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# Choosing the Best College Savings Plan

Q: I'm pregnant with our first child and my parents want to start saving for the baby's college education. My dad said he'd open a Uniform Gift to Minors Act (UTMA) account, but I was thinking a 529 Plan is better. What do you suggest?

A: Congratulations on the upcoming birth of your first child — and your Dad's willingness to help save for college. There is no time like the present to start planning. Tuition at a four-year public university is on pace to cost more than $180,000 by the time your child is ready to attend, based on college inflation data from The College Board.

When trying to choose the best college savings account, you first need to understand the differences, and how each is treated on financial aid applications.

Uniform Gift to Minor (UGMA) and Uniform Transfer to Minor (UTMA) accounts enable an adult to gift financial or other assets to a minor. The UGMA account can hold bank deposits, securities such as mutual funds and insurance. A UTMA account allows almost any type of asset including real estate, said **Claudia Mott, a certified financial planner with Epona Financial Solutions in Basking Ridge**.

She said both UGMA and UTMA accounts are considered the asset of the child, even though the custodian is an adult. The annual contribution that can be made without the donor filing a gift tax return is $14,000 for 2014.

"One of the disadvantages of these accounts for college savings relates to the taxation of unearned income," she said. "Up to $1,000 of income is exempt and the second $1,000 is taxed at the child's rate, but beyond $2,000, the 'kiddie' tax applies, which is the higher of the child's or parent's rate."

And with the amount that needs to be put away for college these days, the "kiddie" tax makes the UGMA/UTMA an expensive place to save in the long run.

When it comes to calculation financial aid, the UGMAs/UTMAs are also at a disadvantage. The current federal financial aid formula will include 20 percent of the value of the asset as the child's contribution towards college costs, Mott said.

A 529 college savings plan may be a better choice and can be owned by either a child's parent or grandparent, Mott said.

"One advantage of a 529 is the tax-deferred growth on income and earnings that accrue over the child's lifetime," she said. "In addition, withdrawals for qualified education costs are free federal income tax."

If you take out the money for non-college expenses, you'd owe a 10 percent penalty and taxes on any earnings that are withdrawn.

"A major advantage of a parent-owned 529 plan is the more favorable treatment on financial aid applications," she said. "The value of the account must be included as an asset, but parents are only expected to contribute up to 5.64 percent of their assets compared to 20 percent for children's assets."

Bryan Smalley, a certified financial planner with RegentAtlantic Capital in Morristown, said a 529 is the way to go. He said your dad can open a 529 account for the benefit of your child, or you can open a 529 account for the benefit of your child and have your parents contribute.

"Who should own it really comes down to who wants to have the control that comes with account ownership, such as change the beneficiary on the account," he said.

Smalley said that even with the taxation and the financial aid implications of the UTMA, there's another reason you may want to stay away from that kind of account.

"At age 21, the child has full control of the assets in the account and may choose to use them anyway they want, which may not be on college expenses," he said. "I recommend using the 529 account to save for college and utilize a UTMA account for any other future savings for the child, such as for a first car."

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