Investing for College

IT'S NEVER TO EARLY TOO START!

The rising cost of a college education

For many of us, a child's college education is largest single expenditure in our yearly budget. College education costs are staggering, rising at levels far surpassing inflation. The cost of sending a child to a top private institution can reach $50,000 per year. Public institutions, though less pricey, can still cost over $15,000 annually.

The projected price of sending your newborn to a four-year college when he or she reaches age 18 could be in excess of $450,000 for a top, private institution and over $140,000 for a public institution. That doesn't even take graduate school into account.

Whether you are the parents of an infant or a teenager, the time to start saving for your child's education is now. Saving now will help ease the financial burden later.

Investment philosophy

No single investment philosophy fits everyone. Some believe that if you start early, you can be more aggressive in your investment choices, while others believe you should be more aggressive if you start later. Still others say that college savings funds should be invested only in a conservative, less risky manner. Whatever your philosophy, it's best to plan now to cover education costs.

Investing without the tax bite

529 tuition plans allow parents and relatives to invest in a child's college education fund using after-tax contributions that grow tax-free. A 529 plan is controlled by the person opening the account and can be a prepaid tuition plan or the more popular savings plan, with funds invested in different investment options. Funds are withdrawn income-tax-free when used for qualified education expenses; however, earnings not used for education expenses are subject to tax and a 10% penalty. A state income tax deduction may be available to residents in some states as an incentive to use that state's plan. A 529 plan allows the beneficiary to be changed and provides the ability to move from one state's plan to another.

Coverdell Education Savings Accounts, also called education IRAs, allow savings to compound and then be withdrawn tax-free if the money is used for qualified education expenses. Earnings not used for qualified education expenses are subject to tax and a 10% penalty.

What are your investment choices?

STOCKS provide more opportunity for growth, but also more exposure to loss.

CORPORATE BONDS generally provide a higher yield than savings accounts or certificates of deposit and are designed to provide a dependable income stream while protecting investment capital.

U.S. GOVERNMENT OBLIGATIONS generally have a lower rate of return than corporate bonds but are considered more secure. If bonds are sold before their maturity, they may be worth more or less than their original cost.

SAVINGS ACCOUNTS, MONEY MARKET FUNDS AND CERTIFICATES OF DEPOSIT are the safest of investments, but the lowest return and no opportunity for growth in principal.

MUTUAL FUNDS are funds that can invest in all kinds of financial assets from domestic and foreign stocks and bonds to obligations of U.S. and foreign governments. Similar to individual common stocks as far as growth, but more balanced. An investor's mutual fund strategy can be tailored to his or her risk tolerance and investment objective. Mutual fund companies will redeem outstanding shares at the current net asset value, which fluctuates with market conditions and may be worth more or less than the original cost.

How to calculate estimated four-year college costs

If you want to start saving regularly for your child's education, the following steps will help you to estimate the amount that you will need to set aside. Table 1 and 2 (opposite) will be used in making your calculations.

Step 1. Enter the number of years until your child begins college. ________

Step 2. Enter the current annual cost of the college that your child will likely attend. $________

Step 3. Enter the appropriate inflation factor from Table 1. ________

Step 4. Multiply the current annual cost by the inflation factor. This equals your child's future annual college costs. $________

Step 5. Multiply by 2 for a two-year college or by 4 for a four-year college. This equals your child's total estimated college costs. $________

Step 6. Select from Table 2 the investment factor for the return that you expect to achieve after taxes. ________

Step 7. Multiply that total estimated cost by the investment factor. This is the amount of money that you need to put aside regularly each year to fund your child's education. Divide this amount by 12 to obtain the monthly figure, and by 52 for the weekly figure.

Required Yearly Savings = $ ______________

Monthly Savings = $ ______________

Weekly Savings = $ ______________

TABLE 1

YEARS TO START COLLEGE	INFLATION FACTOR 4%	6%	8%	10%
1	1.04	1.06	1.08	1.10
2	1.08	1.12	1.17	1.21
3	1.12	1.19	1.26	1.33
4	1.17	1.26	1.36	1.45
5	1.22	1.34	1.47	1.61
6	1.27	1.42	1.59	1.77
7	1.32	1.50	1.71	1.95
8	1.37	1.59	1.85	2.14
9	1.42	1.69	2.00	2.36
10	1.48	1.79	2.16	2.59
11	1.54	1.90	2.33	2.85
12	1.60	2.01	2.52	3.14
13	1.67	2.13	2.72	3.45
14	1.73	2.26	2.94	3.80
15	1.80	2.40	3.17	4.18
16	1.87	2.54	3.43	4.59
17	1.95	2.69	3.70	5.05
18	2.03	2.85	4.00	5.56

TABLE 2

YEARS TO START COLLEGE	INVESTMENT RETURN AFTER TAXES OF 4%	6%	8%
1	.981	.971	.962
2	.481	.471	.463
3	.314	.305	.296
4	.231	.222	.213
5	.181	.172	.164
6	.148	.139	.131
7	.124	.116	.108
8	.106	.098	.090
9	.093	.085	.077
10	.082	.074	.065
11	.073	.065	.058
12	.065	.058	.051
13	.059	.051	.045
14	.054	.046	.040
15	.049	.042	.035
16	.045	.038	.032
17	.041	.034	.029
18	.038	.031	.026

Contact a D.A. Davidson financial professional for assistance setting up a college fund program.

D.A. Davidson & Co. is not a tax advisor. Before investing in any IRA, consult with your personal tax advisor about the specific tax consequences and advantages of your situation.