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Dispelling Myths about 529 Plans

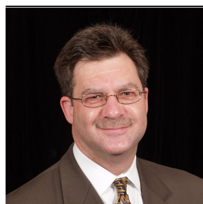
Myth 1: You have to contribute to a 529 in your home state. That statement is false with regard to 529 college-savings plans, in which money is invested in a portfolio of securities on behalf of a beneficiary. Any U.S. resident can contribute to a 529 college-savings plan in any state. Contributing to a plan offered by your home state might offer a state income tax deduction, but that shouldn't be your sole consideration. If your state's plan is poor (with high fees and poor investment options, for example) looking at plans outside your state might be worth forgoing the tax break.

Myth 2: You have to send your child to a school in the state where his 529 plan is offered. Also false. A 529 college-savings plan is fully portable, meaning that assets can be used for college expenses in any state and at some institutions abroad regardless of which state's plan holds the account.

Myth 3: You can only get a tax deduction if you contribute to your state's plan. Usually true, but not always. In fact, residents of Arizona, Kansas, Maine, Missouri, and Pennsylvania get a state income tax break on 529 contributions made to any state's plan. Elsewhere the benefit is restricted to contributions to in-state plans, with deduction limits varying from state to state and some states offering tax credits.

Myth 4: If you save in a 529 account for your child, it will hurt his financial aid prospects. Possibly, but not as much as you might think.

[Continued on page 4.]



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More about COMPASS Wealth Management, LLC

COMPASS Wealth Management, LLC is a client-focused wealth management firm dedicated to providing superior advice to individuals, families, and corporate retirement plans.

Our wealth management services include investment management, retirement and gift planning, education funding, and other advisory services.

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Retirement Contribution Limits Unchanged for the New Year

By Louis E. Conrad II, CFA

The forthcoming New Year will bring no changes to the contribution limits for most retirement accounts, such as IRAs, 401(k)s, and similar accounts. Annual contribution limits are adjusted when the annual increase in the consumer price index meets statutory thresholds. Given the current low inflationary environment, the thresholds were not met to allow for increases in 2014 contribution limits.

Employer-Sponsored Accounts

As indicated above, the amount that you may contribute to an employer-sponsored retirement account is unchanged for 2014. For 401(k), 403(b), and 457 plans, offered by corporate, non-profit, and government employers, respectively, the maximum you may contribute via payroll deduction to such plans is $17,500 annually.

If you will be 50 years of age or older by December 31, 2014, you may contribute an additional $5,500 in 2014 (also known as the “catch-up” provision), though this amount is unchanged from this year. Consequently, if you will be at least 50 years of age during 2014, you may contribute a total of $23,000 to an employer-sponsored retirement account. Contributions to your employer-sponsored retirement account, when made on a pre-tax basis, have the benefit of lowering your taxable income (and thus your taxes), as well as assisting in saving for your retirement.

For those with SIMPLE IRAs, the maximum annual contribution is also unchanged for 2014 at $12,000. The “catch-up” provision of an additional $2,500 also remains unchanged for those individuals over 50.

IRA Accounts

For Traditional and Roth IRAs, you may contribute up to $5,500 as your 2014 tax year contribution until April 15, 2015. If you will be at least 50 years old at any time during 2014, you may contribute an additional $1,000, an amount which is unchanged from this year. To qualify to make an IRA contribution, your taxable compensation must be equal to or greater than the contribution you wish to make.

In addition, to contribute to a Roth IRA, you must be income eligible. To make the full contribution to which you are otherwise entitled, your modified adjusted gross income (MAGI) during 2014 must be $114,000 or less as a single filer and $181,000 or less as a married individual, filing jointly. If your MAGI is between $114,000 and $129,000 as a single filer, or between $181,000 and $191,000 as a married individual, filing jointly, you are entitled to make a prorata contribution to a Roth and a Traditional IRA as long as your total contribution does not exceed the applicable limit.

If your MAGI exceeds the upper end of the applicable MAGI range, then you may contribute up to the allowed maximum to a Traditional IRA. You must be less than 70½ years old to contribute to a Traditional IRA.

Under current law, if you do not qualify to contribute directly to a Roth IRA because your MAGI exceeds the allowed limits, you may contribute to a Traditional IRA and then convert the contribution (and other retirement assets, if you desire) to a Roth IRA, subject to limitations and possible taxes, which are beyond the scope of this article.

One other difference between Roth and Traditional IRAs is worth noting. Contributions to a Roth IRA cannot be used as a deduction to reduce the income taxes you pay, while contributions to a Traditional IRA may or may not be used as a deduction. Whether or not a Traditional IRA contribution can be deducted is dependent on your income level and whether you or your spouse participates in an employer-sponsored retirement plan.

Monthly Market Commentary

The onslaught of positive economic news during the past couple of weeks has been relentless. Even fears of an earlier Federal Reserve reduction in bond purchases couldn't dampen spirits on Dec. 6 when a positive jobs report had everyone cheering. This and other recent numbers put a lot of fears to rest with accelerating purchasing manager data, robust auto sales, improving consumption data, better job growth, and more new-home sales. The economy appears to have gotten back what it lost this summer, and maybe there is even a slight acceleration. The data still doesn't show anything like a boom, but life is better.

GDP: GDP growth for the September quarter was revised up to 3.6% (the third-best quarter of this 17-quarter recovery) from 2.8%. It was also above the 3.1% post-World War II average and the consensus estimate of 3.2% growth.

However, almost all of the upward revision was due to a higher estimate of inventories. GDP counts production whether it is sold or whether it is still sitting on the shelves. The 0.8% increase in the estimated GDP contribution from inventory growth, combined with the original estimate of a 0.9% contribution, means that inventories added 1.7% to the GDP estimate, or almost half of the 3.6% total for the third quarter. Unless consumption, which grew at lethargic 1.4% rate, accelerates quickly, firms are likely going to need to cut production in the fourth quarter to bring inventories and sales into better alignment.

Speaking of consumption, these figures were revised downward in this week's report, which is not good news. Consumption contributed just 1.0% to GDP growth, down from 1.5% in the first quarter and 1.2% in the second quarter, hardly an encouraging sign. The services part of the economy was particularly disappointing, showing no growth in the third quarter.

Employment: The most recent employment report was consistent with slow and steady growth. 203,000 overall jobs were added in November, ahead of expectations of 180,000 jobs and the 200,000 total jobs added the previous month. The number was also surprisingly consistent with the average growth of 193,000 jobs added per month over the past 12 months. The report ranks number six out of the last 13 months and was below last November's 256,000 and February's 319,000.

Housing: New-home sales jumped a seemingly strong 25% in October compared with September. However, that was because sales in September were down sharply, and August sales figures were revised sharply downward. Sales of 444,000 homes for October were above the nine-month average of 420,000, but not by a lot. Sales in September were an embarrassing 354,000, the lowest level since early 2012. Overall, however, the seemingly great October data is a mirage, and it looks like the market for new homes isn't improving all that much. January sales of 458,000 topped the October report, as did several other reports this year. Year-over-year averaged data paints a picture of a housing market that is rapidly losing momentum.

Consumer spending: After months of sluggishness, consumer spending increased 0.3% in October. Incomes showed a small decline after months of massive increases. On a year-over-year basis, the data provides a clearer picture, with incomes improving at better pace than consumption after months of lagging behind (largely because of the payroll tax increase and the income tax increase early in the year).

Inventories: A number of industries, including autos, apparel retailers, homebuilders, and even restaurants stepped up inventories and hiring even if short-term demand didn't fully justify it based on current data. High inventories can indicate a business' confidence and its forecast of better growth in the near future, but they can also be a bad thing if they get too high and anticipated consumer demand fails to materialize.

Dispelling Myths about 529 Plans, continued

Yes, financial aid calculations generally do take into consideration 529 assets, but money in a 529 account owned by the parents or a dependent student counts far less than assets owned by the student outside a 529. In fact, non-529 student-owned assets carry more than 3 times more weight in financial aid calculations than do assets held in the parents' names. So no, 529 accounts aren't completely impact-free when it comes to financial aid, but the impact is relatively minor.

Myth 5: If your child doesn't go to college, you'll lose the money. Unused 529 money does not have to go to waste, or to the tax collector. It can be used to help pay another family member's college costs simply by changing beneficiaries or transferring funds to the family member's existing 529 account. And the list of potential recipients is rather long, including siblings, first cousins, parents, grandchildren, aunts and uncles, and even in-laws. If you do decide to cash out the plan, you'll have to pay federal and state income taxes on earnings, plus a 10% penalty (waived if the beneficiary dies, becomes disabled, or gets a scholarship).

529 plans are tax-deferred college savings vehicles. Any unqualified distribution of earnings will be subject to ordinary income tax and subject to a 10% federal penalty tax. Tax law is ever-changing and can be quite complex. It is highly recommended that you consult with a financial or tax professional with any tax-related questions or concerns. An investor should consider the investment objectives, risks, and charges and expenses associated with municipal fund securities before investing. More information about municipal fund securities is available in the issuer's official statement, and the official statement should be read carefully before investing.

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