WHY GIFTING EDUCATION IS A GREAT WEALTH STRATEGY

By: Janice Moore, CTFA, Senior Vice President, Private Client Advisor

These days a college education comes with a hefty price tag. For many parents, saving and paying for a child's higher education in our current economic environment is a growing challenge.

Perhaps it's one reason more and more Baby Boomers are giving education gifts for holidays and special occasions to help turn a child's dreams into reality. The majority of boomers who went to college place a high value on getting an education—and it's important to them to see that trend continue with future generations.

But the news is not all bad where college costs are concerned. For example, individuals who step up and help finance a child's education costs are able to pass along their wealth without having to pay gift and estate taxes.

The decision to use education gifting as a wealth strategy is personal and unique to each family situation—and it's not reserved for the ultra-wealthy. If you're interested in this win-win situation, here are three options you may want to consider.

WHAT DOES COLLEGE COST THESE DAYS?

According to The College Board's "Trends in College Pricing 2019," the average annual cost (tuition and fees, room and board, books and supplies, transportation and other expenses) for a private four-year school is $53,980. For public four-year in-state schools, the average annual cost is $26,590; for public four-year out-of-state institutions, the average annual cost is $42,970.[1] What's more, tuition often outpaces general inflation, increasing about 8% per year according to Finaid. That means the cost of college doubles every nine years.

PAY THE SCHOOL DIRECTLY

Under federal guidelines, tuition payments of unlimited amounts can be made directly to a college or university without triggering any gift taxes. You don't have to be concerned about the $15,000 annual federal gift tax exclusion either. This means you could pay $50,000 in tuition directly to the school and give a child $15,000 ($30,000 for a joint gift) each year under the exclusion limit.

Keep in mind, however, that direct payments can be applied only to tuition costs—other expenses such as room and board, fees, equipment, books, and other miscellaneous charges do not qualify.

The advantages of this option are twofold:

- By paying the educational institution directly, the funds will be spent on what you intended and not on expenses out of your control.
- It's a great way for you to get money out of your taxable estate. There are no benefits in the year the donation takes place, but it will lower the amount of your taxable estate.

CONTRIBUTE TO A 529 PLAN

Funding a 529 plan for a child's education is another alternative you may want to consider to help draw down your estate. The scope of 529 plans was greatly broadened by the Tax Cuts and Jobs Act tax reform legislation several years ago.

There are two ways you can contribute either a lump sum amount or smaller, regular amounts, for a child's education:

- Open a 529 account and name the child as the beneficiary (only one person can be listed as the account owner).
- Make contributions to a 529 account that has already been opened for the purpose of funding the child's education.

Perhaps the biggest advantage of a 529 plan is that you can front load it by making a single, lump-sum gift of up to $75,000 (based on the current annual gift exclusion of $15,000 per individual) You and your spouse can make a joint gift of up to $150,000 in the first year rather than spreading your contributions out over a five-year period. Not only is this amount five times the annual tax exclusion, you also avoid the federal gift tax. However, you cannot gift any other money to the child during this time period. Also, a 529 plan does not get as much money out of your estate as other options, because tuition is often a much larger amount than 529 funding limits.

There may be another good incentive for you to consider a 529 plan as a wealth strategy. With the passage of the federal tax reform legislation, the guidelines for qualified education expenses for 529 plans were expanded to include tuition contributions of up to $10,000 per year for grades K-12. These payments also do not trigger any gift taxes.

Keep in mind a child of any relative or friend can be the beneficiary of a 529 plan education gift. However, 529 savings plans are offered by each state—and the features and benefits can vary significantly. As you consider your alternatives for education funding as part of your overall wealth strategy, consult with your tax professional and financial advisor regarding the options, fees, and state tax implications.

GIFT CASH OR SECURITIES

If you decide to help with a child's education by gifting cash or securities, there are a few things you may want to think about before doing so. For example, if you give your grandchild a gift of more than $15,000 (or $30,000 for a married couple), it may trigger a gift tax and a generation-skipping transfer (GST) tax. One way to avoid this is to give the cash to the child's parent to save for your grandchild's education. Other alternatives may be more attractive to consider if you are concerned the adult child or parent may not handle your gift responsibly.

DO YOUR HOMEWORK

In addition to the strategies discussed above, there are many other education funding choices, guidelines, and rules to consider before you make a decision. It's important to consult with your tax professional and financial advisor to help you evaluate how various savings and investment options could impact your overall financial plan. Contact Commerce Trust Company today to explore a number of solutions for gifting education as a wealth strategy.

[1] Source: The College Board, "Trends in College Pricing 2019," Figure 1, https://research.college.board.org/pdf/trends-college-pricing-2019-full-report.pdf, November 2019.

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Jan is a private client advisor for Commerce Trust Company. She serves as a senior consultant and relationship manager providing clients with personalized objective advice and oversight across all of our services, including trust administration, financial advisory services, private banking, and investment management. Jan facilitates all aspects of relationship management for the client team, including administering complex trusts, maintaining client communication, and coordinating with internal and external partners to deliver a superior client experience. She joined Plaza Bank and Trust Company, now Commerce Trust, in 1978. She earned her bachelor of arts degree from University of Missouri and holds the Certified Trust and Financial Advisor designation.