Financial Commentary

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Balancing Act: Contributing to Retirement While Saving for College

It's a conundrum parents face today. With retirement on the horizon, many find themselves questioning which is more important: saving for retirement or college? Both seem to have equal weight for their family's future. An MSN Money article aptly called this dilemma the "double-whammy of parenthood."[1] In addition, many parents in their 40s and 50s are also helping financially support their parents.

According to the same article, the average American needs to save up to $700,000 if they want to retire on a modest $40,000 a year.[2] Meanwhile skyrocketing tuitions at many public colleges and universities – upwards of 15 to even 30 percent[3] – have parents worried about being able to fund their child's higher education. State budget deficits of late have cut off funding for higher education. In California, for example, the University of California (UC) system estimates a 30 percent increase in tuitions for the 2010 to 2011 school year.[4]

Financial experts agree that saving for retirement is the ***number one*** priority for parents, as surprising as it sounds. Your financial strength will become the security blanket for your children's future.

I can help you determine the best money management path for both retirement and college saving. Here are some tips to help save for your nest egg and your children's education:

- **Invest in yourself.** It's important to pay yourself first by investing in your own savings and retirement plans. Start by taking a minute to refocus your 401(k) contributions. For example, does your employer offer to match a portion of your retirement contributions, and if so, are you taking advantage of it? The most common corporate matches are $.50 for every $1.00 up to the first 6 percent of pay (32 percent of plans), $1.00 for $1.00 up to the first 4 percent of pay (9.8% of plans), and $1.00 for $1.00 up to the first 3 percent of pay (8.5 percent of plans)[5]. Those with the financial means may consider contributing as much as 80 percent of their salary to meet the $16,500 contribution limit allowed by the IRS (unchanged from last year).
- **Consider a tax-advantaged college savings plan.** Peter Montoya writes that a 529 plan provides tax-advantaged growth and tax-free withdrawals, so long as the withdrawn funds are used to pay for education costs. Not all 529 plans are created equal. In fact, some of them will even provide a little cash "match" or a "start up" bonus when beginning a plan. There are also "prepaid" 529 tuition plans that offer

parents an opportunity to lock in future tuition rates at today's prices. These plans are operated by state governments and are applicable to in-state public colleges[6].

- **Discuss college expectations**. Parents need to asses their financial capabilities to send their children to a public or private university, including the assistance of financial aid and/or scholarships. Talk to your kids early on about your and their college expectations. A high-priced college diploma hanging on the wall isn't always worth the money if the child could have received an equivalent education at a less expensive school – and saved their parents pocketbooks! Make it clear in the beginning that your children are going to have to pay for part of their college expenses themselves, if that is the case for your family. Also, start looking into scholarship opportunities for your children – whether it be in sports, music or academics.
- **Keep your taxable income low.** Financial experts recommend keeping your taxable income as low as possible at the midpoint of your child's junior year of high school. This is the time when financial aid departments at colleges and universities start to assess your family's earned and received income. Montoya suggests you avoid taking capital gains or a 401(k) distribution during that year to keep your income low. Even Roth IRA contributions could raise red flags. Just don't stop contributing to your retirement savings as it's the most important means to supporting your family's ends.
- **Get kids involved in saving early.** Financial advisors have recommended that children set aside 25 percent of their part-time wage earnings for college; however, this will depend on your current financial situation. Consider setting up a bank account specifically for this purpose. Many parents report that the added benefit to this tactic is their children become more actively involved in the college-saving process, and the added responsibility has been known to improve their grades and they start to take school more seriously.
- **Avoid saving money in your child's name.** If you find yourself with extra money to save beyond what has already been set aside for retirement, do not put that money in your child's name. It may seem tempting because of minor tax benefits; however, doing so could reduce your chance of receiving financial aid. 35 percent of your child's assets are considered available for college expenses every year, versus 6 percent of yours.[7]

Please call my office today to schedule an appointment to discuss a money management strategy for retirement and college saving.

[1]MSN Money http://articles.moneycentral.msn.com/RetirementandWills/PlayingCatchUp/BalancingKidsCollegeAndRetirementSaving.aspx

[2]MSN Money http://articles.moneycentral.msn.com/RetirementandWills/PlayingCatchUp/BalancingKidsCollegeAndRetirementSaving.aspx

[3] CNN Money http://money.cnn.com/2010/02/24/news/economy/public_tuition_soars/index.htm

[4] CNN Money http://money.cnn.com/2010/02/24/news/economy/public_tuition_soars/index.htm

[5] "50th Annual Survey of Profit Sharing and 401k Plans," Published By: Profit Sharing/401k Council of America.

[6] Financial Aid.org http://www.finaid.org/savings/529plans.phtml

[7] MSN Money http://articles.moneycentral.msn.com/RetirementandWills/PlayingCatchUp/BalancingKidsCollegeAndRetirementSaving.aspx