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ANDREW HOROWITZ: This is guest host Andrew Horowitz from *The Disciplined Investor* podcast. And today on *Money Girl,* I'll be discussing how to start saving for your children's educational expenses through a tax advantaged 529 plan.

Do you ever wonder how you're going to be able to afford your child's college education? Have you looked into different savings plans? Have you been confused about what's the best choice.

Well, you're not alone. As a matter of fact, listen to Phil Rodin about this subject as he wanted to get some direction for his eight-year-old boy's college plan. Well, Phil, it's never too early to start, and you're asking an important question. Parents of youngsters worry about the same thing every day. I'm one of them.

With the rising costs of education and other expenses, it becomes more worrisome for many every single day. And it should. The College Board estimates that the average cost for college increase at double the rate of inflation. At 8%, the cost will double in nine years. And in difficult economic times, when people are just trying to put food on the table and keep a roof over their family's heads, college savings is so distant a notion it may as well be non-existent.

Luckily, there is some help in what is known as a 529 plan. The 529 plan is a tax-advantaged investment which promotes and encourages savings for higher education. This plan is often favorite over traditional methods because of its tax advantages.

There are two types of 529 plans that are usually discussed-- the prepaid plan and the savings plan. The prepaid plan makes it possible for someone to buy tuition credits at the current rate in today's dollars and save those to be used sometime in the future. These essentially eliminate the worry associated with inflation and rising costs.

The savings plan on the other hand is meant to be used as a tax-advantaged savings plan specifically designed to cover the costs associated with higher education. There are a variety of these. And it's important to understand that these usually carry investment risk and contain penalty provisions if the monies are withdrawn for other uses beyond educational purposes.

There are some of these that offer a stable value and guaranteed option, some that are risk-based, which retain the same equity-to-fixed-income ratio despite age. And then there are the age-based asset allocation plans that will automatically shift the plan assets to a more conservative posture the closer the time until college.

There is a good deal of flexibility here. The money in a 529 plan can be used for the college costs of the plan beneficiary for tuition, books, equipment, room and board, fees, and supplies at any accredited college, university, or vocational school in the United States as well as a handful of foreign universities. The only school expense which cannot be applied toward is the payment of any student loans or the interest accumulated from student loans.

There's also a way to get money out if it isn't all used for educational expenses. But there could be penalties. The money can be withdrawn by the controller of the account, which is usually the donor, but will be subject to income tax and a 10% penalty for early withdrawal.

The plan does provide for some exceptions to the general rule however. Should the beneficiary become disabled to the point that they can no longer perform a gainful activity-- in other words, work for a living-- the money can be withdrawn without penalty. Or if the beneficiary dies, the money can be passed on to another named beneficiary or back to the donor.

There are even more benefits of the 529 plan. Several states offer tax deductions to the donors for these contributions. No federal breaks, however, are available.

Secondly, and at the heart of the plan, is that the principal growth and the beneficiary's distributions are all tax exempt.

Third, the donor continues to control the account. The beneficiary has no right to touch the money. And in most cases, the donor can withdraw the cash at any time. But remember those penalties.

Other reasons to enroll in the program are, well it's easy. Unlike some college programs, there are no hoops to jump through. You don't have to do intensive research and accounting to figure out what you have and where you're at financially. You just fill out simple account forms and make a contribution. Plus, the startup deposit requirements are usually low, and everyone is eligible. And this is because there are no requirements on age or income.

However, there are some disadvantages as well. Some states charge excessive fees that nearly offset the rewards and the earnings. And should one not use all the money that there is, there is that little 10% penalty to deal with.

Also, being named as the beneficiary of a 529 plan can limit your financial aid eligibility as the account value could be counted as an asset. If you think that this may be an issue, you could always have the owner or donor of the plan be someone besides the student or a parent. Here's a tip. Naming a grandparent as the owner, for example, would be a great way to benefit the financial aid application since it won't show the student has a claim on the account.

With the cost of higher education, well, higher, you should really start thinking about plans such as the 529 to help offset the expenses of giving your children an education and a chance at a better life. I've added a few additional links on the show notes to help, like a college cost calculator. Check it out at the *Money Girl* section of qdnow.com. And for helping us with a question for this episode, Phil will be getting a copy of my audiobook, *The Disciplined Investor,* now available as an audio book at iTunes and audible.com.

Chaching! And that's all for now. Thanks for tuning into the *Money Girl.* This is Andrew Horowitz sitting in for the Money Girl. I invite you to listen to my weekly podcast, *The Disciplined Investor,* a top 10, *US News and World Report* investment podcast. It's available for free, so what are you waiting for? Download it today and start on the road to becoming a disciplined investor. Available on iTunes and the Zune Marketplace. And don't forget, there's more information and the transcript of the show notes on qdnow.com.

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