annual gift tax exclusion and may not be subject to the generation skipping transfer tax.

Income in 529 plans accumulates tax-free, and distributions are not taxed if used for qualifying education expenses, including tuition, some room and board, and books and fees



for college, vocational school, some apprenticeships and graduate school. Tuition payments up to $10,000 per year at a qualifying public, private or parochial K-12 school or home school are allowed, as are limited distributions to pay qualified student loans.

To maximize tax-free earning, 529 plans should be started as soon as the child is born and has a Social Security number. Investment and distribution options are not as flexible as some available through trust strategies, and assets in 529 plans are not included in the parent's or grandparent's estate for federal tax purposes. Finally, death may prevent parents or grandparents from fully funding a child's account or funding all children equally.

UGMAs/UTMAs

A state's Uniform Gifts to Minors Act or Uniform Transfers to Minors Act custodial accounts used to be popular ways to fund a child's education. Since the advent of education-specific, tax-advantaged 529 plans, UGMAs and UTMAs have fallen out of favor for education funding. If parents want to be sure gifted assets are used only for education, or if a child wants to qualify for financial aid, a UGMA or UTMA may not be the best choice.

Grandparent gifts

Supporting a grandchild's education is one of the most tax-efficient and satisfying ways to transfer wealth to future generations. Grandparents can use many of the same education funding strategies that parents use, but the tax and financial implications for both the grandparent and the grandchild may be different. Grandparents can also take advantage of complex estate planning strategies that facilitate wealth transfer to grandchildren.

For those making direct gifts or setting up 529 plans for grandchildren, predeceasing the birth of a grandchild is a valid concern. It is important that your estate plan anticipates this possibility and has provisions in place to mitigate mortality risk and ensure all grandchildren are treated equally.

- ***Gifts to students***

  Grandparents can contribute to a grandchild's education by making a yearly gift of cash or securities up to the $15,000 per individual donor or $30,000 per married couple annual federal gift tax exclusion. However, gifts to a student could negatively affect their eligibility for financial aid. If that is a consideration, grandparents can make the gift directly to the parents, who are not required to report it as income on the Free Application for Federal Student Aid.

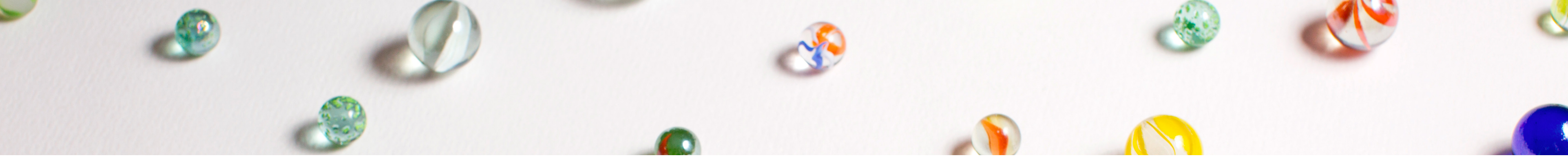
- ***Direct tuition payment to the school***

  Making a direct tuition payment of any size to your grandchild's school is an excellent alternative — or supplement — to a limited gift to the child. Direct tuition-only payments for pre-K through graduate school are not taxable gifts and do not count toward the lifetime gift exemption as long as they are made directly to a qualified "educational organization" as defined by the Internal Revenue Code. Some colleges reduce scholarships or aid by the amount of the grandparent's tuition payment. Before making a direct payment to a school, ask if it will affect your grandchild's eligibility to qualify for aid.

- ***Irrevocable trusts***

  Irrevocable trusts, whether grantor or nongrantor, multigenerational dynasty trusts and their hybrids are sophisticated estate trust planning vehicles that give grandparents tremendous flexibility to make tax efficient transfers of assets to one or more grandchildren. The assets can be used to fund education and other expenses. Each trust strategy has distinct estate and income tax advantages and drawbacks. All require careful coordination with an estate planning attorney to maximize the desired outcomes for the grantor and beneficiaries.

  For example, a Health and Education Exclusion Trust is tailor-made for grandparents who want to establish an irrevocable generation-skipping dynasty trust to fund qualified medical and K-through-graduate school educational expenses for grandchildren and their descendants. A properly structured HEET is most tax efficient for grantors who have exhausted their exemption from the federal GST tax and especially appropriate if the grantor is philanthropically inclined. In addition to "skip persons," such as grandchildren and more remote descendants, a HEET must have at least one charitable beneficiary and may have other "nonskip" beneficiaries.



The charity's interest should be significant and last for the duration of the trust. These requirements are generally met by providing the trustee with discretion to distribute income and principal to the charity — usually in an amount not less than 5% of trust assets — as determined annually on a stated date. The trustee may also distribute HEET assets directly to providers for education and health care expenses on behalf of a grandchild or other skip person without imposition of the GST tax.

Scholarships, grants, financial aid and loans

High-income families often assume they will not qualify for student financial aid, but that is not always the case. Many colleges, universities, and state, local and nonprofit organizations offer merit scholarships and grants to students who meet nonfinancial criteria. Colleges typically require a FAFSA as part of their scholarship and grant award process, so it pays to fill out one every year.

Loans are a common funding source, and some are less expensive than others. Low-interest home equity loans offer parents more competitive rates than government-sponsored or private education loans. Parents or grandparents who believe children benefit from sharing the financial burden of their education can extend an intrafamily loan at very low rates and with terms that support the values they want to reinforce.

Which strategy is right for you?

Finding the right education funding solution for your family is a complex undertaking. Many factors and options come into play, and often a combination of strategies works best. The most important thing is to start early. Your Glenmede Relationship Team can help you identify realistic education funding goals and evaluate the strategies that will best serve your family's educational and financial security for years to come.

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