# COLLEGE FINANCING PROGRAMS

http://www.finaid.org/savings/accountownership.phtml

## Account Ownership: In Whose Name to Save?

The financial aid formulas used by the federal government and the schools assess a portion of the family's assets when computing eligibility for financial aid. Under current financial aid formulas, there are significant benefits to saving the money in the parents name, despite the (meager) tax savings of the child's lower tax bracket. Some of the more important reasons include the following:

- Child assets are assessed at a rate of 20%. (Before July 1, 2007, child assets were assessed at a rate of 35%.) Parent assets are assessed on a bracketed system, with a top rate of 5.64%. This represents a difference in financial aid eligibility equal to 14.46% of the asset. These rates are assessed on the total value of the asset, including both principal and accumulated interest. In contrast, the tax savings due to the child's lower tax bracket is typically 13%, and then only on the earnings, not on the principal.
- Many parent assets are sheltered from the need analysis process. The need analysis formulas include an asset protection allowance based on the age of the older parent which shelters a portion of the family's investments. For the typical parents of college age children (age 45), this asset protection allowance amounts to approximately $45,000. In addition, money in qualified retirement plans, such as an IRA or 401(k), is disregarded by the need analysis formulas. Also, the Federal formula (but not the formulas used by many schools) ignores the value of the family's primary residence as well as the value of small businesses owned and controlled by the family (see small business exclusion). There are no asset protection allowances for money in the child's name.
- Money in the child's name is legally the property of the child, so the child could spend it on whatever they want when the reach the age of majority. If the parents set up a trust to restrict the use of the money to educational expenses, it can negatively impact need assessments, since the full remaining value of the trust gets counted as a child asset each year.

Thus using the Uniform Gift to Minors Act to transfer money into the child's name is generally a mistake for most families. It is almost always better to save for college in the parents name.

## Financial Aid Impact of Savings Vehicles

The following table lists the current financial aid treatment of the most common savings vehicles. For the purpose of assessing the impact on financial aid eligibility, we assume that the beneficiary is the child and the account owner is the parent (except where specified otherwise). Generally speaking, if the account owner has the ability to change the beneficiary at any time, the savings are treated as an asset of the account owner, not the beneficiary.

| Savings Vehicle | Financial Aid Treatment | Comments |
|---|---|---|
| Coverdell Education Savings Account (formerly Education IRA) | asset of account owner (high impact if student owner; low impact if parent owner; high impact if owned by a third party) | If the child is the account owner, it counts as a child asset. If a parent is the account owner, it counts as a parent asset. In most cases the child is the account owner. Distributions do not affect eligibility (i.e., distributions do not count as income or a resource). (See GEN-04-02.) Custodial Coverdell ESAs owned by a student, where the student is both the account owner and beneficiary, are reported as a parent asset if the child is a dependent student and a student asset if the student is an independent student. This treatment is effective with the 2009-10 award year due to a legislative change enacted in the College Cost Reduction and Access Act of 2007. If the Coverdell ESA is owned by a grandparent or other third party, it is not reported as an asset on the FAFSA, but any distributions are reported as untaxed income to the beneficiary on the subsequent year's FAFSA. |
| Section 529 College Savings Plan | asset of account owner (low impact if owned by student or parents; high impact if owned by a third party) | Qualified distributions do not affect eligibility (i.e., qualified distributions do not count as income or a resource). Note that non-qualified distributions (i.e., distributions that are subject to federal income tax) do count as income to the distributee. Custodial 529 college savings plans owned by a student, where the student is both the account owner and beneficiary, are reported as a parent asset if the child is a dependent student and a student asset if the student is an independent student. This treatment is effective with the 2009-10 award year due to a legislative change enacted in the College Cost Reduction and Access Act of 2007. 529 college savings plans owned by a third party, such as a grandparent, are not included as assets on the FAFSA, but distributions from such a plan are reported as untaxed income to the beneficiary on the FAFSA. |
| Section 529 Prepaid Tuition Plan | asset of account owner (low impact if owned by student or parents; high impact if owned by a third party) | Since the Higher Education Reconciliation Act of 2005, prepaid tuition plans have been treated as an asset on the FAFSA, with an asset value equal to the refund value. Qualified distributions do not affect eligibility (i.e., qualified distributions do not count as income or a resource). Note that non-qualified distributions (i.e., distributions that are subject to federal income tax) do count as income to the distributee. Custodial prepaid tuition plans owned by a student, where the student is both the account owner and beneficiary, are reported as a parent asset if the child is a dependent student and a student asset if the student is an independent student. This treatment is effective with the 2009-10 award year due to a legislative change enacted in the College Cost Reduction and Access Act of 2007. 529 prepaid tuition plans owned by a third party, such as a grandparent, are not included as assets on the FAFSA, but distributions from such a plan are reported as untaxed income to the beneficiary on the FAFSA. |
| UGMA/UTMA Custodial Account | asset of beneficiary (high impact) | |
| Series I and EE Savings Bonds | asset of registered owner (low impact) | A savings bond registered in the parent's name counts as a parent asset (low impact). A bond registered in the child's name as a single or co-owner counts as a child asset (high impact). If the bond was registered in the child's name, but parent's (owner's) funds were used to purchase the bond, the parent may change the beneficiary. |
| Regular Taxable Investments | asset of account owner (low impact if owned by parent, high impact if owned by student) | |
| Variable Life Insurance | not reported on FAFSA (low impact) | Generally, the cash value of life insurance and assets in qualified retirement plans are not reported on the FAFSA. |
| Traditional IRA | asset value not reported on FAFSA (low impact) | Withdrawal will count as taxable income, affecting next year's financial aid. Current year taxpayer contributions to IRAs, SEP, SIMPLE, Keogh, 401(k), 403(b) and other retirement plans are reported as untaxed income on the FAFSA. |
| Roth IRA | asset value not reported on FAFSA (low impact) | If Roth IRA owner hasn't been invested for five years, withdrawal will count as taxable income, affecting next year's financial aid. |
| 401(k) | asset value not reported on FAFSA (low impact) | Withdrawal counts as taxable income, affecting next year's financial aid. If you borrow from the 401(k) instead of withdrawing funds, amount received does not count as income. |
| 2503(c) Minor's Trust | asset of beneficiary (high impact) | If trust restrictions prevent liquidation, trust will continue as an asset in subsequent years, continuing to hurt need-based financial aid eligibility. |